UNITED STATES OF AMERICA
Before the
CONSUMER FINANCIAL PROTECTION BUREAU

ADMINISTRATIVE PROCEEDING File No. 2015-CFPB-0029 In the matter of INTEGRITY ADVANCE, LLC and JAMES R. CARNES	**ORAL ARGUMENT REQUESTED**

RESPONDENTS' OPENING APPEAL BRIEF

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Regulations

Other Authorities

ABBREVIATIONS USED IN THIS MEMORANDUM

ALJ: Administrative Law Judge Parlen L. McKenna

APA: Administrative Procedures Act

APR: Annual Percentage Rate

Bureau: Consumer Financial Protection Bureau

CFPA: Consumer Financial Protection Act of 2010.

Director: CFPB Director Richard Cordray.

FTC: Federal Trade Commission

EC: Enforcement Counsel

EC-EX-__: refers to Enforcement Counsel's hearing exhibits, by exhibit number

EFTA: Electronic Fund Transfer Act

Dkt. 28A: Respondents' Brief in Support of Motion to Dismiss Notice of Charges

Dkt. 34: Respondents' Reply Brief in Support of Motion to Dismiss Notice of Charges

Dkt. 075: Order Denying Motion to Dismiss

Dkt. 102A: Respondents' Statement of Disputed Facts In Support of Their Opposition To Enforcement Counsel's Motion for Summary Disposition, Frechette Declaration, Ex. 3, Deposition Testimony of Dr. Manoj Hastak

Dkt. 111: Order Granting In Part and Denying In Part Bureau's Motion for Summary Disposition and Denying Respondents' Motion for Summary Disposition

Dkt. 134: Enforcement Counsel's Prehearing Statement

Dkt. 163: Enforcement Counsel's Proposed Findings of Fact and Conclusions of Law

Dkt. 163B: Declaration of Robert J. Hughes

Dkt. 164: Respondents' Post-Hearing Brief

Dkt. 172: Reporter's Official Transcript of Proceedings Hearings Volume I (Public)

Dkt. 173: Reporter's Official Transcript of Proceedings Hearings Volume II (Public)

Dkt. 174: Reporter's Official Transcript of Proceedings Hearings Volume III (Public)

Dkt. 176: Recommended Decision (Public)

Dkt. 179: Respondents' Motion to Stay Appeal and Remand to Hearing Officer

Dkt. 181: Respondents' Motion for Reconsideration of Director's Denial of Motion to Stay Appeal and Remand to Hearing Officer

RD: Recommended Decision

IA: Respondent Integrity Advance, LLC

Mr. Carnes: Respondent James R. Carnes

OSBC: Delaware Office of State Bank Commissioner

SOL: Statute of Limitations

Reg. Z: Regulation Z, 12 C.F.R. § 1026 *et seq.*

RCC: Remotely created check

RX-__: Refers to Respondents' hearing exhibits, by exhibit number

TILA: Truth in Lending Act

UDAAP: Unfair, Deceptive, or Abusive Acts or Practices

INTRODUCTION

While administrative adjudication is premised on the theory that an agency's ALJs are specialized in that agency's particularized area of law, the ALJ in this matter was assigned to this case by the United States Coast Guard. The Director must reject the RD because it is factually and legally incorrect. The ALJ's conclusions of law apply the wrong legal standards and stem from flawed legal analyses in nearly every instance. His findings of fact and conclusions of law are also not supported by substantial evidence, as required under the APA. *See* 5 U.S.C. § 556(d). In fact, in many instances, the only record evidence directly contradicts the ALJ's findings. The RD cannot stand on this record.

ARGUMENT

I. LEGAL ERROR: AUTHORITY

A. The Bureau Had No CFPA Authority Over Respondents

The Bureau has no authority to pursue CFPA claims against Respondents. This is true because Respondents were never "covered persons" within the meaning of the CFPA. The ALJ misconstrues this argument and renders the wrong conclusions of law. First, he misstates the jurisdictional requirements for bringing a claim, under Sections 1031 and 1036 of the CFPA, Dkt. 176 at 29; specifically, these provisions, provide that the Bureau may take action under the CFPA only against "covered persons." 12 U.S.C. §§ 5531, 5536. Indeed, these are the provisions under which EC brought Counts 2, 3, 4, 6, and 7 of the Notice. Section 1053 of the CFPA does permit the administrative forum to hear a case brought against any "person," as the ALJ notes, but this provision does not specifically confer subject matter jurisdiction, as the ALJ incorrectly states. Second, the ALJ also incorrectly holds that the Bureau has authority to pursue its CFPA claims against Respondents, because they were "covered persons, Dkt. 176 at 28-29, Dkt. 75 at 13. Here, among other things, the ALJ's error hinges on his misreading of the CFPA.

Prior to the lawful appointment of a Director, the Secretary of the Treasury's interim authority was limited to transferred authorities "under Part F." *See* 12 U.S.C. § 5586(a). Contrary to the implications of the ALJ's incorrect reading, the FTC did not transfer any authorities to the Bureau. *Id.* § 5581(b)(5)(A). The ALJ's conclusion that "[t]he Bureau was fully authorized to enforce those [claims arising under the CFPA] against Respondents at the time it brought this proceeding," *see* Dkt. 75 at 13-14, is incorrect. In further support of the arguments that the Bureau lacks authority to pursue any claims arising under the CFPA, Respondents incorporate by reference their briefs in support of Respondents' Motion to Dismiss, Dkt. 28A and Dkt. 34.

B. The ALJ Was Not Appointed In Accordance With the Appointments Clause

As a broader matter, this proceeding, presided over by a U.S. Coast Guard ALJ, was unconstitutional because the ALJ is an "inferior Officer" within the meaning of Article II, section 2, clause 2 of the Constitution. That constitutional provision requires that "inferior Officers" be appointed by the President, the "Courts of Law," or the "Heads of Departments." The ALJ in this matter was not so appointed. Pursuant to an agreement between the Bureau and the Department of Homeland Security, the U.S. Coast Guard assigned him to the case. Thus, the administrative proceedings were unconstitutional. *See PHH Corp. v. CFPB*, No. 15-1177, 2016 WL 5898801 at *41-*42 (D.C. Cir. Oct. 11, 2016) (Randolph, Senior Circuit Judge, concurring).

