

CFPB Maps Out “Larger Participant” Nonbank Supervision Program

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On June 23, the Consumer Financial Protection Bureau (“CFPB”) issued a notice and request for comment (“Notice”) on defining which entities should be included as “larger participants” in its nonbank supervision program.¹ Pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act (“DFA”),² the CFPB is required by July 21, 2012, to define who is a “larger participant of a market for other consumer financial products or services.”³ This provision, included within the CFPB’s nonbank supervision authority, in effect requires the CFPB to identify the markets for “other consumer financial products or services” that will be part of its nonbank supervisory program,⁴ as well as the “larger participants” of such identified markets that will be subject to the CFPB program. Pursuant to this authority, the CFPB can supervise persons/entities covered by the program, including requiring reports and conducting examinations, to monitor and oversee compliance with existing federal consumer financial law.

While the DFA specifically authorizes the CFPB to examine all nonbank mortgage companies, payday lenders, and private education lenders, its supervision of other markets providing consumer financial products and services generally must be conducted via its supervision of “larger participants” in such markets. Thus, the “larger participant” rulemaking is a critical component of the CFPB’s overall nonbank supervision program.

In preparation for the required rulemaking, the Notice seeks public comment on the following six markets the CFPB is considering including in the initial rule: (i) debt collection; (ii) consumer reporting; (iii) consumer credit and related activities; (iv) money transmitting, check cashing, and related activities; (v) prepaid cards; and (vi) debt relief services.

CFPB Identification of Markets to Include in the Initial Rule

In the Notice, the CFPB notes that a variety of consumer financial products and services offered by nonbanks could be subject to the agency’s supervision program pursuant to the “larger participant” rule. In soliciting comment on which markets should be covered in the initial rule, the CFPB is also requesting comment on whether the particular categories it proposes consist of “a single market or multiple markets, and whether other markets also should be addressed.” Among the issues in which the CFPB seeks comment in connection with its consideration of the markets it should include in the initial rule are the following:

- What consumer financial product or service markets should be included in the initial rule?
- How should the financial product or service markets included in the initial rule be defined?

- In addition to considerations relating to how to define the relevant product markets, should all markets be national in scope, or should the CFPB consider regional or other geographic markets in certain instances?
- If regional or other geographic markets should be considered, describe with specificity how they could be defined.
- What specific criteria should be measured, and threshold levels set, to define a larger participant in the markets identified above, and in any other markets that should be included in an initial rule?
- What data should be used to assess whether the thresholds have been met?

Following is the CFPB's analysis with respect to the markets it proposes in the Notice for inclusion in the initial rule.

- **Debt Collection** – The CFPB identified this market both with respect to the collection of debts related to consumer financial products or services for another entity, as well as the debt collectors own behalf following purchase of the debt from a creditor or other holder of the debt.
- **Consumer Reporting Agencies** – This market includes a range of participants engaged in consumer reporting-related activities, and includes large credit bureaus producing consumer credit reports, resellers of consumer credit information, and specialized agencies offering services such as verification of consumer check writing histories.
- **Consumer Credit and Related Activities** – Another important consumer financial market is the consumer credit market, which includes finance companies, consumer lenders, and loan servicers and brokers. This market covers products such as automobile loans and unsecured consumer installment loans. Given certain exceptions within the DFA,⁵ the CFPB notes that it will have to carefully consider how to define the respective consumer credit-related product and service segments in this market.
- **Money Transmission, Check Cashing and Related Activities** – Businesses engaged in money transmission, check cashing and related activities typically offer a menu of consumer financial products and services. These are fee-based consumer financial services that involve the delivery or receipt of money. Related activities within this market include the sale of money orders and other products and services that consumers use to pay bills or conduct other financial transactions. Given the domestic and international dollar volume of money transmission activities originated in the U.S., the CFPB has identified this activity as an important part of its nonbank supervision program. The agency is considering whether related activities, such as check cashing, should also be included within this market category for its initial rule and, if so, how to define the market category.
- **Prepaid Cards** – The prepaid card market includes general purpose reloadable open-loop payment cards, non-reloadable open loop payment cards, closed-loop gift or store cards, electronic benefits transfer cards, and payroll cards.⁶ In evaluating this market, the CFPB is considering what types of prepaid cards products should be covered by its initial rule, as well as how to define the relevant market or markets subject to the rule.

- **Debt Relief Services** – The final consumer financial market identified by the CFPB involves debt relief services, including providers of “debt management plans”⁷ and “debt settlement” entities.⁸ Defining the relevant debt relief provider market(s) is an important CFPB consideration in connection with the initial rule.

CFPB Determination of “Larger Participants” of Included Markets

In addition to requesting comment on the consumer financial product and service markets to be covered by the initial rule, the CFPB is soliciting public input on the “larger participants” within such included markets that should be subject to the CFPB’s nonbank supervisory program. Generally, the CFPB’s effort is focused on determining how to identify, and the appropriate criteria and thresholds for defining, (nonbank) larger participants in a particular market.⁹

A. Definitional Criteria and Thresholds

The CFPB notes that evaluating the size of market participants should be based on objective and measurable data,¹⁰ such as one or more of: (i) annual number of transactions in the market; (ii) annual value of transactions; (iii) annual receipts or revenue; (iv) geographic coverage; (v) asset size; and (vi) outstanding loan balances. Further, the Notice suggests that definitional thresholds for a larger participant could be based on either an absolute (e.g., dollar volume) or relative approach (e.g., percentage market share), or multiple criteria, each with its own absolute or relative threshold. Finally, the Notice discusses whether the CFPB should tailor the various criteria and thresholds to each different included market. In considering the criteria and thresholds for defining a “larger participant,” the CFPB specifically requests comment on the following:

- Should a larger participant be defined based on the relative size of the participants within a market (e.g., whether the number of annual transactions of the market participants is above the mean or median) or, alternatively, should a larger participant be defined based on an absolute threshold, such as doing business in a specified number of states?
- Should more than one criterion be used to determine the size of a market participant, such as the number of annual transactions and/or the number of states in which the participant conducts business?
- Should the same criteria and thresholds be used to define a larger participant for every market, or should different criteria and thresholds be tailored for each market based on the market’s characteristics?

