DREHER TOMKIES LLP

ALERT

FOR CLIENTS AND FRIENDS OF DREHER TOMKIES LLP

February 13, 2015

CALIFORNIA SETTLES WITH ONLINE LENDER FOR DECEPTIVE PRACTICES

The California Department of Business Oversight ("DBO") settled an administrative case with CashCall, Inc., an online nonbank lender licensed under the Finance Lenders Law ("FLL"), who allegedly used deceptive marketing and servicing practices to charge consumers additional interest on unsecured consumer loans. An administrative hearing had been scheduled after the lender contested the DBO's notice of intent to suspend the lender's licenses for violation of the FLL.

The lender's marketing practices allegedly led consumers to obtain loans in higher amounts than consumers desired so that the lender could charge unlimited interest rates. California imposes a 30% interest rate cap on unsecured consumer loans of less than $2,500. The lender made loans of $2,600 or more with an annual percentage rate of 135% to 179%. The lender's marketing materials disclosed no minimum loan amount but indicated that the lender provided loans "up to" $2,600, $5,000 or $10,000.

<u>Alleged Deception</u>

When consumers asked for a loan under $2,600, the lender allegedly convinced consumers to take a $2,600 loan, prepay whatever excess loan amount that the consumers did not want and so receive "interest payment savings" as a result of the prepayment. This technique enabled the lender to charge an unlimited interest rate on a net loan amount that effectively could have been subject to the 30% interest rate cap. Finally, the lender allegedly failed to withdraw initial scheduled monthly payments from bank accounts of consumers who made prepayments. As a result, consumers did not receive the full potential benefit of interest savings insofar as their loan periods were not shortened by prepayment.

In exchange for not suspending its finance lender licenses, the lender agreed to refrain from engaging in the business practices described above, to make restitution payments to affected consumers within 90 days of the settlement and to pay $1 million in penalties and legal costs to the DBO.

<u>New Disclosures</u>

The settlement requires the lender to make specific disclosures to consumers going forward. In any advertisement marketing its loans, the lender must clearly and conspicuously disclose the minimum loan amount. The settlement defined "clear and conspicuous" as (i) for visual text on the Internet or television, not obscured by techniques such as graphical displays, shading or coloration, (ii) for visual text on television, in a manner that allows consumers to read the information disclosed and (iii) for oral advertisements, in a speed and volume sufficient for consumers to hear and comprehend the disclosures. When consumers contact the lender about a loan, the lender must disclose to consumers (i) that it does not make loans of less than $2,600, (ii) California's interest rate cap on loans of less than $2,500 and (iii) that consumers should consider another lender if they want a loan of less than $2,500 . Finally, at the time a consumer authorizes a prepayment, the lender must disclose to consumers that their first regularly scheduled payment will occur on the date scheduled and that the prepayment may reduce the amount of the first regularly scheduled payment from the amount reflected in the promissory note.

Creditors must not only consider the facial accuracy of statements but the potential expectations of consumers and implied benefits. Context matters. The precedent is potentially troubling insofar as creditors often impose minimum loan amounts to avoid various regulations such as licensing. Fuller disclosure of program parameters may be helpful. We can assist in reviewing websites, marketing materials and loan documents for these and other matters. ❑

✧ *Mike Tomkies and Susan Manship*

CLASS CERTIFIED IN CALIFORNIA "TRUE LENDER" CASE

In December 2014, a California district court certified two classes of California borrowers who incurred late fees on Sallie Mae-branded closed-end private student loans made by an Oklahoma national bank and marketed and serviced by Sallie Mae, Inc. (now Navient Solutions, Inc.). *Ubaldi v. SML Corporation*, No. 11-cv-01320-EDL (N.D. Cal. Dec. 19, 2014). The borrowers originally alleged that (i) they were charged unlawful late fees under California law, (ii) they were charged usurious interest (*i.e.*, greater than 10%) and (iii) their promissory notes' choice-of-law provisions were unenforceable because Sallie Mae is the "true lender" of the student loans. To support their *de facto* lender theory, the plaintiffs asserted, among other things, that (i) the bank bore no risk of loss

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because loans were sold to Sallie Mae within 90 days of disbursement and (ii) Sallie Mae controlled approval and funding of the loans.

The plaintiffs' *de facto* lender theory survived an early motion to dismiss by Sallie Mae. *Ubaldi v. SML Corporation*, 852 F.Supp.2d 1190 (N.D Cal. 2012). Sallie Mae argued that Section 85 of the National Bank Act (NBA) completely preempted the plaintiffs' state law claims when (i) a national bank charged interest and fees permissible under its "home" state's law and (ii) the national bank was named as the lender in the loan documents. The district court noted that whether the court should look at the form of the loan documents or the substance of the transaction to identify the actual lender and determine whether the NBA preempts state law claims is an issue of first impression for the Ninth Circuit. The court concluded that none of the authorities proffered by the parties were adequately persuasive and allowed the plaintiffs' case to survive because the case was in the early stages of litigation.

The district court also earlier denied a motion for class certification. *Ubaldi v. SML Corporation*, No. 11-01320 EDL, 2014 WL 1266783 (N.D. Cal. Mar. 24, 2014). The plaintiffs' original classes included all California residents who obtained a particular Sallie Mae private loans for which Sallie Mae was the *de facto* lender. The court found that a common issue did not predominate the class members because Sallie Mae partnered with 14 banks to offer that brand of loan and the individual program agreements between Sallie Mae and the fourteen banks varied. The court noted that the amount of time between disbursement and Sallie Mae's purchase of loans [which ranged from one to 365 days among the 14 banks] is not irrelevant and that the actual practices of Sallie Mae and the banks are relevant to *de facto* lender status because the Sallie Mae-bank agreements do not govern every detail.

Because the court had denied the plaintiffs' motion without prejudice, the plaintiffs were allowed to amend and re-file their motion to certify four classes: two late fee classes and two usury classes. The plaintiffs amended the class definitions to include all California residents who obtained three specific types of Sallie Mae-branded loans where the lender was identified as Stillwater National Bank. The proposed classes excluded any person who has a promissory note that includes an arbitration clause or class action waiver. The court certified the two late fee classes but denied the plaintiffs' motion to certify the two usury classes. The court ruled that plaintiffs failed to demonstrate standing to assert usury claims against the named defendants, which now include SLM PC Student Loan Trust 2004-A.

The court has yet to identify the specific factors, or indicate the relevant weight of those factors, that it will consider in making its *de facto* lender determination.

In addition to potentially providing additional guidance on "true lender" analysis, *Ubaldi* is notable in two respects: First, *Ubaldi* involves traditional closed-end installment loans repayable in equal monthly installments at competitive rates. The named plaintiffs had loans between $6,000 and $23,000. One named plaintiff had a variable annual interest rate that reached only as high as 18%. Many "true lender" cases have involved higher-rate loans (over 100% APR). Second, the plaintiffs named a trust that purchased some of the loans (one of 28 such trusts holding Stillwater loans) as a defendant.

Bank partnering programs require careful structuring of formal legal arrangements and operations to withstand potential substantive challenges. With 30 years' experience with such programs, we can assist in analyzing and creatively structuring programs to accommodate strategic concerns and minimize risks. ❑

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