UNITED STATES OF AMERICA
Before the
CONSUMER FINANCIAL PROTECTION BUREAU

ADMINISTRATIVE PROCEEDING
File No. 2015-CFPB-0029

In the Matter of:	)	**RESPONDENTS' REPLY BRIEF IN SUPPORT OF THEIR MOTION FOR SUMMARY DISPOSITION**
INTEGRITY ADVANCE, LLC and JAMES R. CARNES,	)	
Respondents.	)	

RESPONDENTS' REPLY BRIEF IN SUPPORT OF THEIR MOTION FOR SUMMARY DISPOSITION

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page(s)

CASES

STATUTES

OTHER AUTHORITIES

The Consumer Financial Protection Bureau ("CFPB") has failed to identify any genuine dispute as to the material facts supporting the Motion for Summary Disposition of Respondents Integrity Advance, LLC and James R. Carnes ("Respondents") (Dkt. 272).

First, the CFPB cannot dispute that approximately half of Integrity Advance's customers repaid their loans and then returned to take out additional loans from the same company under the same terms. In light of this fact alone, it is clear that *reasonable* consumers understood Integrity Advance's Loan Agreement and were not misled or harmed by it. *Second*, the CFPB misstates the plain language of the Loan Agreement–claiming that the Agreement does not disclose costs, but relying solely on one section of the Loan Agreement (the "TILA box"). That reading ignores the full Loan Agreement terms, which clearly and conspicuously disclose (both in content and form) recipients' obligations, as well as what happens if those obligations are not met. *Third*, the CFPB has agreed that loan products, such as the one offered by Respondents, provide consumers with access to credit that they would not otherwise have–a significant benefit that outweighs the nonexistent harm in this case. *Fourth*, the CFPB cannot establish a genuine factual dispute to show that Mr. Carnes knew that the Loan Agreement terms were deceptive or unfair. *Finally*, even if there was a material factual dispute regarding liability, restitution is not appropriate because the CFPB has not shown that Respondents intended to defraud customers or that customers did not receive the benefit of their bargain.

Summary disposition should be granted in favor of Respondents.

I. Reasonable consumers understood the Loan Agreement and were not harmed.

The CFPB contends that Respondents "have provided no evidence that consumers understood their loan terms with Integrity Advance." Opp'n at 10. That is wrong. Respondents did provide (strong, undisputed) evidence that reasonable consumers understood the terms of

their loans and were not harmed.[1] *See, e.g.*, Dkt. 272 at 12-13 (noting that of the 82,980 loans originated on or after July 21, 2011, 66% of those loans were loans to repeat customers, with more than 6,527 of those customers choosing to take out five or more loans, and 926 of those customers choosing to take out ten or more loans). Far from being "irrelevant," Opp'n at 11, the undisputed evidence of repeat customers is highly probative and demonstrates that 48% of Integrity Advance's customers (for loans originated on or after July 21, 2011) took out more than one loan from the company under the same terms and conditions that the CFPB claims were deceptive and unfair. *See* Dkt. 274A (Ex. 15 to Zack Decl.) at 803. The fact that such a large number of Integrity Advance's customers took out more than one loan is fatal to the CFPB's case because it shows that *reasonable* consumers understood the terms of the Loan Agreement. *See CFPB v. Weltman, Weinberg & Reis Co.*, 2018 U.S. Dist. LEXIS 124630, at *6 n.1 (N.D. Ohio July 25, 2018) (the CFPB must show that a "reasonable consumer" was likely to be misled, not merely that the "least sophisticated consumer" would be misled).

The CFPB's attempt to sidestep this undisputed evidence is unavailing. Its claim that the existence of repeat customers does not show that they understood the loan terms and that "[b]eing a repeat customer is not evidence of customer satisfaction" defies common sense. Opp'n at 11, 31. Further, its reliance on *FTC v. AMG Capital Mgmt., LLC*, 910 F.3d 417 (9th Cir. 2018) is unavailing. In that case, defendants had not shown that "repeat borrowers across loan portfolios knew they were dealing with the same enterprise," so customers would not necessarily know they were accepting the same loan terms from the same company. *Id.* at 425.

[1] Even if Respondents had not come forward with any evidence, they could still demonstrate their entitlement to summary disposition by showing that Enforcement Counsel—the party with the burden of proof in this proceeding—has failed to provide sufficient evidence to succeed on its claims. *See* Dkt. 272 at 7-8 (citing cases). Respondents have done so here. *See, e.g.*, *id.* at 14 (noting that the CFPB has not conducted any consumer surveys or sought to present any consumer testimony to support its claims).