B. Measurement Data

In determining the criteria to be used in evaluating a particular market a necessary consideration is whether the criteria can be measured with respect to specific market participants. As noted by the CFPB, such data could include: (i) publicly available data, including from state and federal sources; (ii) nonpublic state or federal data; (3) commercial data, including industry market analyses; and (4) data obtained directly from market participants. The CFPB is also considering the establishment of a registration program for certain covered persons under its nonbank supervision program. In considering appropriate measurement data, the CFPB request comment on the following:

- For each market, what reliable data sources are available and would be suitable for the CFPB to use in its larger participant determinations?
- What data should the CFPB collect through a registration process to use in its larger participant determinations?

C. Measurement Dates and Supervision Timeframes

A final issue addressed in the Notice is the measurement date and timeframes for evaluating the measurement data for the applicable criteria, as well as the applicable period in which a larger participant would be subject to CFPB supervision based on such criteria. For example, measurements could be based on the “immediately preceding calendar year or years, or at one or more points in time.”¹¹ With respect to the supervision timeframe, the CFPB is evaluating how long a larger participant should be subject to its supervision if, for example, it falls below the applicable threshold in a subsequent year; as well as the circumstances under which a subsequent examination should be required. In particular, the CFPB is requesting comment on the following:

- In evaluating a market participant’s size, should the CFPB measure the size of a market participant based on the relevant criteria for the previous one year, two years, or more – or at one or more than one points in time?
- Should a market participant be a larger participant if it meets the applicable threshold in any one of a specified number of prior years, or only if it meets the threshold in the most recent period?
- What factors should the CFPB consider in connection with the treatment of events such as the merger of market participants during an assessment time period?
- Are there alternative approaches for establishing an assessment time period that the CFPB should consider?
- For what length of time should a market participant be subject to supervision once it meets the applicable threshold?
- How should subsequent changes in a participant’s size be treated?

Conclusion

Pursuant to the Notice, the CFPB is seeking comment on issues that will help the agency map out its nonbank supervision program, including the entities that should be subject to CFPB oversight as “larger participants” in the portion of the program the CFPB is currently developing. In preparing for the issuance of an initial rule addressing such larger participants in the CFPB’s nonbank program, the CFPB raises a number of important considerations, including the criteria for measuring a market participant; determining the thresholds for inclusion; whether a general test or specifically tailored tests should be used for different markets; and the consumer financial markets that should be covered by the initial rule. These are important issues for purposes of the initial larger participant rule, and also have implications that bear upon much wider policies and issues in the overall formation of the CFPB’s nonbank supervision program.

Entities implicated by the Notice or that could be subject to subsequent rulemakings if/when the CFPB expands the markets included within the larger participant rule should consider this first opportunity to comment on the CFPB’s efforts to map out its nonbank supervision program. Public comments on these issues and the other questions highlighted throughout this client alert are due to the CFPB by August 15, 2011. An electronic copy of the Federal Register version of the Notice is available at: <http://www.gpo.gov/fdsys/pkg/FR-2011-06-29/pdf/2011-15984.pdf>.

If you have any questions concerning the Notice, or you are interested in working with Paul Hastings lawyers to provide comments to the CFPB on the Notice, please do not hesitate to contact any of the following:

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¹ The Notice was published in the Federal Register on June 29, 2011; see 78 Fed. Reg. 38059 (June 29, 2011).

² Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (enacted July 21, 2010).

³ DFA § 1024(a)(1)(B).

⁴ Pursuant to DFA § 1024(a), persons/entities specifically covered by the program include (i) nonbank mortgage companies, (ii) payday lenders, and (iii) private education lenders.

⁵ The DFA provisions relating to the CFPB's authority in this context includes important exceptions that carve out vehicle dealerships, retailers and merchants.

⁶ While multiple parties may be involved in offering a prepaid card product, the CFPB notice highlights that only entities exercising "substantial control" over the terms or conditions of a card would be subject to its oversight. Merchants selling or reloading a card would not be subject to CFPB oversight by virtue of that activity alone.

⁷ Typically, these are non-profit credit counseling agencies that work with creditors to renegotiate interest and/or fees to enable consumers to repay the full credit balance owed.

⁸ These entities typically negotiate with a consumer's creditor(s) to enable the consumer to settle a debt obligation via a lump-sum payment of less than the entire balance owed to the creditor(s).

⁹ Of particular note, the CFPB highlights that this determination should not be limited to the "largest" participants in each market, and at the same time should not include smaller market participants.

¹⁰ In computing the activities of a participant, the CFPB notes that the aggregate activities of nondepository "affiliated companies" of the participant should be included in the calculation.

¹¹ Also important is how to treat certain significant events, such as the merger of market participants and the timing for making a "larger participant" determination.