UNITED STATES OF AMERICA
Before the
CONSUMER FINANCIAL PROTECTION BUREAU

ADMINISTRATIVE PROCEEDING
File No. 2015-CFPB-0029

In the Matter of:	)	**RESPONDENTS' SUPPLEMENTAL BRIEF IN SUPPORT OF THEIR MOTION TO OPEN RECORD FOR A NEW HEARING**
INTEGRITY ADVANCE, LLC and JAMES R. CARNES,	)	
Respondents.	)	

RESPONDENTS' SUPPLEMENTAL BRIEF IN SUPPORT OF THEIR MOTION TO OPEN RECORD FOR A NEW HEARING

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

CASES

STATUTES

OTHER AUTHORITIES

I. INTRODUCTION AND SUMMARY

Pursuant to Administrative Law Judge ("ALJ") Christine L. Kirby's March 13, 2020 Order, Respondents Integrity Advance, LLC and James R. Carnes ("Respondents") respectfully submit this Supplemental Brief in support of their Motion to Open Record for a New Hearing.

As explained in Respondents' August 14, 2019 Brief in support of their Motion to Open Record for a New Hearing ("Respondents' First Brief"), it is appropriate to open the record for a new hearing for several reasons. First, a "new hearing and recommended decision in accordance with the Bureau's Rules of Practice for Adjudication Proceedings [the "CFPB Rules"]" was expressly ordered by Director Kathleen L. Kraninger, consistent with the Supreme Court's ruling in *Lucia v. SEC*, 138 S. Ct. 2044, 2055 (2018). Second, the ALJ must make credibility determinations if she is to find for the CFPB and recommend the imposition of restitution and the other financial sanctions that the CFPB is seeking, all of which necessarily requires observing live witness testimony. Third, in the first proceeding, certain material testimony and evidence was never presented in a live hearing because the ALJ improperly granted summary disposition on multiple claims. Finally, the law has developed on the critical issues of advice of counsel/good faith and restitution, so additional evidence is now highly relevant.

II. BACKGROUND

On May 29, 2019, Director Kraninger remanded this matter to ALJ Kirby for a "new hearing and recommended decision in accordance with the Bureau's Rules of Practice for Adjudication Proceedings." Dkt. 216 at 2, 9. In part due to significant legal developments in the time since the prior proceedings occurred, on August 14, 2019, Respondents filed a Motion to Open Record for a New Hearing in which Respondents argued, inter alia, that further discovery

was needed on the statute of limitations issue. *See* Dkt. 229A at 7-8. By Order dated October 28, 2019, the ALJ denied further discovery and ordered briefing on the merits of the threshold statute of limitations issue. Dkt. 238. Following briefing and oral argument on the statute of limitations issue, the ALJ denied Respondents' Motion to Dismiss/and or for Summary Disposition on Grounds Limited to October 28, 2019 Order, and directed that the parties file a Joint Proposed Schedule for further proceedings by February 6, 2020. Dkt. 249. The parties conferred but were unable to agree, so each party offered its own proposed schedule. Dkt. 250.

By Order dated February 7, 2020, the ALJ directed that the parties brief the issues of whether the CFPB is unconstitutional because it violates separation of powers principles and whether further proceedings should be stayed pending the outcome of *Seila Law*. Dkt. 251. After briefing, the ALJ denied Respondents' Motion to Dismiss on separation of powers grounds and Motion to Stay Proceedings by Order dated March 13, 2020. The ALJ further directed Respondents to file, as relevant here, their Supplemental Brief in support of their Motion to Open Record for a New Hearing.

III. LEGAL STANDARD

The appropriate remedy for an adjudication tainted by an Appointments Clause violation is a "new hearing before a properly appointed official." *Lucia*, 138 S. Ct. 2044 at 2055 (internal citations omitted). Here, the CFPB Director ordered a "new hearing and recommended decision in accordance with" the CFPB Rules. Dkt. 216 at 2. The CFPB Rules provide for, among other things, live witness testimony at a hearing before an Administrative Law Judge. *See* 12 CFR §1081.303(g)(2) ("A party is entitled to present its case or defense by sworn oral testimony and documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as, in the discretion of the hearing officer, may be required for a full and true disclosure of the facts.").