That is not the case here, where Integrity Advance offered a single loan product, using one of only two nearly identical Loan Agreement forms throughout the time at issue. *See* Dkt. 277 ("EC Facts") ¶¶ 5, 58-59. The reliance on *FTC v. Nat'l Urological Grp., Inc.*, 645 F. Supp. 2d 1167, 1213 (N.D. Ga. 2008) also is misplaced, as that court addressed false advertising for a weight loss product. In that circumstance, it is logical that consumers may have continued to rely on false advertising to repeatedly purchase the product, even where the consumer did not experience the purported benefits of the product. *Id.* That is not the case for Integrity Advance's repeat customers, who experienced the loan repayment process firsthand before taking out another loan. *See* Dkt. 273 ("Resp'ts' Facts") ¶¶ 48-49.

Notably, the CFPB has not even attempted to provide an alternative justification for why a consumer (acting reasonably) would have taken out multiple loans from a company that was taking more money from the consumer than he or she expected. And, the CFPB does not explain how a customer could be confused about the loan terms on the second, third, fourth, or fifth time that he or she took out a loan. Its inability to do so only underscores Respondents' entitlement to summary disposition. The high rate of repeat customers shows that *reasonable* consumers understood the terms of the Loan Agreement and, certainly, that once a customer returned to take out another loan, he or she was well informed of the loan terms.[2]

The CFPB's attempt to rely on a handful of consumer complaints also fails. The complaints constitute unreliable double hearsay, as they are out-of-court statements recorded in the Federal Trade Commission's ("FTC") complaint database, and the CFPB seeks to offer those complaints in this proceeding to prove the truth of the matter asserted (i.e. that consumers were

[2] Enforcement Counsel does not make a serious attempt to argue that returning customers could not have reasonably avoided the alleged harm. *See* Opp'n at 17. Of course, returning customers could have easily done so by choosing not to take out another loan under the same terms and conditions that were allegedly harmful.

misled and harmed by the Loan Agreement). The CFPB has not corroborated any of the statements made in those FTC reports (again, it has not conducted any consumer surveys or sought to present any direct consumer testimony), and has not otherwise justified the admission of this evidence, particularly where its own expert has cast doubt on the relevance of such evidence. *See* Resp'ts' Facts ¶ 24 (Dr. Manoj Hastak testifying that "the complaints are not representatives of the customers of Integrity Advance, and so they're just a small sampling of individuals who had a problem with Integrity Advance . . ." and were, thus, not "representative in any way" of a "typical consumer"). Such evidence is unreliable and should be excluded. *See* 12 C.F.R. § 1081.303(b) (hearsay evidence admissible only where "it is relevant, material, and bears satisfactory indicia of reliability so that its use is fair").

Even if the evidence were admissible, the small number of complaints actually further justifies granting summary disposition in Respondents' favor. At most, the CFPB has identified 127 complaints out of the 54,130 customers Integrity Advance serviced on or after July 21, 2011, *see* Opp'n at 9 (citing Dkt. 87C ¶¶ 6, 7)—this equates to a complaint rate of approximately 0.2%. *See* Dkt. 274A (Ex. 17 to Zack Decl.) at 807. And, only ***one*** of the complaints that the CFPB highlighted in its own Motion for Summary Disposition post-dates July 21, 2011, the relevant time period in this case. Dkt. 276 at 16-17 (citing Dkt. 88E, Ex. 30 to EC Facts at 69-72). A single potentially relevant complaint, or even 127 potentially relevant complaints, is a far cry from the thousands of consumer complaints the court found persuasive in the *AMG* case. *See FTC v. AMG Servs., Inc.*, 29 F. Supp. 3d 1338, 1362 (D. Nev. 2014), *aff'd sub nom. FTC v. AMG Capital Mgmt., LLC*, 910 F.3d 417 (9th Cir. 2018). Indeed, the small number of complaints relative to the number of loans issued by Integrity Advance provides

further evidence that reasonable consumers understood the terms of the Loan Agreement and that Respondents had no reason to believe otherwise.

