

Regulatory Report

For the Payment Processing Industry



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FEATURE ARTICLE

U.S. District Court Dismisses CFPB Lawsuit Against Payment Processor

By [Keith Barnett](#), [Ashley Taylor](#) and [Reade Jacob](#)

On March 17, the U.S. District Court for the District of North Dakota granted Intercept Corporation ("Intercept"), Bryan Smith, and Craig Dresser's Motion to Dismiss the Consumer Financial Protection Bureau's ("CFPB" or "Bureau") Complaint in the case between the CFPB and Intercept. The Court held that the Bureau failed to adequately plead an unfair, deceptive, or abusive act or practice under the Consumer Financial Protection Act ("CFPA"). In addition, the court held that the CFPB failed to show that Intercept violated any substantive federal law or industry standards. The decision to grant the Motion to Dismiss marks the first time that the Bureau has had its entire case dismissed through a motion to dismiss.

By way of background, the CFPB filed a Complaint against Intercept, Bryan Smith, and Craig Dresser in June 2016. The CFPB alleged that Intercept continually processed transactions for clients "they knew, or should have known, were making fraudulent or other illegal transactions" and that Intercept ignored certain "red flags" related to fraudulent or illegal transactions. These actions violated the Consumer Financial Protection Act's prohibition against unfair and deceptive practices, according to the CFPB's Complaint. Intercept filed a Motion to Dismiss the Complaint in August 2016.

The Third Party Payments Processors Association ("TPPPA") filed an Amicus Brief in support of Intercept's Motion to Dismiss. Chief among the TPPPA's concerns was that the CFPB's Complaint against Intercept failed to adequately allege that Intercept violated any substantive federal law or industry rule – notably, the NACHA Operating Rules that were in place at the time the alleged violations occurred. The TPPPA's Amicus Brief explained to the Court that the Bureau's Complaint completely misstated the NACHA Rules and omitted portions of the NACHA Rules that rendered the allegations in the Complaint misleading and incorrect. Additionally, the TPPPA asserted that the CFPB failed to allege Intercept or its banks ignored certain "red flags" in light of the fact that Intercept never received a rules violation from NACHA.

Judge Ralph R. Erickson granted Intercept's Motion to Dismiss the case without prejudice, relying on the TPPPA's arguments stated above and explanation of the participants in an ACH transaction. In his Order granting the Motion to Dismiss, Judge Erickson wrote that "A close review of the complaint yields a conclusion that the complaint does not contain sufficient factual allegations to back up its conclusory statements regarding Intercept's allegedly unlawful acts or omissions. While the complaint indicates that Intercept was

required to follow certain industry standards, it fails to sufficiently allege facts tending to show that those standards were violated.”

The court also sided with the TPPPA’s argument that the CFPB failed to identify “red flags” or how Intercept’s failure to act upon those “red flag” caused harm or was likely to cause harm to consumers. “A complaint containing mere conclusory statements without sufficient factual allegations to support the conclusory statements,” the court wrote, “cannot survive a motion to dismiss.”

The CFPB will now have the option to file an Amended Complaint, or appeal the decision to the Eight Circuit. If the

Bureau decides to file an Amended Complaint, it will likely be dismissed unless the Bureau establishes a direct link between actual violations of the NACHA Operating Rules and Intercept’s alleged conduct.

Troutman Sanders attorneys, Ashley L. Taylor, Keith J. Barnett, and Reade Jacob represented the TPPPA in the case. Keith Barnett argued on behalf of the TPPPA at oral arguments.

CFPB Releases Monthly Report Highlighting Credit Card Complaints

By [Brooke Conkle](#) and [Michael E. Lacy](#)

On March 28, the Consumer Financial Protection Bureau released its monthly complaint snapshot, with a specific focus on credit cards. Since its inception in July 2011, the Bureau has handled 1,136,000 consumer complaints across all products, with 116,200 complaints related to credit cards. The CFPB received 26,300 complaints in February 2017, with 2,299 of those complaints related to credit cards.