II. LEGAL ERROR: DUE PROCESS

A. The Administrative Proceeding Has Violated Respondents' Due Process Rights And, This Alone, Mandates Reversal Of The ALJ's Holdings

The administrative adjudicatory process denied Respondents critical procedural protections that they would have had in federal court. Respondents' due process and equal protection rights are violated because of this denial of critical protections. As the CFPA makes clear, "the CFPB has full discretion to pursue administrative actions instead of court proceedings

and can obtain all of the same remedies through administrative actions that it can obtain in court." *Id.* at *40 (citing 12 U.S.C. §§ 5563-5564, 5565(A)(2)). Indeed, as numerous courts have noted in the context of SEC administrative forums, it is manifestly unfair that the SEC, just like the CFPB, can, at its sole discretion, determine which parties are defendants in federal court and which parties are respondents in its administrative forum. In this way, the Bureau can unilaterally determine which defendants, like Mr. Carnes and IA, are deprived of due process rights that these parties would have otherwise had in district court. *See, e.g.*, *Gupta v. SEC*, 796 F. Supp. 2d 503, 508 (S.D.N.Y. 2011) (describing the advantages of the SEC's "home turf," administrative forum, which eliminates rights accorded to defendants in federal court). In fact, in *SEC v. Citigroup Global Mkts., Inc.*, No. 11-cv-7387 34 F.Supp.3d 379, 381 n.8 (S.D.N.Y 2014), Judge Rakoff described the inherent unfairness of this choice, by noting that the SEC, which has a nearly-identical administrative regime to the CFPB, has the apparent ability to "eschew the involvement of the courts and employ its own arsenal of remedies instead," and that this represents "unchecked and unbalanced administrative power."

Here, too, the administrative forum's rules, as well as the ALJ's application of those rules, violated Respondents' due process rights. For example, the administrative forum mandates an accelerated litigation schedule, but the ALJ's own decisions failed to adhere to this schedule, requiring that Respondents litigate nearly their entire case, before the ALJ ever ruled on their Motion to Dismiss. *See, e.g.*, 12 C.F.R. § 1081.400(a). This hampered Respondents' ability to adequately prepare a defense. The administrative forum did not provide Respondents with the protections that the Federal Rules of Civil Procedure and the Federal Rules of Evidence provide to litigants. *See id.* § 1081.303(b)(4). The administrative forum also deprived Respondents of meaningful pre-trial discovery. *See id.* §§ 1081.209, 1081.210. The

administrative forum also deprived Respondents of their right to a jury trial, which they would have had in federal district court, as EC sought civil money penalties, along with equitable relief. Respondents were subjected to a profoundly unfair process that deprived them of core due process rights during the entirety of the administrative litigation and at the hearing.

B. EC's Failed to Argue Its Damages Case Until Its Post-Hearing Opposition Brief And This Substantially Prejudiced Respondents

The ALJ violated Respondents' due process rights by allowing EC to wait until after the hearing to articulate a damages theory in this matter. "It is a basic tenet of administrative law that each party to a formal adjudication must have a full and fair opportunity to litigate the issues to be decided by the agency." *See Trident Seafoods, Inc. v. NLRB*, 101 F.3d 111, 116 (D.C. Cir. 1996). The *Trident* court held that the NLRB had waived a particular argument "by failing to raise it until its post-hearing brief" because "[w]hen one party utterly fails to raise a significant issue before the ALJ, the record developed with regard to that issue will usually be inadequate to support a substantive finding in its favor and, generally speaking, neither the ALJ nor the Board should consider such an issue." *Id.* Here, too, EC waived its damages arguments.

The ALJ acknowledges that EC's "delay" in articulating its damages case "was unhelpful to the court in the damages assessment," and that EC "did not lay out a theory of damages until the final day of the hearing." Dkt. 176 at 56. But during closing argument, EC only first stated the *amount of money* it was seeking for each count, without specifying an actual theory of relief. *See* Dkt. 174 at 179:11-181:13, 183:23-184:2. It was not until *after* the hearing that EC enunciated its apparent theories of joint and several liability (of which Respondents had no prior notice), restitution, disgorgement, injunctive relief and civil money penalties. Accordingly, Respondents were left to guess in their opening post-hearing brief as to the ultimate theory that EC would argue regarding damages. Respondents were not able to cross-examine or otherwise

test the efficacy of EC's damages theory. Indeed, Respondents were not even able to respond by fully briefing these damages theories.

It is axiomatic that basic procedural due process requires that "evidence [be] subject to adversarial testing." *Strickland v. Washington*, 466 U.S. 668, 685 (1984). Moreover, under 12 C.F.R. § 1081.400(e)(1), once the hearing record is closed, an ALJ can only accept new evidence by "reopen[ing] the proceeding for the receipt of further evidence for good cause shown." The ALJ did not reopen the proceeding pursuant to Rule 400(e)(1). 12 U.S.C. § 1801.400(e)(1). Rather, the ALJ permitted EC to introduce new evidence, and relied on the July 29, 2016 Declaration from Mr. Hughes in formulating the RD. *See* Dkt. 176 at 60. The ALJ, without citing any legal standard, also rejected Respondents' due process concerns, as he argues that Respondents could have cured substantial constitutional infirmities by merely submitting additional exhibits into the post-hearing record for his review and determination alone.[1] Dkt. 176 at 57-58.

Here, EC's failures are particularly egregious, as it chose the administrative forum, and brought this case, which grew out of an investigation that started more than three years ago, during which time, EC could have – presumably – formulated a cognizable damages theory. EC, of course, bears the ultimate burden of proof. 12 C.F.R. § 1081.303(a). Nevertheless, in support of its apparent request for monetary relief, at the hearing, EC presented testimony from a data specialist, who "performs numeric analysis for Enforcement investigations." *See* EC-EX-072. Indeed, Robert J. Hughes offered no testimony about the characteristics of the data points that he had incorporated into the charts that EC proffered as proof that it was entitled to more than $100

[1] The ALJ further opined that Respondents "waited until the very last moment to turn over their datasets," which is inaccurate. Dkt. 176 at 58. EC made its data request for the first time almost three years after it began its investigation and Respondents provided EC with datasets well in advance of the hearing.

million dollars in restitution. Mr. Hughes did not testify about whether the data reflected on his charts were an accurate assessment of consumer harm. He did not testify about how that data was linked to the alleged conduct in this matter. Indeed, on direct, Mr. Hughes merely regurgitated the numbers on the data charts EC proffered as evidence. *See, e.g.*, Dkt. 173 126:3-25. Neither Mr. Hughes nor any other EC witness offered testimony to support a cognizable damages theory, or evidence that, at a minimum, linked allegedly unlawful conduct to alleged consumer harm. In short, Respondents have never had an opportunity to test, through cross-examination, the efficacy of EC's apparent damages theory. This is a due process violation, and the Director should deny EC's request for any monetary remedy, as that request has been waived by EC's failure to present any cognizable damages theory during the hearing in this matter. Here, Respondents have been substantially prejudiced and deprived of due process.

