

Date of Hearing: March 28, 2022

ASSEMBLY COMMITTEE ON BANKING AND FINANCE

Timothy Grayson, Chair

AB 2433 (Grayson) – As Amended March 11, 2022

SUBJECT: Department of Financial Protection and Innovation: unlawful practices

SUMMARY: Clarifies that the Department of Financial Protection and Innovation (DFPI) can bring an order to discontinue violations (ODV) against a licensee or person for a violation that has already occurred.

Specifically, **this bill:**

- 1) Clarifies that the commissioner may bring an ODV against a licensee or person when the licensee or person *has* violated the law, *has* conducted business in an unsafe or injurious manner, or *has* engaged in any activity in violation of the law in the following statutes:
 - a) The Corporate Securities Law Act of 1968. (Corp Code 2250.)
 - b) The California Commodity Law of 1990. (Corp. Code Sec. 29542.)
 - c) The Franchise Investment Law. (Corp. Code Secs 31406 and 31407.)
 - d) The Money Transmission Act. (Fin. Code Sec. 2148.)
 - e) The Check Sellers, Bill Payers, and Proraters Law. (Fin. Code Sec. 12307.2.)
 - f) The Escrow Law. (Fin. Code Sec. 17415, 17602, 17603, and 17604.)
 - g) The California Financing Law. (Fin. Code Sec. 22690, 22707.5, and 22712.)
 - h) The Student Loan Servicing Act. (Fin. Code Sec. 28164.)
 - i) The California Residential Mortgage Lending Act. (Fin. Code Sec. 50321, 50322, 50323.)
- 2) Clarifies in the following statutes that the commissioner may bring ODV against a licensee or person when the licensee or person *is* violating the law or *is* failing to comply with specified provisions: Brokers and Investment Advisors under the Corporate Securities Law Act of 1968 (Corp Code 2250) and Escrow Law (Financial Code Sections 17415).

EXISTING LAW:

Existing law establishes DFPI in the Business, Consumer Services, and Housing Agency, headed by the Commissioner of Financial Protection and Innovation. Under existing law, DFPI is charged with oversight and enforcement of various laws and may bring an ODV as follows:

- 1) The Corporate Securities Law of 1968 (Corp Code Sec. 25000 et seq.) requires persons offering or selling securities such as stocks or bonds to qualify (e.g., submit to the

Department for review and approval) the proposed securities, and requires licensing and regulation of securities broker-dealers and certain investment advisers, except as specified.

If the commissioner has reasonable grounds to believe that a broker-dealer or investment advisor, except in specified circumstances, has violated any law or rule binding upon it, the commissioner must direct the discontinuance of the violation. If the commissioner has reasonable grounds to believe that a broker-dealer or investment advisor, is conducting business in an unsafe or injurious manner, the commissioner may direct the discontinuance of the unsafe or injurious practices. (Corp Code Secs. 25249 and 25250.)

- 2) The California Commodity Law of 1990 (Corp Code Sec. 29500 et seq.) prohibits misrepresentation, fraudulent and deceptive acts in the offer and sale of certain off-exchange commodities, except as specified; and provides administrative, civil (injunctions, ancillary relief and appointment of receiver) and criminal remedies for violations of the law.

Grants the commissioner power to order a person who is engaging in an activity in violation of that law or rule or order thereunder, to order the person to desist and refrain from the activity, as prescribed. (Corp. Code Sec. 29542.)

- 3) The Franchise Investment Law (Corp. Code Sec. 31000 et seq.) requires persons offering or selling franchises to register (e.g., submit to the Department for review and approval) the proposed franchises with the Department, except as specified; prohibits misrepresentation, fraudulent and deceptive acts in the offer and sale of franchises; and provides administrative, civil (injunction, ancillary relief and appoint of receiver) and criminal remedies for violations of the law.

Authorizes the commissioner to issue a citation to a person when the commissioner has cause to believe that a person is violating any provision of that law or any rule or order promulgated pursuant to that law, as prescribed. The commissioner may, after examination or investigation, if the commissioner has reasonable grounds to believe that a person is conducting business in violation of any provision of this law or related rule or order to direct the discontinuance of the violation by written order, as specified. (Corp. Code Secs 31406 and 31407.)

- 4) The Money Transmission Act (Fin. Code Sec. 2000 et seq.) permits the commissioner, if it appears to the commissioner that a licensee is violating or failing to comply with any state law, to direct the licensee to comply with the law by order, or if it appears that any licensee is conducting its business in an unsafe or injurious manner, to direct the discontinuance of the unsafe or injurious practices. The commissioner may, after holding a hearing concerning the above acts and finding that the licensee is violating or failing to comply with any state law or is conducting its business in an unsafe or injurious manner, to make a final order directing the licensee to comply with the law or discontinue the unsafe or injurious practices, as prescribed. (Fin. Code Sec. 2148.)
- 5) Check Sellers, Bill Payers and Proraters Law (Fin. Code Sec. 12000 et seq.) requires licensing and regulation of persons issuing negotiable instruments and paying bills or obligations on behalf of customers, except certain persons including nonprofit consumer credit counselors; prohibits misrepresentations, fraudulent and deceptive advertising in

connection with these business activities; and provides administrative, civil (injunction and appointment of receiver) and criminal remedies for violations of the law.