IV. ARGUMENT

A. A new hearing is required by the Supreme Court's Ruling in *Lucia v. SEC* and the CFPB Director's Order

The CFPB Director specifically ordered a "new hearing and recommended decision in accordance with" the CFPB Rules. Dkt. 216 at 2. This necessarily includes the ability to question witnesses at a live hearing before the properly-appointed ALJ.[1] 12 CFR §1081.303(g)(2). The CFPB Director's order is consistent with the Supreme Court's recent decision in *Lucia*, in which the Supreme Court held that the appropriate remedy for an adjudication tainted by an Appointments Clause violation is a "new hearing before a properly appointed official." *Lucia*, 138 S. Ct. at 2055. To the degree that the 2015 D.C. Circuit Court opinion in *Intercollegiate* stands for the proposition that a mere *de novo* record review is a sufficient remedy after an Appointments Clause violation, it should be deemed overruled by *Lucia*. *See Intercollegiate Broad Sys., Inc. v. Copyright Royalty Bd.*, 796 F.3d 111 (D.C. Cir. 2015); *cf. Lucia*, 138 S. Ct. at 2055 ("To cure the constitutional error, another ALJ (or the Commission itself) must hold the new hearing to which Luca is entitled.")

However, even if *Intercollegiate* is still good law, the circumstances in this matter call for, and due process considerations require, a new hearing. Under the court's reasoning in *Intercollegiate*, a de novo record review may be appropriate where the parties have not identified (1) any determination that "turned on witness credibility" nor (2) any relevant evidence that is not on the record. *See Intercollegiate*, 796 F.3d at 116 (the parties "fail[ed] . . . to point to any instance of an exclusion of relevant evidence that affected the outcome . . . or to any portion of

[1] Consistent with the CFPB Rules, Respondents reserve the right to seek summary disposition regarding claims in the Notice of Charges and recognize that Enforcement Counsel may also move for summary disposition. *See* 12 CFR §1081.212. However, to the extent that this matter is not resolved by way of summary disposition, the parties should be provided the opportunity to present live testimony and cross-examine witnesses.

the Final Determination that turned on witness credibility.") It is clear that a new hearing is warranted here where key issues turn on witness credibility, and the written record does not contain all of the relevant evidence.

B. <u>A new hearing is needed to assess witness credibility.</u>

As explained in Respondents' First Brief, the ALJ must be afforded the opportunity to hear live testimony from the witnesses and judge credibility for herself. *See Anderson v. Bessemer* City, 470 U.S. 564, 575 (1985) ("[O]nly the trial judge can be aware of the variations in demeanor and tone of voice that bear so heavily on the listener's understanding of and belief in what is said."). Further, the ALJ cannot make factual findings based on a paper review of the existing record as the prior ALJ explicitly relied upon credibility determinations to make his factual findings. Under these circumstances, a new hearing with live testimony is appropriate even under the court's analysis in *Intercollegiate*. *Id.* at 126 (finding that a paper record review was reasonable where the determination did not turn on witness credibility).

The prior ALJ explained that he made factual findings after judging witness credibility based on a number of "traditional factors" including "the demeanor of the witness." Dkt. 176 at 12-13. In doing so, the ALJ accepted the testimony of some witnesses, but found certain portions of testimony from other witnesses not credible. This is evident in the fact that the ALJ "accepted and incorporated" every fact finding proposed by Enforcement Counsel, most of which relied on live witness testimony.[2] Dkt. 176, App'x B. The ALJ also "accepted and incorporated" fact findings proposed by Respondents that relied on the testimony of witnesses such as Bruce Andonian and Timothy Madsen, thus finding their testimony to be credible. Dkt.

[2] For one proposed finding, the ALJ "accepted and incorporated as modified herein." Dkt. 176, App'x B at 90-91, ¶ 15. All others were accepted as written.

.