III. LEGAL ERROR: STATUTE OF LIMITATIONS

The ALJ erred as a matter of law in ruling that the SOLs that apply to causes of action brought under the CFPA, TILA, and EFTA in federal district court do not apply when those same causes of action are brought in the Bureau's administrative forum. *See* Dkt. 75 at 29. The ALJ cites the Decision of the Director, *In the Matter of PHH Corp.*, File No. 2014-CFPB-0002 (Jun. 4, 2015) in support of this conclusion. In vacating that decision, the D.C. Circuit ruled that statutes of limitations apply to causes of action arising in the Bureau's administrative forum, just as they apply in federal district court. *See CFPB v. PHH Corp.*, 2016 WL 5898801 at *40-*41. The court specifically acknowledged, through a rhetorical question, the incongruent and unfair result that would otherwise exist: "Why would Congress create such a nonsensical dichotomy between CFPB court actions and CFPB administrative actions?" *See id.* at *41. Here, the Director should apply the D.C. Circuit's holding in *CFPB v. PHH Corp.*, and find that EC's TILA and EFTA claims are time-barred and that EC's CFPA claims as to Mr. Carnes, including its UDAAP claims, are also time-

barred. This is true for all of the reasons that Respondents have previously noted in their Motions to Dismiss and Stay this Action. Dkts. 28-A, 34, 179, 181.

Specifically, the law is clear that there is a three-year SOL for any claims arising under the CFPA, including EC's UDAAP claims, which run from the date of discovery. 12 U.S.C. § 5564(g). In other contexts, courts have routinely interpreted "date of discovery" to mean "the date a plaintiff, in the exercise of reasonable diligence, discovered or should have discovered the breach or violation." *See Harris v. Koenig*, 722 F. Supp. 2d 44, 55 (D.D.C. 2010); *see also Gabelli v. SEC*, 133, S. Ct. 1216, 1220 (2013) (analyzing "date discovery" in the context of government agencies). As to Mr. Carnes, EC knew or had reason to know about his purported conduct more than three years before EC brought suit here. In addition, the only federal district court to consider the applicable SOL to TILA claims that the Bureau prosecutes, held that the agency was subject to a one-year SOL. *CFPB v. ITT Educ. Servs., Inc.*, No. 1:14-CV-00292-SEB, 2015 WL 1013508, at *32-*33 (S.D. Ind. Mar. 6, 2015). That same limiting language in TILA is in EFTA, and EC's EFTA claims are similarly time-barred. *See* 15 U.S.C. § 1693m(g).

Each of these SOL questions is a threshold issue, and their resolution would eliminate nearly all of the claims in this matter. Nonetheless, Respondents address below the numerous other legal and factual errors in the ALJ's decisions that warrant reversal.

IV. LEGAL ERROR: LIABILITY AS TO TILA

The ALJ erred as a matter of law in concluding that IA's loan agreement did not clearly and accurately disclose the terms of the loan as required under TILA and Reg. Z. *See* Dkt. 111 at 26-27. The ALJ incorrectly holds that IA customers were legally obligated, *at the time the loan was made*, to repay the loan principle, initial finance charge, *and* all possible renewal charges. *Id.* at 24-25. But the ALJ misapplies TILA, and IA's disclosures complied with TILA.

The "clear and conspicuous" requirement under TILA and Reg. Z requires specific disclosures, including a loan's APR, the finance charge, the amount financed, and a payment schedule, to be legible and in a reasonably understandable form. *See* 12 C.F.R. § 1026.17(a)(1); Cmt. 17(a)(1)-1). Further, disclosures must "reflect the terms of the legal obligation between the parties." *Id.* § 1026.17(c)(1. The Official Commentary to Reg. Z states that "[t]he disclosures should reflect the credit terms to which the parties are legally bound *at the time of giving the disclosures.*" Cmt. 1026(5)(c)-1 (emphasis added). *At the time the loan disclosures were made*, consumers only owed the "Total of Payments," *(i.e.*, the loan principle and initial finance charge). There is no evidence that an IA customer's initial legal obligation – at the moment the loan was consummated – included renewal payments. Under the Loan Agreement, consumers "[p]romise[d] to pay Integrity Advance the Total of Payments . . . on the Payment Due Date . . ." and, contingent on the consumers' choices, "[a]ll other amounts owed to us under the Loan Agreement." *See, e.g.*. EC-EX-002 at 4. The Loan Agreement also obligated the consumer to select a payment option before the Payment Due Date. *Id.* at 3. Under the Loan Agreement, when consumers did not select a payment method as required, the Loan Agreement could renew automatically. *Id.* at 4.

Contrary to the ALJ's analysis, TILA and Reg. Z are clear that the existence of a renewal option does not eliminate the fact that on the date that the loan was made, the borrowers had a legal obligation to repay the loan. The option to renew the loan was an option – and not an obligation – extended to a consumer in the event he failed to repay the loan by his next payday. Indeed, Reg. Z is clear that post-disclosure events, such as an election to renew a loan contract after consummation, do not need to appear on an initial TILA box disclosure. 12 C.F.R. § 1026.17(e).

The ALJ erred by evaluating the IA loan agreement as a "multi-payment loan," and conflates the analysis of EC's TILA/Reg. Z claims with the claims of deception. *See* Dkt. 111 at 15-24, 29-30. The Loan Agreement's TILA Box disclosure clearly displayed the total legal obligation that consumers had at the time the loan was consummated. IA did not violate TILA.

V. LEGAL AND FACTUAL ERROR: LIABILITY AS TO DECEPTION

In order to prove that an act or practice is deceptive, EC needed to establish by a preponderance of evidence each of the following elements: (1) there was a representation, omission, or practice that (2) was likely to mislead consumers acting reasonably under the circumstances, and (3) the representation, omission or practice was material. *See Steadman v. SEC*, 450 U.S. 91, 103 (1981) (applying the preponderance of the evidence standard to adjudicatory proceedings subject to the APA). The ALJ acknowledges this standard, but fails to apply it properly. *See* Dkt. 176 at 25 (internal citations omitted). Instead, the ALJ makes an unsupported legal and factual determination about who a "reasonable consumer" was; renders unsupported factual determinations regarding what that consumer would have understood; and misstates the materiality standard under deception doctrine.

A. Legal Error And Lack of Substantial Evidence: Likelihood To Mislead Consumers Acting Reasonably

First, the ALJ makes an unsupported legal determination about who a "reasonable consumer" would be, even as he acknowledges that the "reasonable person determination" is "limited to 'the relevant audience.'" *Id.* at 26 (quoting *Publishers Bus. Servs., Inc.*, 821 F. Supp. 2d 1205, 1223 (D. Nev. 2010)). Indeed, the Bureau's guidance about deception doctrine explains that "whether an act or practice is deceptive depends on how a reasonable member *of the target audience* would interpret the representation." CFPB, Supervision and Examination Manual V.2 at UDAAP 6 (Oct. 2012) (emphasis added). The ALJ expressly notes that the record lacks any

evidence about "the intelligence, education level, or income bracket of the IA's customers." *See* Dkt. 176 at 26. Nevertheless, and contrary to well-established deception doctrine, the ALJ makes an unfounded determination about the nature of a reasonable IA customer.