II. The Loan Agreement clearly disclosed consumers' legal obligations.

In its response, the CFPB contends that the format of the Loan Agreement is "irrelevant" because its claims are based on the "inaccurate contents of Integrity Advance's disclosures, not the format." Opp'n at 6. But of course format matters. Indeed, in the *AMG* case relied on heavily by the CFPB, the court rested its decision largely on the "convoluted" format of the loan agreement, which "create[d] uncertainty" and "visually prioritize[ed] one half" of the agreement, while "hiding important information—including the provision that makes 'renewal' automatic . . . ." *FTC v. AMG Servs.*, 29 F. Supp. 3d 1338, 1361, 1370 (D. Nev. Jan. 28, 2014), *report and recommendation adopted by* 29 F. Supp. 3d 1338 (D. Nev. May 28, 2014). Unlike the loan agreement in *AMG*, Integrity Advance's Loan Agreement clearly and conspicuously disclosed consumers' legal obligation to select a payment option directly below the TILA Box, demarcated by bold, all-caps headers, and formatted for ease of comprehension by separating these sections into individual paragraphs. *See* Dkt. 274A (Ex. 1 to Zack Decl.) at 2.

The CFPB also is wrong when it states that "[i]f an Integrity Advance customer takes no action, and the loan therefore rolls over automatically, the customer has not breached any of his or her obligations under the terms of the loan." Opp'n at 7. Integrity Advance's customers were in fact required to take action (i.e. select a payment option), and their loans were automatically renewed only when they failed to do so. *See* Resp'ts' Facts ¶ 13 ("You must select your payment option at least three (3) business days prior to your Payment Due Date by contacting us at (800) 505-6073."); *id.* ¶ 21 ("If you fail to contact us to confirm your Payment Option at least three (3) business days prior to any Payment Due Date, or otherwise fail to pay the loan in full on any Pay Date, Lender may automatically renew your loan . . . ."). Because

that obligation was clearly and conspicuously disclosed, and not obscured by the format of the loan agreement like in *AMG*, it follows that the Loan Agreement was not deceptive or unfair.[3]

Similarly, although the CFPB claims that there were "additional costs that went beyond what was disclosed in the loan agreement," Opp'n at 4, the CFPB again ignores the clear terms of the Loan Agreement, which disclosed that additional fees would be incurred if a loan was renewed, *see* Resp'ts' Facts ¶ 17, and clearly explained how the auto-renewal process worked. *See id.* ¶ 21. The Loan Agreement also contained a "Special Notice," which clearly stated that "ADDITIONAL FEES MAY ACCRUE IF THE LOAN IS REFINANCED OR 'ROLLED OVER.'" Resp'ts' Facts ¶ 17. Even without the special notice, a reasonable consumer would expect to incur additional fees and costs if he or she failed to repay the loan on its due date.

The Loan Agreement also clearly allowed consumers to pay back their loans using forms of payment other than EFTs, *see id.* ¶¶ 63-66, and the CFPB's own allegations and evidence confirm that fact. *See* Dkt. 1 ¶ 41 (acknowledging that 5% of consumers obtained loans with Integrity Advance without having signed the ACH authorization); Dkt. 87D at 3, ¶ 8 (finding that 1.5% of initial loan repayments were made by electronic means).[4] The evidence establishes that Integrity Advance did not require its consumers pay their loans back through an EFT and, thus, that there is no violation of the EFTA.

[3] The CFPB's interpretation of the TILA requirement also is incorrect. *See* Opp'n at 6-7. Under the CFPB's view, Respondents could only have satisfied TILA by including at least five TILA boxes laying out the cost of the loan under various potential scenarios (*e.g.*, loan paid in full, loan paid off after one renewal, etc.). But such a disclosure would be confusing to consumers and would likely have violated TILA's mandate that disclosures be "clear and conspicuous." *See* 15 U.S.C. §§ 1631 and 1638. As discussed in Respondents' Opposition to Enforcement Counsel's Motion for Summary Disposition, this view is fundamentally at odds with TILA's intent to balance the need for disclosures against the need to avoid "information overload." *See* Resp'ts' Opp'n at 3-6 & n.2.

[4] The fact that most people chose to repay electronically is not surprising given the convenience of EFTs. That is not the same thing, however, as *requiring* consumers to repay electronically, which Integrity Advance expressly did not do. *See* Resp'ts' Facts ¶¶ 63-66.

III. The Loan Agreement offered a benefit to consumers.

Payday loan products, such as the one offered by Integrity Advance, provide a benefit to consumers that the CFPB has publicly acknowledged. *See* Resp'ts' Facts ¶ 23. Such products offer avenues to credit through a quick and simple process, and can help consumers to avoid overdrawing accounts or missing bill payments. *Id.* The CFPB attempts to brush aside these undisputed facts by saying they are "entirely irrelevant." Opp'n at 17. However, not only is the benefit to consumers a relevant issue – it is an element of the 'unfairness' claim that the CFPB has the burden to establish. *See* 12 U.S.C. § 5531(c) ("substantial injury is not outweighed by countervailing benefits to consumers or competition"). The CFPB does not attempt to show that there is no such benefit, but instead recycles its inaccurate assertion that the Loan Agreement "fail[s] to disclose the cost of the loans." Opp'n at 17. For the reasons stated in the sections above, that is incorrect.