176, App'x D at 109-111. At the same time, the ALJ rejected as not credible some of Respondents' proposed fact findings that were based on portions of testimony from Respondent Carnes and Edward Foster, legal counsel for Integrity Advance. Dkt. 176 App'x D at 112, ¶ 33; 112-113, ¶ 35; 116, ¶ 32; 117, ¶68; 120, ¶ 98. Therefore, consistent with his role as fact-finder, the ALJ made credibility determinations regarding all of the witnesses. As a result, the current ALJ cannot rely on the transcript of the testimony of any of the witnesses in the first hearing. Instead, the ALJ must conduct a new hearing with live testimony, consistent with the CFPB Rules, so that she can hear and judge the credibility of all of the witnesses for herself. Only then can she make credibility determinations about Mr. Carnes and all of the other witnesses.

1. *James Carnes*

The need to make appropriate credibility assessments is most evident as it pertains to the testimony of Mr. Carnes. The prior ALJ wrongly rejected key portions of Mr. Carnes' testimony based on credibility determinations. *See* Dkt. 176 at 52 ("Mr. Carnes also testified that outside counsel drafted Integrity Advance's loan agreement and he did not change, edit, or meaningfully review the substance of the agreement. However, I do not find it credible that he was unfamiliar with the terms of the agreement."); Dkt. 176 at 54 ("I have thoroughly considered Mr. Carnes' testimony about his role at Integrity Advance and do not find it fully credible. . ."). Indeed, the prior ALJ had to disbelieve Mr. Carnes' testimony in order to find him personally liable, as Mr. Carnes' testimony negated necessary elements of the claims.

To hold an individual liable, the CFPB has to prove that the individual (1) participated directly in the allegedly deceptive acts or had the authority to control those acts, and (2) had knowledge of the alleged misrepresentations, was recklessly indifferent to the truth or falsity of the alleged misrepresentations, or was aware of a high probability of the alleged fraud along with an intentional avoidance of the truth. *See CFPB v. Gordon*, 819 F.3d 1179, 1193 (9th

Cir. 2016). But, at the prior hearing, Mr. Carnes testified that he relied upon outside counsel to draft the loan agreement and to ensure it complied with the law. Hr'g Tr. I-231:23 – I-232:3.

Further, Respondents proposed the following factual findings, based on Mr. Carnes' testimony:

> Mr. Carnes did not discuss the loan agreement template with its drafters (legal counsel from an outside law firm) or Integrity Advance personnel. Id. at I-227:10-12. Mr. Carnes testified that he did not recall Integrity Advance's in-house counsel, Mr. Foster, ever explaining Integrity Advance's loan agreement to him. Id. at I-231:11-12. Mr. Carnes did not recall specific conversations with Integrity Advance personnel about the loan agreement. Id. at I-232:14-17.

But the prior ALJ "rejected as incredible" this proposed finding. Dkt. 176, App'x D at 112, ¶33.

Respondents further asserted:

> Moreover, Mr. Carnes testified that consumer complaints did not rise to the level of his personal attention and awareness.

But the prior ALJ "rejected as not credible and contradicted by other evidence in the record." *Id.* at 120, ¶98.

Because Mr. Carnes' testimony disproves his personal liability, Enforcement Counsel requested that the prior ALJ disregard that testimony as not credible. For example, Enforcement Counsel stated:

> At trial, Carnes and Foster would not clearly state who decided to implement Integrity Advance's deceptive loan agreement . . . Based on all of the evidence and the credibility of the witness' testimony, the ALJ can find that Carnes approved the use of the deceptive loan agreement.

Dkt. 162 at 11. Enforcement Counsel further urged the prior ALJ:

> While Carnes tried to distance himself from this decision (testifying that he "possibly" saw a loan agreement template at some point in 2008) the Administrative Law Judge should find Carnes's testimony on this topic not credible and reject it.

Id. at 17.

It is clear that, in order to find Mr. Carnes personally liable, which he is not, the ALJ would have to reject portions of his testimony. The ALJ must conduct a live hearing in which she can evaluate Mr. Carnes for herself.

2. *Edward Foster*

In addition to making credibility determinations about Mr. Carnes, Enforcement Counsel requested, and the prior ALJ made, adverse credibility determinations regarding Edward Foster. For example, in their post-trial briefing, Enforcement Counsel called Mr. Foster's testimony into question:

> At trial, Carnes and Foster would not clearly state who decided to implement Integrity Advance's deceptive loan agreement . . . Based on all of the evidence and the credibility of the witness' testimony, the ALJ can find that Carnes approved the use of the deceptive loan agreement.