Second, the ALJ reaches conclusions, unsupported by the evidence in the record, regarding what his self-described reasonable IA customer would have believed about the Loan Agreement more than three years ago. EC, however, offered no survey of IA's customers, even as EC's expert, Dr. Manoj Hastak, noted, during his deposition, that "consumer data provides the best way to assess consumer, you know, take-away from materials." *See* Dkt. 102A, Ex.2 at 90:14-16. Similarly, EC proffered neither live testimony nor any sworn statements from even one IA customer. Moreover, EC entered a mere four consumer complaints into the hearing record, and these complaints were not accompanied by any sworn declarations. EC-EX-75A-D. In fact, the ALJ explained that he would "not give weight to unsworn, largely anonymous consumer complaints." *See* Dkt. 176 at 37. This dearth of complaints and related testimony is directly contrary to the circumstances in *FTC v. AMG Services, Inc*., 29 F. Supp. 3d 1338, 1362 (D. Nev. 2014), upon which the ALJ relies. In that case, the court took notice of *8,500 consumer complaints,* as well as testimony from the lender's former employees that consumers were confused by the loan terms in rendering its finding that the loan agreements were deceptive. *See id*. Here, there is no evidence in the record, let alone substantial evidence, of what a reasonable IA customer would have understood about the Loan Agreement.

The ALJ also makes other conclusions of law that have no basis in the record. For example, he concludes that "consumers were not likely to understand the full implications of allowing a loan to renew and enter auto-workout status, and even a consumer who understood that renewing a loan would incur additional costs would be unable to easily calculate how

substantial the difference would be under that option." *Id*. at 29. But there is no evidence of what a reasonable IA customer would have been likely to understand about the Loan Agreement's operation, including its renewal options. The ALJ impermissibly imposed his own views of who a reasonable IA customer was and what that customer would have believed about the Loan Agreement.

B. Legal Error And Lack Of Substantial Evidence: Materiality

It is axiomatic in deception doctrine that "[a] material representation, omission, act or practice involves information that is important to consumers and, hence, likely to affect their choice of, or conduct regarding, a product." *See Cliffdale Assocs., Inc*., 1984 WL 565319 at *37 (FTC 1984). The ALJ, however, does not apply this legal standard; rather, he inexplicably looks to the definition of "materiality" as it concerns consumer's rights of rescission in a credit transaction under TILA. Dkt. 111 at 29. He simultaneously acknowledged the problems with this analysis, noting that "[t]he broadly applicable TILA definitions found at 12 C.F.R. § 1026.2 *do not explain what constitutes a material disclosure for other purposes*." *Id.* at 29 n.10 (emphasis added). Nevertheless, the ALJ quotes the Congressional declaration on the purpose of TILA to conclude that Respondents' argument "that cost is not a material element in a *TILA deception analysis* is specious" (emphasis added). *Id*. at 30-31. The ALJ use of the term "TILA deception analysis" highlights his misapplication of the law.

And if the ALJ had applied the proper materiality analysis, he would find that there is no evidence that the cost of renewing the loan was material to even one IA customer, such that it would have likely affected that customer's choice to enter into the Loan Agreement. There is no empirical survey of payday lending customers, sworn consumer testimony, or other statement addressing what an IA customer would have considered material. Indeed, the ALJ never concludes that the cost of renewing the loan was material to IA customers. Instead, the ALJ

ignores this element of deception doctrine, and concludes that even if the costs were immaterial, "a reasonable consumer would still want an accurate disclosure of the payment schedule." *See* Dkt. 111 at 30. Here, too, the ALJ misapplies the relevant legal standard and makes findings of fact that the record does not support.

VI. LEGAL AND FACTUAL ERROR: LIABILITY AS TO UNFAIRNESS

A. Lack of Substantial Evidence: Substantial Injury

The ALJ erred in finding that Respondents engaged in unfair acts or practices as to the use of RCCs. To prove that a practice is unfair under the CFPA, EC needed to prove by a preponderance of the evidence that it: (1) causes or is likely to cause substantial injury to consumers; (2) that injury is not reasonably avoidable by consumers; and (3) such substantial injury is not outweighed by countervailing benefits to consumers or competition. *See* 12 U.S.C. § 5531(c)(1).

There is no dispute that RCCs are legal and were legal during all times IA operated. *See* Dkt. 176 at 30. As the ALJ acknowledged, EC sought to impose a strict-liability standard regarding the use of RCCs. That is to argue – by implication, if not with actual law – that every instance in which IA used an RCC was a *per se* unlawful act. EC underscored this strict liability assessment during its closing argument when it stated that it was "seeking the total amount paid by consumers after the transfer date, July 21st, 2011" for any RCC. *Id*. at 34. Then, for the first time in post-trial briefing, EC "substantially" changed its theory and instead asserted that the use of RCCs was unfair only in instances where a consumer had paid more than the "total of payments" disclosed in the TILA box and had withdrawn ACH authorization. *Id*. Respondents, of course, were deprived of the opportunity to test this damages theory, as well. But, nevertheless, the ALJ adopts EC's newly-announced theory, and asserts, without any basis for doing so, that it also "eliminate[d] Respondents' concern about situations where 'consumers could have been trying to renege on their obligation to pay.'" *Id*.

However, the ALJ's rationale ignores a crucial flaw: EC presented no evidence to support its theory that even a single consumer was harmed or likely to have been harmed by virtue of IA using RCCs, even under EC's newly-announced theory. *See, e.g., Am. Fin Servs. Ass'n v. FTC*, 767 F.2d 957, 972 (D.C. Cir. 1985) (explaining that "merely speculative harms" are not the type of injury that can be addressed through unfairness). At best, EC's theory, and the RD, rest on an unproven assumption that every consumer who withdrew ACH authorization and paid more than the "total of payments" suffered harm. Indeed, the ALJ specifically recognizes that "[w]hile the Bureau's conclusion is one logical explanation for the behavior, it is certainly not the only one." Dkt. 176 at 37, n.3; *see also* Dkt. 111 at 23 (acknowledging that "[s]ome consumers affirmatively chose the option to extend their loan due date in return for an additional finance charge … [and these] consumers got the benefit of their bargain.").

There is no evidence that amounts withdrawn by RCCs – even those amounts above the "total of payments" – were unauthorized. EC, and the ALJ, *assumed* they were unauthorized. But there were no sworn consumer complaints, no consumer testimony, no consumer survey and no other evidence that supports this supposition. *See id.* at 37. EC's witness, Joseph Baressi, who impermissibly opined (as opposed to testifying as a fact witness) about the use of RCCs generally, offered no information specific to IA. *See* Dkt. 173 at 167:15-19. EC has never met its burden of showing by a preponderance of the evidence, that amounts withdrawn above the "total of payments" via RCC were unauthorized or that the withdrawal of those amounts – via RCCs – harmed even one IA customer. There is no evidence that the use of RCCs caused substantial injury to IA customers.