“Credit cards are a vital financial tool used daily by more than half of all adults in this country,” said CFPB Director Richard Cordray in a statement. “Consumers deserve clear guidance and need to be able to resolve problems that arise with their cards.”

The Bureau’s snapshot highlights particular areas where consumers have reported problems to the CFPB, including:

- **Fraudulent Charges:** The highest number of consumer complaints about credit cards were related to billing disputes. A number of consumers complained to the Bureau that they experienced charges on their credit cards which they had not initiated. Many consumers disputed the unauthorized charges, but also reported difficulty having the charges removed, even after disputes were resolved in their favor.
- **Rewards Programs:** Consumers also reported problems related to credit card rewards programs. Some consumers contacted the CFPB after they were unable to take advantage of rewards benefits after meeting program criteria. Consumers also reported

that credit card companies’ customer service representatives provided them with conflicting program information from that provided online.

- **Identity Theft and Fraud:** The Bureau also received complaints of negative credit reporting for account activity that was not initiated or authorized. Some consumers told the CFPB that credit card companies did not respond promptly to billing disputes and did not correct the reporting of the account. Other consumers reported that credit card accounts were fraudulently opened in their name even though their files included alerts warning of potential fraud.
- **Late Fees and Servicing Costs:** Consumers complained to the CFPB that credit card companies frequently assessed late fees to their accounts even when payments were made on the due date. Further, consumers also detailed untimely processing of payments.

The snapshot also included a geographic analysis of the data, and highlighted trending complaints in the metropolitan Boston area, as well as Massachusetts as a whole. The Bureau reported receiving 20,600 complaints from Massachusetts consumers since 2011, with 15,400 from the Boston area. Average monthly complaints from Massachusetts increased 19 percent over the past three months – slightly lower than the national average of 22 percent.

The March 2017 Monthly Complaint Report is available [here](#).

Republicans Move to Roll Back CFPB Prepaid Card Rules

By [Brooke Conkle](#) and [Michael E. Lacy](#)

Republicans in Congress have moved to repeal recently issued Consumer Financial Protection Bureau regulations governing the prepaid card industry. Rep. Tom Graves (R-Ga.) introduced a bill in the House in early February that would submit the rules to a vote of disapproval under the Congressional Review Act. A group of Republicans filed a similar measure in the Senate.

[As we reported](#) last year, the CFPB issued final rules regarding prepaid accounts in October 2016. “Prepaid accounts” are those accounts marketed or labeled as “prepaid” for use at unaffiliated merchants or ATMs, but are not linked to checking accounts, share draft accounts, or negotiable order of withdrawal (NOW) accounts. The new rules confirm that Regulation E applies to prepaid accounts and, as a result, employers cannot require their employees to receive wages through payroll cards. Furthermore, the prepaid card rules require issuers to investigate and resolve errors when consumers report fraudulent activity or errors on their accounts and provisionally credit the disputed amount during the investigation. Issuers must also provide consumers with “easy-to-understand” disclosures describing the costs associated with prepaid accounts. For those prepaid accounts that offer credit features, issuers must provide consumers with a monthly credit billing statement

and are prohibited from automatically using uploaded funds to satisfy credit repayments.

“As a business guy, I have experienced first-hand the impact overregulation has on growth and innovation,” said Sen. David Perdue (R-Ga.), one of the bill’s sponsors in the Senate. “This rule is entirely too broad and would cripple the electronic payment marketplace which Georgians and millions of consumers across the country depend on.”

However, consumer groups who hailed the rules’ issuance in the fall are now expressing concern. “The CFPB’s new rules will help consumers compare cards more easily so they can find the most affordable option and give them the peace of mind that their money will be protected if their card is lost or stolen. But those safeguards will disappear if Congress passes this misguided resolution and revokes these common sense protections for consumers,” said Christina Tetreault, a staff attorney at Consumers Union.

The House version of the bill is available [here](#); the Senate version is available [here](#).