Dkt. 162 at 11. The ALJ wrongly rejected the "substance" of Mr. Foster's testimony that "the vast majority of that, what the [Integrity Advance loan] product looked like and how it functioned was defined by Delaware law." Dkt. 176, App'x D at 117, ¶ 68. Further, the ALJ "rejected as contradictory to the weight of the evidence" Mr. Foster's testimony that "repayment issues were 'handled specifically by the call centers on a day-to-day basis." Dkt. 176, App'x D at 118-119, ¶ 83.

It also is apparent that the prior ALJ wrongly made adverse credibility determinations about Mr. Foster's testimony due to his invocation of the attorney-client privilege, even though it is undisputed that Mr. Foster was legal counsel for Integrity Advance. For example, during Mr. Foster's questioning by Enforcement Counsel about who approved the loan agreement, Mr. Foster invoked the attorney-client privilege. Tr. II 44:12-17. In response, the ALJ stated "He's not going to answer it, so let's move on. There is a thing called adverse inference." Tr. II 45:1-3.

At this new hearing, the ALJ must assess Mr. Foster's credibility through live testimony. Additionally, as described in Section IV.C.1 below, Respondents intend to show that restitution is not appropriate in this case, given Respondents' good faith reliance on the advice of their counsel, consistent with developments in the law that have occurred since the first proceeding. Therefore, Respondents will now waive attorney-client privilege as to any advice that was given regarding the contents of the loan agreement during the relevant time period. As a result, both parties will have questions for Mr. Foster that he previously declined to answer due to his ethical obligations under the attorney-client privilege.

3. *Delaware Office of the State Bank Commissioner: Elizabeth Quinn Miller*

Elizabeth Quinn Miller, representative of the Delaware Office of the State Bank Commissioner ("the Delaware Bank Commissioner"), also provided testimony in the prior proceeding. Hr'g Tr. III-116 – III-153. Ms. Miller's testimony was relied upon by the prior ALJ and evidently found credible. Dkt. 176 at 19-20. The ALJ expressly relied on portions of Ms. Miller's testimony, such as finding that "Ms. Miller looked at agreements to make sure the TILA disclosures were presented in the correct format" but her team does "not specifically approve the contract" and, other than APR, does not conduct any mathematical calculations. Dkt. 176 at 19-20, ¶¶92, 94-96. However, the ALJ did not appear to rely on other portions of Ms. Miller's testimony such as the fact that she reviews loan agreements for compliance with Delaware law. Hr'g Tr. III-127:2-14. This is critical because Delaware law has requirements that are directly relevant to the claims in this matter, such as requiring that loan applications disclose in writing that "[a]dditional fees may accrue if the loan is rolled over." 5 Del. C. §2235A(b)(2).[3] The ALJ should have the opportunity to hear live testimony from a representative of the Delaware Bank

[3] While this code section has been revised over time, this requirement has been in effect since 2002. 2002 Del. ALS 398 (July 9, 2002).

Commissioner[4] to understand the full context of the approval process, so that she can assess Respondents' good faith reliance on the repeated approvals by the Delaware Bank Commissioner. In the first proceeding, Enforcement Counsel argued that "any such reliance [on Delaware regulators] would go to Carnes's intent, which is not relevant to his liability." Dkt. 168 at 12. However, as discussed in more detail in section IV.C.1 below, the law has since developed regarding the relevance of intent on the decision to award restitution. Therefore, this testimony is highly relevant, and the ALJ should have an opportunity to hear from, and evaluate the testimony of, a representative of the Delaware Bank Commissioner.

4. *Damages Testimony: Robert Hughes and Dr. Xiaoling Ang*

The prior ALJ considered the live testimony of the CFPB's damages witness, Robert Hughes, and the Respondents' damages witness, Dr. Xiaoling Ang. Hr'g Tr. II-110 – II-163; III-4 – III-46; IIII-64 – III-106; III-154 – III-166. In his decision, the ALJ concluded that Mr. Hughes' damages calculation methodology was "more reasonable" than that of Dr. Ang. Dkt. 176 at 60. The current ALJ also may have to make decisions regarding potentially conflicting damages calculations in the current proceeding. This will require the ALJ to assess the "reasonableness" of the calculations and analysis, which will rely in part on the credibility of the witnesses. Therefore, Respondents should be permitted to put on live witness testimony regarding the calculation of damages. Additionally, as discussed in section IV.C.2 below, Respondents will seek testimony on damages, consistent with developing law.