The CFPB also provides no evidence that consumers did not benefit from the use of RCCs, although it is their burden, but instead faults Respondents for not proving the inverse. *See* Opp'n at 19. However, the benefit to consumers who seek payday loans is readily apparent. RCCs can provide a payment alternative if a consumer attempts to renege on his or her payment obligations; this protects lenders, which in turn allows them to extend credit to consumers who might not otherwise be eligible. This benefit is not outweighed by any purported injury, as the CFPB has not established the reason that even a single customer withdrew his or her ACH authorization, necessitating the use of RCCs, or that the withdrawal was justified. *Id.* ¶ 68. Further, any such injury is easily avoidable because consumers could repay loans through other means and even had the option to stop RCCs once initiated. *Id.* ¶¶ 66-67. Finally, the Loan Agreement disclosed, and the consumers consented to, the potential use of RCCs along with the

ACH authorization, which had its own clearly demarcated section that required a separate authorizing signature. *Id.* ¶¶ 69-72.

IV. Carnes did not have the requisite level of knowledge to be found personally liable.

The CFPB implies that Respondents argued that Mr. Carnes must know[5] that the Loan Agreement disclosures were *illegal* to be held liable. Opp'n at 22-23. That is not the case. Respondents have instead explained that the CFPB must establish that Mr. Carnes knew the disclosures were *deceptive* and/or *unfair*. *See* Dkt. 272 at 27-29. The CFPB must do more than show that Mr. Carnes knew generally how the loan process worked or that RCCs were used to collect payment in some instances. *Id.* The CFPB must show that Mr. Carnes knew that the information disclosed in the Loan Agreement, and the manner in which the disclosures were made, were likely to mislead or unavoidably harm consumers.[6] The CFPB cannot meet this burden because the Loan Agreement template was created by outside counsel, and Mr. Carnes did not substantively review or approve the text of the Loan Agreement.[7] Resp'ts' Facts ¶¶ 40-41, 97-99. Further, the CFPB has not shown that Mr. Carnes was otherwise aware of any purported deception or unfairness (such as through personal awareness of a significant number of consumer complaints). The undisputed facts instead establish that complaints were handled by

[5] As used here, the word "know" encompasses the fuller definition set forth in *CFPB v. Gordon*, 819 F.3d 1179, 1193 (9th Cir. 2016) ("[H]e 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."). As explained in Respondents' Motion for Summary Disposition, the *Gordon* standard also provides that the underlying acts must amount to "misrepresentations," "falsity," or "fraud." Dkt. 272 at 29-30.

[6] The CFPB incorrectly asserts that "Carnes admitted that he understood how Integrity Advance disclosed its loans as single-payment loans." Opp'n at 21 (citing EC Facts ¶ 96). However, the underlying testimony merely supports that Mr. Carnes understood that the TILA box disclosure showed a cost of $130 for a person with a $100 loan. EC Facts ¶ 96. That does not establish that Mr. Carnes knew about the full scope of the disclosures in the Loan Agreement, such as how renewals were disclosed, nor that they were deceptive or unfair.

[7] Having no evidence, the CFPB argues that Mr. Carnes *must* have approved the Loan Agreement template in/around 2008 because there was a small number of staff. Opp'n at 26-27. However, the staff included Edward Foster, who was general counsel and, thus, reasonably and naturally would have overseen the work of outside counsel. *Id.*

the third party call center, the number of complaints was low, the rate of repeat business was high, and Delaware regulators approved Integrity Advance to operate.[8] *Id.* ¶¶ 27-29, 47, 50-52.

Additionally, the CFPB asserts that Respondents have argued that Mr. Carnes is not liable due to his good faith reliance on counsel. Opp'n at 27. That misconstrues the argument. Mr. Carnes is not liable because he did not know about the specific disclosures in the Loan Agreement or that they were deceptive or unfair as demonstrated by, among other evidence, the fact that outside counsel created the Loan Agreement – *not* because he is shielded from liability due to his good faith reliance on counsel.