B. Lack of Substantial Evidence: Reasonable Avoidability

There also is no evidence that consumer harm was not reasonably avoidable. The ALJ concludes that the Bureau did not provide "any credible, sworn testimony in support of its claim

that consumers blocked ACH access out of sheer self-preservation." Dkt. 176 at 37. Despite this clear lack of evidence, the ALJ inexplicably concludes that "the preponderance of all evidence in the record establishes harm." *Id*. The ALJ's decision appears to rest on (a) the ALJ's own interpretation of how consumers understood the Loan Agreement, and (b) the ALJ's unsupported opinion that consumers "did not believe" that they "legitimately owed" certain sums. *Id*. at 37-38. EC bears the burden of presenting credible evidence of consumer understanding and consumer action. *See* 12 C.F.R. § 1081.303(a). That burden was not met here and EC's unfairness claim fails.[2]

VII. LEGAL ERROR: LIABILITY AS TO EFTA

The ALJ errs as a matter of law in concluding that IA violated EFTA. In reaching that conclusion, the ALJ incorrectly finds that the IA loan agreement conditioned the extension of credit on repayment by recurring electronic funds transfer. Dkt. 111 at 32. The record shows contrary facts. In authorizing ACH, consumers indicated that they "[a]greed that [they] could repay [their] indebtedness through other means . . . ." EC-EX-002, at 9. And the ALJ correctly notes that "[c]onsumers were also permitted to make payment by alternate means, such as cashier's check or money order, by timely mailing payment to IA." *Id*. at 19. The record evidence shows that IA allowed loan repayment by non-electronic means; thus, IA could not have violated EFTA's

[2] The RD also reflects a misapplication of public policy, stemming from EC's improper efforts to cast a patina of fraud around IA's use of RCCs. During trial, EC repeatedly attempted to insinuate that IA acted unfairly because the mere use of RCC's suggests fraud, despite their legality. *See* Dkt. 164 at 13. Fraud was not at issue in this matter. Yet by finding that EC did not present anything more than several unsworn, anonymous consumer complaints and nonetheless concluding that "the preponderance of all the evidence in the record establishes harm," the ALJ implicitly elevates public policy considerations above and beyond the weight of the record evidence. Dkt. 176 at 37-38. Indeed, the ALJ makes clear that he is concerned about consumers who were "caught in a cycle of debt and saw no other option than to take out multiple loans." *Id*. at 28. The broader public policy questions relating to payday lending and the propriety of RCCs as a payment mechanism cannot, as a matter of law, outweigh the dearth of evidence presented by EC and, thus, cannot justify a conclusion that runs counter to the actual evidence in the record.

prohibition on conditioning the extension of credit on repayment by preauthorized electronic funds transfers. 12 U.S.C. § 1693(k)(1).

The ALJ further errs in finding that "[a] reasonable consumer reading the Payment Options section of the contract would conclude that ACH debits were a required method of payment." *Id.* at 36. First, this is not the standard under EFTA. Further, this finding presupposes that consumers would not also review the ACH authorization, which expressly stated that "[y]ou may repay your indebtedness through other means, including by providing timely payment via cashier's check or money order . . . ." *See* EC-EX-002 at 10. Here, too, neither the facts in the record nor the actual law support a holding that IA is liable for violations of the EFTA.

VIII. LEGAL AND FACTUAL ERROR: INDIVIDUAL LIABILITY

The ALJ errs in holding that Mr. Carnes was individually liable for deceptive and unfair acts. Indeed, EC's pretrial statement clearly noted that the salient question as to Mr. Carnes's liability concerned the question of whether he knew or had reason to know "how Integrity Advance's loan product operated and how that did not align with the company's loan agreement disclosures." *See* Dkt. 134 at 5. EC, however, offered no evidence that shows that Mr. Carnes knew or should have known of the misrepresentations argued to exist in IA's loan agreements. Rather than hold EC to its burden, the ALJ invents a new legal standard and then makes findings of fact that record evidence contradicts.

A. Legal Error: Individual Liability Standard

1. The ALJ Ignores The Relevant Caselaw

The ALJ errs by announcing a standard for individual liability that ignores two relevant CFPA cases in which individual liability was examined, *CFPB v. Gordon*, 819 F.3d 1179, 1197 (9th Cir. 2016) and *CFPB v. CashCall, Inc.*, No. CV157522, 2016 WL 4820635 (C.D. Cal. Aug, 31, 2016). Under these cases, an individual, who is found to be a related person, may be liable for

deception if "(1) he participated directly in the deceptive acts or had the authority to control them [*i.e.*, "control"] and (2) he had knowledge *of the misrepresentations*, was recklessly indifferent to the truth or falsity of the misrepresentation, or was aware of a high probability of fraud along with an intentional avoidance of the truth [*i.e.*, "requisite knowledge"]." *Gordon*, 819 F.3d at 1193 (emphasis added).

However, both of these cases also illustrate that, with regard to requisite knowledge, individual liability can only be found when a defendant has direct knowledge of a misrepresentation, or a clear and specific warning of the same. *Gordon*, 819 F.3d at 1197 (defendant reviewed, edited, modified and approved marketing material and scripts for deceptive mortgage relief schemes and stated in a business plan that he would "assure all advertising is legal"); *see also CashCall*, 2016 WL 4820635 at *15 (defendant expressly approved a legal arrangement designed to evade state and federal usury laws and "frequently discussed the status of ongoing lawsuits" regarding loan products with counsel).

The record is clear that Mr. Carnes did not know, and had no reason to know that consumers may not have understood IA's loan agreements. Over the course of IA's five years of lending, a third of its customers were repeat borrowers, with that number growing substantially with each passing year. *See* RX-021 (showing repeat IA customers relative to all customers).

2. The ALJ Applies The Wrong Requisite Knowledge Standard

The standard for finding that a related person has requisite knowledge is "whether a person knew or should have known that a consumer was likely to be misled." Dkt. 176 at 43. The ALJ, however, holds incorrectly that the knowledge requirement may be satisfied through a showing of an individual's "involvement with the company" such that the individual "knew or should have known that certain practices were unfair or deceptive." *Id*. at 44. Mere

"involvement in the company" is not legally sufficient to hold an individual, even a CEO, personally liable for the representations or conduct of a company. Nevertheless, the ALJ relies on Mr. Carnes's general knowledge of how the business operated as evidence that Mr. Carnes is individually liable. The ALJ, for example, points to the fact that "Mr. Carnes actively reviewed numerous metrics related to Integrity Advance's business throughout the company's time in operation." Dkt. 176 at 53. But these "metrics" were presumably the data points available through the TranDotCom and IA dashboards described by EC's witness, Timothy Madsen. Those data points concern lead conversion and certain aspects of the loan process; they have nothing to do with the Loan Agreement, its disclosures or what IA customers understood about the loan or the Loan Agreement. *See* Dkt. 172 at 45:13-46:13. Indeed, to the extent EC's hearing witnesses knew about Mr. Carnes's involvement with IA, their testimony show that Mr. Carnes's had no knowledge about the Loan Agreement's disclosures and whether consumers would have been misled by that language.