5. *Joseph Baressi*

In the first proceeding, Enforcement Counsel presented the testimony of CFPB employee Joseph Baressi to explain how remotely-created checks ("RCCs") work. Hr'g Tr. II-

[4] Sadly, Ms. Miller has passed away since the first proceeding. Accordingly, Respondents intend to subpoena another representative of the Office.

165 – II-194. However, Mr. Baressi's testimony went much further, providing prejudicial and impermissible opinion testimony regarding what a consumer would understand regarding RCCs. Respondents objected to this testimony during the first hearing as well as afterwards in a motion to strike. Dkt. 153. For the reasons stated in the motion to strike, Enforcement Counsel should not be permitted to present Mr. Baressi's testimony in this proceeding. However, to the degree the ALJ relies upon or considers Mr. Baressi's testimony, she should only do so after hearing his live testimony and judging the credibility and quality of that testimony for herself.

6. *Bruce Andonian; Timothy Madsen*

In the first proceeding, Enforcement Counsel also presented testimony from former Integrity Advance employees Bruce Andonian and Timothy Madsen. Hr'g Tr. I-27 – I-90. The former ALJ accepted and relied upon that testimony, therefore finding it credible. Dkt. 176 at 18-19, ¶¶67-86. The current ALJ should also have the opportunity to the hear this testimony, before accepting it or ruling on its credibility.

C. A new hearing is needed to supplement the record on issues where the prior ALJ granted summary disposition

In the first proceeding, the former ALJ granted summary disposition in favor of the CFPB as to Integrity Advance's liability for Count I (TILA); Count II (CFPA derivative of TILA); Count III (CFPA – Deception); Count V (EFTA); and Count VI (CFPA derivative of EFTA). Dkt. 111. In his ruling, the ALJ found that Integrity Advance offered a multi-payment loan and that the loan agreement was deceptive on its face.[5] Dkt. 111 at 18, 31. Further, the

[5] The prior ALJ found this despite the fact that the loan agreements included all material terms, including the fees for a loan repaid in a single payment (as scheduled by the agreement) and the fees incurred should the loan be renewed. In fact, the TILA box in the loan agreement contained the explanation: "Your Payment Schedule will be: One (1) payment of $[amount] due on [date] (Payment Due Date)." *See* Dkt. 111 at 20. In rejecting Respondents' argument that this demonstrates a single-pay obligation, as well as clearly-defined loan terms, the prior ALJ referenced an alternative version of the loan agreement that did not include this explanatory

ALJ found that the loan agreements were conditioned on consumers' repayment by electronic fund transfer, even though the loan agreement explicitly stated that consumers could repay by other means, and there was evidence that customers received loans without signing the ACH authorization. Dkt. 111 at 35, 38-39.

The ALJ also granted the CFPB's Motion in Limine to Preclude Evidence Disputing Issues Decided and Facts Established at Summary Disposition. Dkt. 141. Therefore, Respondents have never had the opportunity to present live testimony or cross-examine CFPB witnesses on these issues. Respondents should be permitted to do so now, in a live hearing in accordance with the CFPB Rules.

D. A new hearing is needed to present testimony that has become relevant due to changes in the law

1. Relevance of Respondents' good faith and reliance on advice of counsel.

If the ALJ finds Respondents liable on any of the charges in the Notice, the ALJ must then address the question of whether restitution is an appropriate remedy. The prior ALJ previously addressed this issue, but, as he noted, "only one circuit ha[d] ruled on the proper scope of restitution under the CFPA" at the time. Dkt. 176 at 61 (referencing *CFPB v. Gordon*, 819 F.3d 1179, 1195 (9th Cir. 2016)). The *Gordon* decision did not recognize the relevance of advice of counsel/good faith to the appropriateness of restitution in a CFPA matter, so Respondents had an insufficient basis to present such evidence at the prior hearing. In the time since the prior ALJ's decision, however, there have been at least two additional cases that have further defined the proper scope of restitution under the CFPA, both of which reflect that restitution is not an appropriate remedy in a CFPA case where the CFPB does not establish

language in the TILA box. *Id.* However, Enforcement Counsel put on no evidence to show how many customers received the alternative version of the loan agreement. Dkt. 88 at 2-3, ¶13 (stating that Integrity Advance "generated all of its contracts" with one or the other agreement).

