Alerts & Publications

California Announces Revamp of Consumer Protection Regime in Place of Sidelined CFPB

January 17, 2020

KEY CONTACTS

Elizabeth L. McKeen
Newport Beach
D: +1-949-823-7150

Pamela A. Miller
New York
D: +1-212-326-2088

Laurel Loomis Rimon
Washington, DC
D: +1-202-383-5335

Josh Ji
Newport Beach
D: +1-949-823-6995

On January 10, 2020, California Governor Gavin Newsom formally unveiled his plans to expand California's enforcement activities with respect to consumer protection laws. Although the text of the law is not yet available, Governor Newsom's proposed state budget for 2020-2021 contemplates passage of the California Consumer Financial Protection Law (CCFPL). Among other things, the CCFPL would revamp the California Department of Business Oversight (DBO) into the Department of Financial Protection and Innovation (DFPI), with a substantial increase in staff and enforcement powers.

This initiative is part of Governor Newsom's response to "the rollback of the CFPB" under the Trump administration, and it involves key players from the industry, including former CFPB Director Richard Cordray and current DBO Commissioner Manuel Alvarez, who previously worked at the CFPB as an enforcement attorney under Cordray. State-level consumer protections that go beyond federal standards, such as those contemplated by Governor Newsom, may be permitted under the Dodd-Frank Act so long as they are not inconsistent with federal laws.

Currently, the DBO regulates financial services offered by state-chartered banks and credit unions, payday lenders, auto lenders, residential mortgage lenders, money transmitters, investment advisers, and securities dealers and brokers. It has power to bring enforcement actions, which can result in the suspension, denial, or revocation of a license, as well as receivership, rescission, restitution, and penalties. For example, in December 2019, the DBO settled a three-year action against auto title lender TitleMax of California, Inc., which must deliver nearly $700,000 in refunds to more than 21,000 TitleMax customers and pay a $25,000 penalty to resolve allegations that it charged excessive interest rates and fees. Last year, the DBO pursued over 500 enforcement actions against individuals and entities located around the country.

Under Governor Newsom's proposal, the DFPI would have expanded jurisdiction to regulate "debt collectors, credit reporting agencies, and financial technology (Fintech) companies." The DFPI would also gain additional responsibilities and powers, including:

- Offering services to "empower and educate consumers," including the elderly, students, military service members, and recent immigrants;
- Licensing and examining new financial industries;
- Analyzing patterns and developments in the market to inform evidence-based policies and enforcement;
- Enforcing laws prohibiting unfair, deceptive, and abusive practices;
- Establishing a Financial Technology Innovation Office tasked with cultivating the responsible development of new consumer financial products;
- Offering legal support for the administration of the new law; and
- Expanding existing administrative and information technology staff to support the Department's increased regulatory responsibilities.

Two of these potential developments are particularly noteworthy.

First, the DFPI's expanded authority to protect against "unfair, deceptive, and abusive practices" may greatly broaden the DFPI's regulatory reach while also creating legal uncertainty. Although unfair and deceptive practices have an established history of enforcement at both the state and federal level, the "abusive" standard introduced under the Dodd-Frank Act has proven amorphous and continues to raise concerns within industry about the breadth of conduct that may be considered "abusive." Inclusion of the abusive prong, along with the broadened range of businesses and sectors over which the proposed DFPI would have jurisdiction, would make the DFPI a significantly larger enforcement presence for any company that does business, in whole or in part, in California.

Second, the creation of the Financial Technology Innovation Office (FTIO) reflects the state's desire to protect consumers, while also fostering the responsible development of new financial products. Indeed, the DBO's website acknowledges the agency's intent to "[s]pur – not stifle – innovation in financial services," bolstered by Commissioner Alvarez's experience as the former head of legal at a Fintech company, Affirm Inc. Nonetheless, Fintech companies should not assume there will be protections similar to the CFPB's regulatory sandbox (which provides avenues to shield Fintech companies from potential legal liability in the testing of new products and services that could benefit consumers), as the CFPB's Fintech sandbox has been met with opposition by a group of 22 state attorneys general, including California Attorney General Xavier Becerra. Notably, one of the first items on the agenda for the newly established FTIO, according to the DBO, will be to assess a state-level regulatory scheme for virtual currencies.

In terms of the resources needed to establish and administer the CCFPL, the proposed budget includes $10.2 million and 44 staff positions in 2020-2021, growing to $19.3 million and 90 positions ongoing in 2022-2023. The DFPI will purportedly be funded during its first three years by the reserves in the State Corporations and Financial Institution Funds, and it aims to be self-funded by licensing and settlement fees thereafter.

Legislative approval of the proposed budget is required by June 15, 2020. Although Democrats currently hold super-majorities in both legislative chambers and may be inclined to support the Governor's initiatives, substantive changes will likely be made to the proposal before California's "mini-CFPB" becomes a reality.