The ALJ also states incorrectly that because Mr. Carnes was "actively involved" and the "driving force behind the [HIP] companies and the controlling shareholder," he faces a "heavy burden of exculpation." Dkt. 176 at 51 (citing *Standard Educators, Inc. v. FTC*, 475 F.2d 401, 403 (D.C. Cir. 1973)). In *Standard Educators*, however, the individual defendant "devised the form contract used by the company's salesmen, a contract whose provisions were an integral part of the deceptive scheme" and that "[t]he pattern of deception was facilitated by the contract written by [the defendant]." 475 F.2d at 402. Here, EC never even *alleged* – much less proved – such involvement by Mr. Carnes. Indeed, Mr. Carnes testified that he did not substantively review or approve IA's loan agreement, Dkt. 172 at 231:23-232:3. He also testified that he did not write, edit, or revise IA's loan agreement template or any version of the agreement. Dkt. 173

at 75:11-25, 76:1-13; *see also* Dkt. 172 at 228:25-229:6. There is no contrary evidence in the record.

Indeed, the ALJ points to no cases or facts that support his version of the requisite knowledge standard. For example, the ALJ cites cases that involve individual defendants, who unlike Mr. Carnes, had knowledge of or reason to know about allegedly deceptive conduct. For example, in *FTC v. Network Servs. Depot*, Inc., 617 F.3d 1127 (9th Cir. 2010), the court held that defendants were recklessly indifferent "[i]n the face of numerous warning signs—multiple customer complaints, admitted delays, . . . suspicious financial practices, and . . . false statements." *Id*. at 1141.

Also inapposite to the facts here, the court in *FTC v. Grant Connect, LLC*, No. 2:09-CV-01349-PMP-RJ, 2009 WL 3074346, at *10 (D. Nev. Sept. 22, 2009), on which the ALJ also relies, held that the two individual defendants were liable for having engaged in deceptive acts or practices because they received clear and specific warnings about the company's fraudulent conduct. The court in *Grant Connect* found that several different sources, including internal emails, warned the individual defendants that the company's advertisements were misleading. *Id.* at *10. The defendants also knew that the company was incurring fines for its high chargeback rates. *Id*. Here, there is no evidence that Mr. Carnes received specific warnings about misrepresentations in IA's loan agreement, either from internal or external sources. The low number of complaints and the high rate of returning customers, *see* RX-021, provided indications to the contrary.[3] Notwithstanding this, the ALJ takes substantial liberties in

[3] The ALJ erroneously concludes from *FTC v. Five-Star Auto Club, Inc.*, 97 F. Supp. 2d 502, 539 (S.D.N.Y. 2000) that "[a] very low level of involvement in the corporation satisfied the knowledge test . . . ." Dkt. 176 at 46. Again, *none* that the ALJ cites support his legal conclusion. In *Five-Star*, the relevant defendant communicated with law enforcement on behalf of the company about the company's alleged misconduct. 97 F. Supp. 2d at 538. In *FTC v.*

presupposing that Mr. Carnes was – in fact – aware of facts that would have alerted him to potential consumer misunderstanding about the operation of the loan.[4]

The RD also relies on other inapposite cases, which further underscore why Mr. Carnes is not liable here. In *FTC v. Bay Area Bus. Council, Inc.*, 423 F.3d 627, 638 (7th Cir. 2005), "the individual defendants were aware of the 'near-constant stream of complaints.'" Dkt. 176 at 43-44. In each of these other cases, courts found an individual liable when they found that the individual defendants were (or should have been) alerted to possible deception or unfairness. *See FTC v. Lanier Law, LLC*, No. 3:14-CV-786-J-34PDB, 2016 WL 3632371, at *30 (M.D. Fla. July 7, 2016) (one defendant was frequently copied on emails discussing how to respond to complaints and investigations, and the other defendant was "kept up-to-date" on written and oral complaints from consumers, as well as complaints from the BBB and governmental agencies); *FTC v. NHS Sys., Inc.*, 936 F. Supp. 2d 520, 535 (E.D. Pa. 2013) (individual defendant sent

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Direct Mktg. Concepts, Inc., the individual defendant managed the advertising of an entire business line and the record showed that the defendant knew that the company did not have support to back up its claims. *See* 569 F. Supp. 2d 285, 309 (D. Mass. 2008), *aff'd*, 624 F.3d 1 (1st Cir. 2010).

[4] The ALJ's impression notwithstanding, there is no contradiction between Mr. Carnes's answer at the hearing that he was not personally aware of complaints from IA borrowers and his response during his investigative hearing that he was generally aware of a type of complaint, but gave it no credence. Mr. Carnes answered truthfully the precise questions he was asked. At the hearing, EC asked "[w]ere there any complaints that you received about IA's loan product?" *See id*. at 50 (emphasis added). Mr. Carnes responded that "Complaints never rose to my level, so I don't know." *Id*. EC then asked "[s]o you were unaware personally of any complaints?" *Id*. Mr. Carnes responded "I wasn't aware of complaints." *Id.* This testimony is consistent with Mr. Carnes's statements at his investigative interview, where he noted that he was aware that certain types of complaints were "out there" or that a complaint "came out," but he did not personally receive or handle complaints. *See id*. at 50 (citing EC-EX-068 at 243:6-244:5; 244:9-11). Nonetheless, the ALJ concluded that "even though Mr. Carnes was not responsible for reviewing and responding to individual complaints, he was generally aware that such complaints existed." *Id.* (emphasis added). However, EC did not ask whether Mr. Carnes was "generally aware that such complaints existed." Mr. Carnes was asked if he received any complaints or if he was made aware personally of any complaints. As Mr. Carnes explained, he did not personally receive or review consumer complaints.

emails demonstrating her receipt of complaints, and accompanying consumer refunds; and another supervised and controlled the call centers); *FTC v. Wilcox*, 926 F. Supp. 1091, 1104 (S.D. Fla 1995) (defendants saw thousands of consumer complaints showing that their solicitations had misled the consumers).

There is no evidence in the record that Mr. Carnes had requisite knowledge about any misrepresentation, even applying the ALJ's incorrect legal standard. Indeed, the ALJ renders an unsupported conclusion that Mr. Carnes knew that IA's loan agreement "would have a tendency to mislead consumers," Dkt. 176 at 53. But the evidence in the record requires a different conclusion. The representations at issue in the case are mandated and defined by regulation. In other words, there would need to be evidence that Mr. Carnes understood the regulatory-mandated language requirements or that he disregarded clear warnings that the disclosures failed to comply with the law. The record shows that Mr. Carnes did not have this knowledge. First, as Edward Foster, IA's former general counsel, testified, "no one at the Hayfield group of companies, including myself or Mr. Carnes, were consumer lawyers or experts in consumer law," and that "[a]ll agreements were written by outside counsel." Dkt. 173 at 26:20-25, 27:1, 27:5-6. Mr. Carnes also testified that IA "hired outside counsel to create . . . loan documents that conformed with Delaware and federal law." *Id*. at 95:10-13.