fraudulent intent. *See CFPB v. CashCall, Inc.*, 2018 U.S. Dist. LEXIS 9057, at *39-41 (C.D. Cal. Jan. 19, 2018); *CFPB v. Nationwide Biweekly Admin., Inc.*, No. 15-cv-02106-RS, 2017 U.S. Dist. LEXIS 145923, at *27-31 (N.D. Cal. Sep. 8, 2017). Respondents should be permitted to present additional evidence in light of these developments in the law, particularly where such evidence can have a significant impact on the financial penalties that can be imposed in this case.

In *CashCall*, the district court addressed the question of whether restitution was an appropriate remedy in a case in which the defendants were found liable for offering loans to consumers that were void and unenforceable under various state usury and licensing laws. *See* 2018 U.S. Dist. LEXIS 9057, at *36. The court concluded that restitution was not an appropriate remedy because the CFPB failed to prove by a preponderance of the evidence "that Defendants intended to defraud consumers or that consumers did not receive the benefit of their bargain" from the loan program at issue in that case. *Id.* at *36-37. In addition to concluding that the CFPB failed to show any evidence of fraudulent intent, *id.* at *39, the court further concluded that evidence of the defendants' reliance on advice of counsel weighed against an order of restitution. *See id.* at *39-41 (finding that defendants "only agreed to participate in the Western Sky Loan Program after consulting with prominent legal counsel and receiving advice that the structure of the Western Sky Loan Program was not unlawful" and that defendants reasonably relied on that advice); *see also id.* at *40 (recognizing that "advice of counsel is. . . relevant to the determination of whether restitution is an appropriate remedy") (citing *Chase v. Trs. of W. Conference of Teamsters Pension Tr. Fund*, 753 F.2d 744, 753 (9th Cir. 1985)). The court further concluded that restitution was inappropriate because "the evidence indicated quite clearly that consumers received the benefit of their bargain." *Id.* at *42.

Similarly, in *Nationwide Biweekly Admin., Inc.*, the court addressed whether restitution was appropriate in a case in which defendants were found liable for misleading consumers about a program to assist consumers in minimizing interest paid on their mortgages. 2017 U.S. Dist. LEXIS 145923, at *4-7. The court determined that restitution was not an appropriate remedy because the CFPB failed to show "that defendants engaged in the type of fraud commonly connoted by the well-worn phrase 'snake oil salesmen'" or that "the [interest minimizer program] never provides a benefit to consumers, or that no fully-informed consumer would ever elect to pay to participate in the program." *Id.* at *28-29.

Respondents should be permitted to present additional evidence at a new hearing in light of these recent developments in the law. For example, at the prior hearing, Integrity Advance's legal counsel, Mr. Foster, did not testify as to certain matters on the basis of the attorney-client privilege. *See* Dkt. 176 at 49-50 (invoking attorney-client privilege in response to question about whether he discussed consumer complaints with Mr. Carnes). Since the state of the law has now changed, Respondents now seek to recall Mr. Foster to explore additional avenues of testimony related to advice of counsel/good faith. Additionally, Respondents will present testimony from Integrity Advance's outside counsel, Claudia Callaway (the same lawyer who provided legal advice to the defendants in the *CashCall* case) relating to legal advice regarding the loan agreement.[6] Respondents also will present evidence from a representative of the Delaware Bank Commissioner relating to Respondents' good faith reliance on the state regulator to support their belief that they were not engaging in unlawful conduct.

[6] Mr. Carnes has previously testified that he did not personally speak to outside counsel regarding the loan agreement template. Hr'g Tr. I-227:10-12. However, he relied on his experienced outside counsel to draft a loan agreement that complied with the relevant law. *See* Hr'g Tr. I-226:20 – I-227:9. Further, Ms. Calloway provided advice to the company, Integrity Advance. *See* Hr'g Tr. II-26:20 – II-27:6.

