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# Back to the Future:

## On the Potential of Innovation and Compliance in Financial Services Under the Trump CFPB

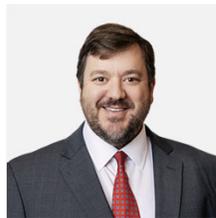
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## **Presentation Roadmap**

1. Consumer Demand in Shaping Innovation
2. Balancing Innovation with Consumer Protection
3. Leveraging Technology for Compliance and Protection
4. Regulatory Perspectives and Industry Insights
5. Best Practices

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## **Importance of Balancing Innovation and Regulation in Financial Services**

- Delicate balance between protecting consumers without hindering financial innovation
  - Striking the right balance can ensure a healthy relationship for all parties involved
  - What is the proper role of regulators (state and federal) in facilitating that balance?

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# Consumer Demand in Shaping Financial Innovation

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## Trends in Consumer Preferences



### Convenience and Speed

Instant Payments  
Mobile-First Experiences



### Accessibility

Low-Cost Financial Products  
Digital Banking



### Flexibility

Buy Now, Pay Later  
Customized Financial Planning

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## Impact on Financial Product Development

Consumer preferences have encouraged the creation of more accessible, user-friendly, and customizable financial products and services

- Reflects a broader cultural shift towards digitalization and autonomy

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## Mobile Banking

Mobile Banking Applications have transitioned into comprehensive platforms, reducing the need for physical branch visits and broadening accessibility for consumers

- Investing
- Budgeting
- Accessing Customer Support
- Remote Check Deposits



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## Peer-to-Peer Payment Systems

Consumers have shown an increased preference for alternative lending models outside of traditional banks

- Gives consumers access to more customized, transparent loan terms



## Digital Payments

The shift toward convenience and speed has spurred the development of digital payment systems, mobile wallets, and contactless payments



## Buy Now, Pay Later Services

The growing consumer demand for flexible payment options has driven the rise of BNPL services

afterpay 

affirm 

Pay later with  
**Klarna.**

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# Balancing Innovation with Consumer Protection

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## Risks of Technological Advancements – Data Privacy



**Unauthorized Access:** Open banking systems can increase the risk of unauthorized access or improper use of consumer data if not adequately safeguarded



**Data Retention:** If data is retained indefinitely, or for unnecessarily long durations, it increases the chances that sensitive information could be exposed



**AI and Automation:** Machine learning models and automated systems are often trained on large datasets, which can include sensitive personal information. Without robust privacy protection, these systems could inadvertently expose or misuse consumer data.

## Risks of Technological Advancement – Financial Fraud & Cybersecurity

### Financial Fraud:

- As consumers increasingly store financial information in digital platforms, the risk of identity theft rises
  - Compromised accounts could allow malicious actors to make fraudulent transactions or gain access to sensitive financial information

### Cybersecurity:

- Financial institutions and Fintech companies handling large amounts of personal and financial data become prime targets for cyberattacks

## Strategies for Mitigating Risks



### Implementing Robust Security Measures

- Data Encryption
- Tokenization
- Using Secure APIs
- Multi-Factor/Biometric Authentication



### Developing Transparent Communication Channels with Consumers

- Education and Awareness
- Consumer Consent and Control Over Data
- Communication About Data Usage
- Open Channels for Consumer Input

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## Leveraging Technology for Compliance and Protection

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# Leveraging Technology for Compliance and Protection

## Automated Compliance Monitoring Tools

- Data Privacy and Protection Tools:
  - Tools that monitor how customer data is handled and ensure privacy rights are respected
- Know Your Customer Automation:
  - Tools that automatically verify customer identity, conduct background checks, and collect necessary documentation
- Transaction Monitoring Systems:
  - Track and analyze transactions to prevent money laundering, fraud, and other illicit transactions
  - Identifies suspicious patterns that may require investigation

# Leveraging Technology for Compliance and Protection

## AI-Driven Risk Assessment Platforms

Many Fintech companies are adopting AI and machine learning platforms to automatically detect risks, monitor transactions, and analyze patterns for compliance

- AI and machine learning may automatically detect anomalies in financial transactions and monitor systems for potential threats
- May also improve compliance by automatically analyzing data for regulatory adherence

## Technology as a Tool for Consumer Protection

### Real-Time Fraud Detection Systems

- Detects fraudulent activity before the transactions take place

### Personalized Financial Advice and Education

- AI and other technologies can create enhanced consumer experiences through personalized financial products with more transparency

## Regulatory Perspectives and Industry Insights

## CFPB's Shifting Approach to Innovation

- Agency's approach to innovation issues has vacillated depending on leadership in charge
- Cordray – Some activity, but less of a priority
  - Project Catalyst had potential, but never really got off the ground
  - Some substantive rulemakings touched on innovation issues – e.g., payday rule consideration of “wage advance products” and cash-flow underwriting models.
- Kraninger – Leaned into innovation
  - Stood up a robust Innovation Office and created processes for regulatory relief and sandboxes
  - Intertwined with CFPB's approach to guidance at the time. Under Kraninger, CFPB recognized that regulatory ambiguity could chill development of innovative products and services
  - 2019 Innovation Policies: (1) No-Action Letters, (2) Trial Disclosure Program Waivers, (3) Compliance Assistance Sandbox Approvals
- Chopra – Tech-skeptical?
  - Innovation Office rebranded as Office of Competition and Innovation, and most 2019 policies were revoked
  - Shift to providing guidance writ large, rather than helping individual companies solve regulatory issues
  - Statement on AVM rulemaking: “We've terminated the program that handed out special legal immunities and favors to individual AI companies that they could exploit to gain an unfair advantage.”
- New leadership: Return to Kraninger approach, or new direction?