Further, outside counsel and regulators regularly reviewed the loan agreement to ensure its compliance with relevant laws. Indeed, Mr. Foster also testified at that "the company's outside counsel reviewed the agreement of IA on a regular basis as did the Delaware Banking Commission through its annual licensing process and the exams Integrity Advance received all reviewed the agreement." Dkt. 173 at 38:10-15. IA was properly licensed throughout its active existence. *See* RX-008 – RX-013 (documenting IA's Delaware licensure and renewal). Such

ongoing licensure requires compliance with Delaware law – including Delaware's provision allowing for renewals of short-term loans, *see* Dkt. 174 at 134:22-135:7; 137:24-138:7, and necessarily involves oversight and review by the OSBC – including reviews of the loan agreements. Specifically, Elizabeth Quinn Miller, Senior Investigator for the OSBC testified that the lending licensure process involves a review of the applicant's loan agreement – including the TILA box. *Id.* at 127:1-19. She also indicated that during the years that IA had a lending license with the state of Delaware, she personally looked at lenders' loan agreements before those lenders were allowed to obtain a license. *Id.* at 118:18-120:5; 126:12-128:6. She explained lenders' loan agreements were likely reviewed on a regular basis during the State's supervisory examination process and that she had no reason to doubt that IA was treated any differently. *Id.* at 132:19-20.

The ALJ acknowledges that Mr. Carnes "knew Integrity Advance had satisfied all the requirements for licensure by the State of Delaware," Dkt. 176 at 42, but fails to apply this finding to his analysis of individual liability. IA's compliance with Delaware requirements, along with the Company's high rate of returning customers, extremely low rate of complaints (of which Mr. Carnes was not personally aware) all indicate the Mr. Carnes had no knowledge, or reason to know that there could have been a misrepresentation in the Loan Agreement about the operation of the loan.

EC failed to meet its burden, but the ALJ ignores the record. In fact, the ALJ's findings and conclusions in the RD betray a fundamental interest in fairly deciding this matter by employing a preponderance of the evidence standard. For example, the ALJ baselessly states that "[t]he record as a whole establishes that Mr. Carnes was primarily interested in his companies' profitability." *Id.* at 54. Notwithstanding that this is directly contradicted by

evidence entered by EC, *see, e.g.*, Dkt. 172 at 177:6-178:11,[5] it is irrelevant as to the question of Mr. Carnes liability. There is no evidence in the record that Mr. Carnes had the requisite knowledge of the misrepresentation so as to be held personally liable.

As with his analysis of deception, the ALJ attempts to hold Mr. Carnes individually liable for IA's alleged unfairness based solely on Mr. Carnes' general understanding of IA's business. Dkt. 176 at 56. The ALJ finds that Mr. Carnes knew that IA used RCCs and, generally, when RCCs may have been used. *See id.* The ALJ also found that "Mr. Carnes observed RCCs being printed in the Kansas City office . . . ." *Id.* However, there is no evidence that Mr. Carnes knew or had reason to know about allegedly unfair conduct.

IX. LEGAL AND FACTUAL ERROR: RELIEF

A. Legal Error: Equitable Monetary Relief

The ALJ applies the wrong legal standard in determining the amount of equitable monetary relief, as he does not engage in the well-established burden-shifting framework. Specifically, the Bureau had the initial burden of putting forward sufficient evidence to "reasonably approximate" equitable monetary damages that would go back to consumers, which EC has never done. Under the proper burden-shifting framework, the "government [first] 'bears the burden of proving that the amount it seeks in restitution reasonably approximates the defendant's unjust gains. . . . If the government makes this threshold showing, the burden shifts to the defendant to demonstrate that the net revenues figure overstates the defendant's unjust gains." *See Gordon*, 819 F.3d at 1195; *see also FTC v. Bronson Partners*, 654 F.3d 359, 368-69 (2d Cir. 2011); *FTC v. Febre*, 128 F.3d 530, 535 (7th Cir. 1997); *FTC v. Kuykendall*, 371 F.3d 745, 766 (10th Cir. 2004). Courts have held that while defendants' gross receipts "is a proper

[5] Describing an e-mail indicating that Mr. Carnes' response upon the discovering of fraud by a call center employee was to ensure that IA "take care of the customers . . ." and "refund any fees and bank charges" the customers incurred. *Id.* (citing EC-EX-87).

baseline," in calculating unjust gains, "[a] baseline is only the beginning, however. To accurately calculate *actual loss*, the defendants must be allowed to put forth evidence showing that certain amounts should offset the sanctions assessed against them." *See Kuykendall*, 371 F.3d at 766. An example of such an offset, said the *Kuykendall* court: "the defendants might be able to show that some customers received full refunds of their payments or that others were wholly satisfied with their purchases and thus suffered no damages." *Id*. The Ninth Circuit similarly vacated a damages calculation based on net revenue, holding that the court may, in determining appropriate damages, consider "a customer who renewed subscriptions *necessarily knew* the actual terms of the transaction at the time of the renewal." *Pub. Bus. Servs. Inc.*, 540 F. App'x at 558.

Specifically, in failing to exclude any repeat customers from the restitution calculus, the ALJ fails to distinguish between the separate determinations of liability and damages. The ALJ declines to exclude returning customers because he perceives "the proper test for deceptive conduct is not whether an actual consumer was deceived, but rather whether the act or practice had the potential to deceive." Dkt. 176 at 69 (citing *FTC v. Johnson*, 96 F. Supp. 3d 1110, 1119 (D. Nev. 2015)). But the test of deceptive conduct is not the same as the test for measuring damages. *On its face*, the standard articulated in *Johnson*, and as the ALJ applies it here, is not a restitution *damages* calculus, but a standard to determine the binary question of whether a defendant is *liable* for deception in the first instance. Another case that the ALJ cites acknowledges this distinction. In acknowledging that "[t]he existence of some satisfied customers does not constitute a defense under the FTCA," the court in *FTC v. Amy Travel Serv. Inc.*, 875 F.2d 564, 572 (7th Cir. 1989) found that "[t]he magistrate *correctly acknowledged the existence of satisfied customers in computing the amount of defendants' liability* – customers

who actually took vacation trips were excluded when the magistrate computed the amount of restitution awarded." In other words, liability is a different question than a determination of the quantum of damages. While the existence of satisfied customers may arguably not constitute a defense to liability, it surely does constitute evidence that such customers should be excluded from a restitution damages calculus because they were not harmed.