V. Restitution should not be awarded.

Restitution is not appropriate unless the CFPB establishes that "Defendants intended to defraud consumers or that consumers did not receive the benefit of their bargain." *CFPB v. CashCall, Inc.*, 2018 U.S. Dist. LEXIS 9057, at *36-37 (C.D. Cal. Jan. 19, 2018); *see also CFPB v. Nationwide Biweekly Admin., Inc.*, 2017 U.S. Dist. LEXIS 145923, at *28-29 (N.D. Cal. Sep. 8, 2017) (declining to award restitution where the CFPB failed to show fraud or that consumers did not receive a benefit).[9]

The CFPB does not allege that Mr. Carnes or Integrity Advance acted in bad faith, but instead argues that Respondents' good faith is not a reason to deny restitution – effectively

[8] The CFPB's citation to two letters and one enforcement action by state regulators does not have any bearing on whether the Loan Agreement was deceptive or unfair, or whether Mr. Carnes knew about it. *See* Opp'n at 23. The actions cited by the CFPB relate to state licensing issues, because Integrity Advance was incorporated in Delaware and acted pursuant to Delaware law, but did business over the internet with consumers who resided in other states. These three states contended that Integrity Advance should have been licensed in and followed their law. *Id.* (citing Dkt. 100B at Ex. 3 at 1, Ex. 4 at 1; *State ex rel. Swanson v. Integrity Advance, LLC*, 870 N.W.2d 90, 96-97 (Minn. 2015)). Further, the CFPB has not demonstrated that Mr. Carnes was aware of these actions.

[9] The CFPB seeks to bar Respondents from asserting that they acted in good faith for purposes of determining the appropriateness of restitution because Respondents did not previously assert that they relied on counsel at the first hearing. Opp'n at 28 n.11. However, Respondents always have maintained that they depended on counsel to create a legally compliant Loan Agreement. Further, the first hearing pre-dated the developments in the law found in the *CashCall* and *Nationwide* decisions.

ignoring the *CashCall* and *Nationwide* decisions that are directly relevant, without any justification. Opp'n at 28, 30. The CFPB instead relies on inapposite employment and housing cases to argue that it is entitled to restitution as legal rather than equitable relief, essentially as a form of money damages. *See id.* at 29-30. However, under the analysis in these cases, the imposition of this type of legal relief triggers the Seventh Amendment right to a jury, as opposed to equitable relief which does not trigger this right. *See Curtis v. Loether*, 415 U.S. 189, 197 (1974) (claims for legal damages trigger the right to a jury trial, in contrast to equitable remedies like restitution). Accordingly, the CFPB cannot seek this type of legal relief in an administrative setting where defendants do not have the ability to exercise their right to a jury trial. *See, e.g., FTC v. Verity International, Ltd.*, 443 F.3d 48, 67 (2d Cir. 2006) ("The fact that only an equitable remedy [of restitution] is available eviscerates the defendants-appellants' contention that the Seventh Amendment confers a right to a jury trial in this case."). The only type of restitution that the CFPB can lawfully seek in this setting is equitable restitution. If the CFPB is in fact seeking restitution as a legal remedy, then restitution should be denied.

The CFPB also misses the import of Respondents' good faith reliance on Delaware regulators by arguing that the Delaware regulators did not review the Loan Agreement for deceptive or unfair practices. Opp'n at 21-22. Although the evidence suggests that the Delaware regulators did in fact review the loan agreement, *see* Resp'ts' Facts ¶¶ 33-34, that is not the point. The point is that Respondents transparently provided the Loan Agreement, and other documents, to the Delaware regulators for their review. After which, Integrity Advance was licensed. This reflects that Respondents were acting in good faith and reasonably believed they were legally compliant.[10] Restitution should not be awarded.

[10] The CFPB also has not shown, as they must, that consumers did not receive the benefit of their bargain. *See CashCall, Inc.*, 2018 U.S. Dist. LEXIS 9057, at *36-37; *see also Nationwide Biweekly Admin., Inc.*, 2017 U.S.

* * *

For the foregoing reasons, the ALJ should grant Respondents' Motion for Summary Disposition in its entirety.

Dated: June 10, 2020

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

Dist. LEXIS 145923, at *28-29. Integrity Advance's customers did in fact receive the benefit of their bargain, as evidenced by the number of customers who returned. *See* Dkt. 272 at 32. The CFPB incorrectly asserts that Respondents have waived this argument. *See* Opp'n at 30, n.13. However, Respondents have appropriately raised the issue in their Motion for Summary Disposition, where it is pertinent. Respondents did not raise the issue earlier in their Motion to Open Record for a New Hearing because Respondents were not seeking to introduce additional evidence on these grounds, given that the relevant evidence already was on the record. *See* Dkt. 272 at 32 n.8.

CERTIFICATE OF SERVICE

I hereby certify that on the 10th day of June 2020, I caused a copy of the foregoing Respondents' Reply Brief in Support of their Motion for Summary Disposition 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.