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## Current Regulatory Landscape – CFPB

- *Seila Law*: Director subject to President firing at will
  - Perpetual 4-year clock for agency leadership to impose policy preferences
  - Chopra fired on February 1
  - Acting Director Russell Vought appointed on February 7; **has shuttered agency effectively.**
- Focus under Chopra on Non-Rulemaking Activities
  - Non-rulemaking Guidance (Circulars, Advisory Opinions, etc.)
  - Speeches, Press Releases, Blogs, Tweets (“Bully Pulpit”)

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## The Current Regulatory Landscape

### Whirlwind of Releases Last Few Months of Chopra's Tenure

- Rebooted NAL and CAS Policies with new, stringent requirements
- Notice of Proposed Rulemaking subjecting Data Brokers to the FCRA
- Implemented § 1033 of the Dodd-Frank Act, finalizing Open Banking
- Potential LP Rule for Consumer Loans (response to petition)
- Guidance on Earned Wage Access (unclear impact)
- Regulation AA rulemaking/revived Credit Practices Rule proposal

**All of this may be quickly undone by new agency leadership**

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## Anticipated Changes Under New CFPB Leadership



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## Anticipated Changes Under New CFPB Leadership

### Rollback of Many of the Agency's Actions Under the Biden Administration

- Eye towards deregulation, more industry friendly approach
- Potential Rules on Chopping Block
  - Section 1033
  - Section 1071 Small Business Data Collection
  - Overdraft Fees
  - FCRA Data Broker and Medical Debt
  - Nonbank Registry of Terms and Conditions and Enforceable Orders
  - Mortgage Closing Cost "Junk Fees"
  - Credit Card Late Fees

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MARKETS & FINANCE | REGULATION

### Vought Moves to Defang CFPB, Telling Staff to Halt All Supervision

The acting director issues new orders to staff and says he won't ask for funding

### 'Delete CFPB': Musk calls for elimination of consumer bureau

Republicans and the financial industry have long targeted the CFPB for what they consider its overly aggressive regulation.

### Ted Cruz Leads Republican Charge to Defund Consumer-Protection Agency

CFPB was created by Democrats in the wake of the 2008 financial crisis

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## Lessons Learned from Prior Transitions

### How much is past prologue for what will happen now?

- Transition from Rich Cordray to Mick Mulvaney/Kathy Kraninger
- Transition from Kathy Kraninger to Dave Uejio/Rohit Chopra
- Recurring themes
  - Shifting tool choice focus (rulemaking, guidance, enforcement, supervision, innovation)
  - Disclosure vs. substantive regulation; principles based vs. prescriptive rules
  - Maturation of agency as an organization, or lack thereof
- Expect the unexpected!

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## Innovation Friendly Policies on Horizon?

### 12 U.S.C. § 5511(b): The CFPB's Multi-Purpose Mandate

1. To provide consumers with timely and understandable information
2. To *protect consumers* from unfair, deceptive, or abusive acts and practices and discrimination
3. To *remove outdated, unnecessary, or unduly burdensome regulations*
4. To enforce Federal consumer financial law consistently; and
5. To ensure that markets for consumer financial products and services operate transparently and efficiently to *facilitate access and innovation*

## Innovation Friendly Policies on the Horizon?

### Creating an Innovation-Friendly Regulatory Environment

- Incentivize Collaboration Between Innovators and Regulators
- Encourage Regulatory Sandboxes
- Streamline Licensing and Approval Processes

## **Innovation Friendly Policies on the Horizon**

### **Balancing Business Growth with Consumer Protection**

- Focus on Education and Transparency
- Utilize Tech to Improve Oversight
- Provide Clear Guidance and Safe Harbors

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## **Best Practices**

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## Collaboration Between Regulators and Innovators

### Regulators Need to Work *With*, Not Against, Financial Innovators

- The CFPB should facilitate partnerships between financial service providers, Fintechs, and consumer advocacy groups to create solutions that both advance innovation and ensure consumer protection
- Positive feedback loops between the CFPB and innovators can help the agency stay ahead of emerging technologies
- Targeted outreach to CFPB and other regulators could be beneficial to get *informal* buy-in to product development and legal compliance

## Continuous Adaptation to Evolving Consumer Needs

As consumer demands grow and evolve, financial service providers and Fintechs are poised to meet and service those demands

- Overregulation could hinder progress in financial innovation
- An open dialogue between regulators and innovators will ensure a healthy relationship between all parties

# Conclusion

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## Summary of Key Insights

### Consumer Preferences are Shaping Financial Innovation

- Trends such as convenience, speed, mobile-first experiences, and flexible payment options are driving the development of new financial products and services

### Technological Advancements – Creating and Addressing New Risks

- Technological advances will create new risks, including potential weaknesses with data privacy, financial fraud, and cybersecurity
- However, technology can also be leveraged to assist with regulatory compliance and consumer protection

### Balancing Innovation and Regulation

- To best create an innovation-friendly regulatory environment, regulators and innovators must work together to ensure a healthy relationship and continuous adaptation to evolving consumer needs

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## **Future Outlook for Financial Services**

- Consumer demands will continue to evolve, and financial innovators will continue to employ new technologies to meet those demands
- New technologies introduce new risks, but also present opportunities to mitigate those risks

## **Call to Action: Emphasizing the Need for Collaboration and Innovation**

- Developing an innovation-friendly regulatory environment will enable consumer demands to be addressed while also safeguarding them from financial fraud and other cybersecurity risks
- Collaboration will allow regulators to stay ahead of the evolving financial landscape and address risks where they are

# Questions?

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