Here, customers who were aware of the terms of the transaction – such as customers who returned to IA for second, third and even tenth loans – could not reasonably be said to have been injured by IA's loan agreements. However, the ALJ instead finds that *all* amounts collected above the "total of payments" for *all* loans made after the transfer date was a "reasonable approximation," and discounted evidence presented by Respondents of consumers who were not harmed by virtue of returning to IA multiple times for additional loans. Dkt. 176 at 69. It is axiomatic that any equitable monetary relief must reflect *only* actual injury *to consumers*. *See* 540 F. App'x at 558. Respondents presented substantial evidence regarding repeat customers, *see* Dkt. 164 at 28-31, evidence which belies any notion that *all* consumers should be included in any restitution calculus. The ALJ's holding to the contrary is, thus, based on unsupported and demonstrably erroneous assumptions about the extent of consumer injury, and should be reversed.

B. Legal Error and Lack of Substantial Evidence: Mitigating Factors

The ALJ does not properly consider all of the mitigating factors under 12 U.S.C. §5565(c)(3). While expressly acknowledging that he "***must*** consider" each of these mitigating factors, the ALJ barely even considers two of these factors. *See* Dkt. 176 at 73 (emphasis added). At that, the ALJ short-changes factor (c), as he does little more than note the number of loans that IA made. As to factor (a), the ALJ expressly acknowledges that there is no evidence in the record regarding Mr. Carnes's current financial resources and that IA "has virtually no

financial resources." *See id*. As to Mr. Carnes's "good faith," the ALJ makes the conclusory and baseless assertion that Mr. Carnes was "clearly aware of the predatory nature of payday loans," but there is no evidence in the record to substantiate this statement. *Id.*

Furthermore, the ALJ alleges that Mr. Carnes was "not fully candid with the court," presumably a reference to the ALJ's allegation earlier in the RD that Mr. Carnes's testimony was "inherently incredible." *See id.* at 51, 73. However, as discussed above, Mr. Carnes answered truthfully the precise question he was asked. *See supra* note 4.

Finally, the ALJ makes the wholly unsupported assertion that Respondents' demonstrated compliance with Delaware state law reflected that "Respondents had the resources and acumen to exploit" a "loophole in Delaware state law" that "permitted IA to repeatedly renew its loans without affirmative action on consumers' part to stop them . . . ." Dkt. 176 at 73-74. There is no evidence in the record that any such "loophole" existed. To the contrary, Ms. Miller testified that, since 2002, Delaware law has allowed for any short-term consumer loan to be rolled over four times. *See* Dkt. 174 at 134:22-135:7; 137:24-138:7; 146:15-147:18. Further, IA's compliance with Delaware statute is well-supported by the record evidence demonstrating that its lending license was renewed during each year it made loans to consumers. *See* Dkt. 173 at 38:10-15 (testimony of Edward Foster); *see also* RX-008 – RX-013 (documenting IA's Delaware licensure and renewals). Indeed, the ALJ acknowledges that Respondents complied with Delaware state law. *See* Dkt. 176 at 25. Nonetheless, the ALJ now uses Respondents' *compliance* with Delaware state law as a basis for awarding civil money penalties against them.

C. Legal Error And Lack Of Substantial Evidence: *Sua Sponte* Injunction

The ALJ's award of injunctive relief ignores the appropriate legal standard. In evaluating EC's request, "[u]nless the statute authorizing injunctive relief modifies the standard, the Court reviews a request for permanent injunctive relief under 'well-established principles of equity.'"

CFPB v. Siringoringo, No. 14-01155, 2016 WL 102435 at *5 (C.D. Cal. 2016) (quoting *eBay, Inc. v. MercExchange, L.L.C.*, 547 U.S. 388, 391 (2006)). Accordingly, "[t]o obtain a permanent injunction, EC had to demonstrate: (1) that it has suffered an irreparable injury; (2) that remedies available at law, such as monetary damages, are inadequate to compensate for that injury; (3) that, considering the balance of hardships between the plaintiff and defendant, a remedy in equity is warranted; and (4) that the public interest would not be disserved by a permanent injunction." *Id.*

The ALJ addresses none of these factors, finds that the Bureau's request to enjoin Respondents from future violations of any Federal consumer financial protection laws is "unenforceable," and instead renders a *sua sponte* injunction that bars Respondents from "engaging in payday lending operations" for 15 years. Dkt. 176 at 77. Despite acknowledging that an "injunction must be narrowly tailored to remedy only the specific harms that the Bureau has proved," the ALJ offers no explanation for how this *sua sponte* injunction is tied to any evidence in the record. *See id*. at 75. Instead, the ALJ merely states that he is following the Director's reasoning in *In the Matter of PHH Corp.* "in recommending the same length of time." *Id*. at 77. As an initial matter, the D.C. Circuit vacated this decision. *See PHH Corp. v. CFPB,* 2016 WL 5898801 at *41. Further, the specific facts supporting the 15-year injunction in *PHH* are distinguishable from this case. First, and most importantly, IA is no longer an operating business. The ALJ noted that, in *PHH*, the Director found that "a cognizable danger of future violations existed where the company could easily resume its once-profitable business." Dkt. 176 at 75 (citing *PHH*, File No. 2014-CFPB-0002 at *32-*33. Here, there is no evidence in the record demonstrating – or even suggesting – that the Respondents are likely to engage in future violations.

Moreover, in *PHH*, the Director stated that the 15-year bar was appropriate "[g]iven the nature and breadth of PHH's violations of Section 8 [of RESPA] in this case, as well as the [5-year] time frame over which they extended . . . ." *See PHH*, File No. 2014-CFPB-0002 at *33. By contrast, RESPA is not at issue in this case and the ALJ has found violations that span less than two years. *Id.* at 35-36. Finally, PHH was enjoined from "entering into any captive reinsurance agreements" which was "reasonably tailored to PHH's conduct." *Id.* at 32. Conversely, Respondents are overbroadly (and vaguely) banned from "engaging in payday lending operations." *See* Dkt. 176 at 77. It is unclear what specific activities this restriction includes, and it goes far beyond the realm of Respondents' purported liability, which pertains specifically to the Loan Agreement.

If the ALJ had applied the appropriate legal standard, he would have found that there is no support for any injunctive relief in this matter. The restrictions against Respondents are overbroad and insufficiently specific, and it is unclear what corresponding benefit consumers and the public would obtain from this proposed *sua sponte* injunction.

CONCLUSION

For all of the foregoing reasons, the Director should reverse the decisions of the ALJ and find in favor of Respondents.

Respectfully submitted,

Dated: November 4, 2016

By: /s/ Allyson B. Baker

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CERTIFICATION OF SERVICE

I hereby certify that on the 4th day of November, 2016, I caused a copy of the foregoing Respondents' Opening Appeal Brief to be filed by electronic transmission (e-mail) with the CFPB's Office of Administrative Adjudication (CFPB_Electronic_Filings@cfpb.gov). A copy of this brief is provided by electronic mail to U.S. Coast Guard Hearing Docket Clerk (aljdocketcenter@uscg.mil), Heather L. MacClintock (Heather.L.MacClintock@uscg.mil), and Administrative Law Judge Parlen L. McKenna (cindy.j.melendres@uscg.mil), and served by electronic mail on the following parties who have consented to electronic service:

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