Federal Court Transfers Payment Processor’s Case Seeking Collection of \$4.5M Judgment

By [Brooke Conkle](#) and [Michael E. Lacy](#)

A New York payment processor successfully defended one personal jurisdiction challenge, but lost the other in the Northern District of Texas. The case represents an attempt by TransFirst Group, Inc. to collect a \$4.5 million judgment it obtained against Dominic “Nick” Magliarditi in 2013 related to the group’s purchase of Magliarditi’s payment processing company, Payment Resources International. Magliarditi and other entities were found guilty of RICO violations after a three-week bench trial in 2009. The Northern District of Texas further found that Magliarditi, who is a licensed attorney, lied under oath in his interrogatory responses in affidavits. The Fifth Circuit affirmed the judgment.

Since then, TransFirst has repeatedly sought to enforce the judgment in Texas, as well as in California and Nevada, to no avail. TransFirst again filed suit in the Northern District of Texas in 2016, this time against Magliarditi, his wife Francine, and a number of companies and trusts that were not parties to the 2013 judgment. According to TransFirst, Magliarditi fraudulently transferred assets to the new defendants, which it characterizes as shell companies, in an effort to shield his assets from collection. TransFirst argues that Magliarditi has paid a mere \$62 toward the judgment, while intentionally evading service, refusing to answer subpoenas, and ignoring requests to have his deposition taken.

Magliarditi and the other defendants challenged the suit, arguing that the court could not exercise personal jurisdiction over them because all of the defendants live or are incorporated in Nevada and California.

[The court concluded otherwise](#), finding that the new action to collect on the judgment was merely a continuation of the earlier case in which Magliarditi was found liable. Because the court could exercise personal jurisdiction over Magliarditi, it also was able to exercise personal jurisdiction over his alter ego companies. "As alleged alter egos of Mr. Magliarditi, over whom the court has personal jurisdiction,

and in light of plaintiffs' demonstrated inability to collect on the judgment notwithstanding several years of postjudgment discovery and proceedings," Judge Sam A. Lindsay wrote, "the court concludes that this is not one of those rare cases in which the court's exercise of personal jurisdiction over the entity defendants would offend 'traditional notions of fair play and substantial justice.'" However, [in a later opinion](#), the court found that it could not exercise personal jurisdiction over Francine Magliarditi.

The case continues in the District of Nevada, where the Magliarditis live.

CFPB Orders MasterCard and UniRush to Pay \$13 Million

By [Brooke Conkle](#) and [Keith J. Barnett](#)

On February 1, the Consumer Financial Protection Bureau [ordered](#) payment card companies MasterCard and UniRush to pay \$10 million in restitution and a \$3 million fine related to service breakdowns that left customers unable to access their funds. "MasterCard and UniRush's failures cut off tens of thousands of vulnerable consumers from their own money, and threw some into a personal financial crisis," said CFPB Director Richard Cordray. "The companies must set things right for consumers and make sure such devastating service disruptions are not repeated."

UniRush is the program manager for RushCard, a reloadable prepaid debit card, which many consumers use for government benefits or payroll deposits. In 2014, UniRush decided to switch payment processors to MasterCard, and the parties spent thirteen months preparing for the service transfer. The switch occurred in mid-October 2015, when RushCard had approximately 650,000 active users. However, there were a number of problems associated with the transfer and, as a result, many customers could not use their cards to receive paychecks and other direct deposits, withdraw cash, make purchases, pay bills, or get accurate account information.

According to the Bureau, MasterCard and UniRush denied consumers access to their funds because UniRush did not accurately transfer all of its accounts to MasterCard.

Furthermore, the Bureau claims that UniRush delayed processing customers' direct deposits during the service transfer or failed to process their deposits at all. The consent order also alleges that the company double posted deposits, which falsely inflated customers' account balances and led some customers to overdraw their accounts. The Bureau claims that UniRush compounded the problem by failing to provide customer service to many customers who sought help from the company. The Bureau recorded 830 complaints from RushCard customers regarding the service transfer. By comparison, the CFPB received 147 complaints about prepaid cards in general from November 2014 to January 2015.

In addition to having to pay the ordered restitution and fine, the two companies must devise a plan to prevent future service disruptions. The Bureau plans to monitor the companies' compliance with the consent order.