In short, since the previous hearing, the law has evolved such that it is now clear that evidence of advice of counsel/good faith is highly relevant to the determination of restitution in CFPA matters. In light of that development in the law, and in particular where the CFPB is seeking restitution in the range of roughly $40-$132 million, Respondents should be permitted to present additional evidence that would demonstrate why restitution is an inappropriate remedy in this matter.

2. Calculation of restitution.

As demonstrated above, restitution is not an appropriate remedy in this case because Enforcement Counsel cannot show that Respondents acted with the requisite bad intent or that consumers did not receive the benefit of their bargain. However, should the ALJ reach the stage of calculating restitution damages, she will need to first determine whether Enforcement Counsel's evidence "reasonably approximates the defendant's unjust gains." *CFPB v. Gordon*, 819 F.3d 1179, 1195 (9th Cir. 2016); *see also CashCall*, 2018 U.S. Dist. LEXIS 9057, at *43. The burden then shifts to Respondents to show that this amount overstates any "unjust gains." *Gordon*, 819 F.3d at 1195; *CashCall*, 2018 U.S. Dist. LEXIS 9057, at *43.

In calculating "unjust gains," courts typically consider the harm to the consumer though not the "full amount lost by consumers." *FTC v. Verity Int'l, Ltd.*, 443 F.3d 48, 67 (2d Cir. 2006) (district court should "entertain only ***reasonable*** approximations of the defendants' [] unjust gains, rather than their overall gains"). Additionally, "unjust gains" can be calculated as "net revenues." *CashCall*, 2018 U.S. Dist. LEXIS 9057, at *44.

The law has continued to develop regarding the calculation of "unjust gains" in CFPA matters since the first proceeding. In particular, in 2018, the district court in *CashCall* discussed at length the appropriate standard for imposing and calculating restitution in CFPB enforcement actions. *Id.* at 35-45. That court has now made clear that adjudicators should

consider whether the damages calculation has been "netted for expenses" in determining whether the CFPB's approximation is reasonable. *Id.* at 44 (finding that the CFPB did not meet its burden of establishing a reasonable approximation of "net revenues" where its witness "admitted on cross-examination that he did not believe the CFPB's proposed restitution amount was netted to account for expenses.") The court's decision in *CashCall* is consistent with the aim of restitution, which is remedial rather than punitive in nature.

The record in this case is silent on Respondents' expenses. Therefore, Respondents should have the opportunity put on evidence regarding their expenses that should be taken into account in any restitution calculation.

V. CONCLUSION

For the foregoing reasons as well as the reasons articulated in Respondents' First Brief, Respondents respectfully request that the ALJ grant their Motion to Open Record for a New Hearing.

Respectfully submitted,

/s/ Richard J. Zack
Richard J. Zack, Esq.
zackr@pepperlaw.com
215.981.4726

Michael A. Schwartz, Esq.
215.981.4494
schwarma@pepperlaw.com

Christen M. Tuttle, Esq.
tuttlec@pepperlaw.com
215.981.4285

Saverio S. Romeo, Esq.
romeos@pepperlaw.com
215.981.4440

PEPPER HAMILTON LLP
3000 Two Logan Square
Eighteenth & Arch Streets
Philadelphia, PA 19103-2799

Counsel for Respondents Integrity Advance LLC and James R. Carnes

Dated: March 26, 2020

CERTIFICATE OF SERVICE

I hereby certify that on the 26th day of March 2020, I caused a copy of the foregoing Respondents' Supplemental Brief in support of Motion to Open Record for a New Hearing to be filed by electronic transmission (email) with the Office of Administrative Adjudication (CFPB_electronic_filings@cfpb.gov), and served by email on opposing counsel at the following addresses:

Stephen Jacques, Esq.
Stephen.Jacques@cfpb.gov

Benjamin Clark, Esq.
Benjamin.Clark@cfpb.gov

Alusheyi Wheeler, Esq.
Alusheyi.Wheeler@cfpb.gov

Deborah Morris, Esq.
Deborah.Morris@cfpb.gov

/s/ Saverio S. Romeo
Saverio S. Romeo, Esq.