If the commissioner finds that a licensee is insolvent or is conducting business in such an unsafe or injurious manner as to render its further operations hazardous to the public, the commissioner may, by order addressed to and served on the licensee and on any other person having the licensee's funds or customer's in their possession, direct discontinuance of the disbursement of those funds and further conduct of business by the licensee. (Fin. Code Sec. 12307.2.)

- 6) The Escrow Law (Fin. Code Sec. 17000 et seq.) requires licensing and regulation of independent escrow companies, except as specified; prohibits misrepresentation, fraudulent and deceptive acts in connection with certain escrow transactions; creates a private indemnity arrangement to protect Licensed escrow companies against specified losses; and provides administrative, civil (injunction, ancillary relief and appointment of receiver) and criminal remedies for violations of the law.

Authorizes the commissioner, upon finding that a person subject to that law is in an insolvent condition, is conducting escrow business in such an unsafe or injurious manner as to render further operations hazardous to the public or to customers, has failed to comply with certain provisions, has permitted its tangible net worth to be lower than the legal required minimum, has failed to maintain its liquid assets in excess of current liabilities, or has failed to comply with bonding requirements, to, by order, take specified steps related to the discontinuance of the disbursement of trust funds and other escrow business operations. (Fin. Code Sec. 17415, 17602, 17603, and 17604.)

- 7) The California Financing Law (Fin. Code Sec. 22000 et seq.) requires licensing and regulation of Finance lenders and brokers making and brokering consumer and commercial loans, except as specified; prohibits misrepresentations, fraudulent and deceptive acts in connection with making and brokering of loans; and provides administrative, civil (injunction and ancillary relief) and criminal remedies for violations of the law.

Authorizes the commissioner, upon having cause to believe that a licensee or other person is violating the CFL, to issue a citation to the licensee or person and to assess an administrative fine, as specified. The commissioner, if, after investigation, the commissioner has reasonable grounds to believe that a person is conducting business in an unsafe or injurious manner, must direct, by written order, the discontinuance of the unsafe or injurious practices.

- 8) The Student Loan Servicing Act (Fin. Code sec. 28100 et seq.) requires licensing and regulation of student loan servicers. Covered servicing includes activity that originated in California and is directed to persons in or outside of California, or originated outside of California and is directed to persons inside California. The statute established state standards to ensure consistent, fair, and quality servicing; and provides administrative and criminal remedies for violations of the law.

Requires the commissioner, upon having reasonable grounds after investigation to believe that a licensee is conducting business in an unsafe or injurious manner, to direct, by written order, the discontinuance of the unsafe or injurious practices. The commissioner may, if, upon the hearing, it appears to the commissioner that the licensee is conducting or has

conducted business in an unsafe and injurious manner or is failing to comply with the act, to make the order of discontinuance of those practices final.

- 9) The California Residential Mortgage Lending Act (Fin. Code Sec. 50000 et seq.) requires licensing and regulation of residential mortgage lenders and servicers of specified federally-regulated mortgage loans, except as specified; prohibits misrepresentations, fraudulent and deceptive acts in connection with making, brokering and servicing of these residential mortgage loans; and provides administrative, civil (injunction, ancillary relief and appointment of receiver) and criminal remedies for violations of the law.

Requires the commissioner, if, after investigation, the commissioner has reasonable grounds to believe that a licensee under the act has violated its articles of incorporation or any law or binding rule, to, by written order, direct the discontinuance of the violation. If the commissioner has reasonable grounds to believe that a licensee is conducting business in an unsafe or injurious manner, then the commissioner may, by written order, direct the discontinuance of the unsafe or injurious practices. (Fin. Code Sec. 50321, 50322, 50323.)

FISCAL EFFECT: Unknown. This bill is keyed Fiscal by Legislative Counsel.

COMMENTS:

1) **Purpose.**

According to the author:

AB 2433 clarifies that when the Department of Financial Protection and Innovation (DFPI) brings an order to discontinue violations against a licensee, the order can be upheld even in cases where the licensee stops violating the law in advance of the hearing. This proposal will hold bad actors accountable and assure greater transparency for consumers.

2) **Background.**

DFPI's Enforcement Division enforces the laws administered by DFPI and has available a number of administrative and legal tools. DFPI's administrative tools include orders to stop violations of the laws, to deny, censure, suspend, revoke or take possession of a license, and to censure, suspend, or bar individuals from participating in a regulated industry. A licensee, person, or business may challenge these orders through the Office of Administrative Hearings (OAH). An Administrative Law Judge (ALJ), who is independent of DFPI, presides over an OAH proceeding in a manner similar to a civil court trial, with each party making an opening statement, offering evidence, and making closing argument.

One function of DFPI's enforcement activity is, in addition to stopping harmful activity, to also create a public record of those licensees who have broken state law. DFPI publishes on its website its actions and orders against licensees as well as the ALJ decisions following an OAH proceeding. Thus, DFPI's list of licensees include information on whether they have

been subject to public action, which provides consumers with important information on whether they should do business with the licensee.¹

3) **What problem does this bill address?**

This bill addresses ambiguities and inconsistencies in DFPI's authority to issue and make final an ODV, which is an administrative action to stop a licensee from violating the law. In 2020, ODVs issued by DFPI were not upheld by the ALJ in two cases, based on the ALJ's reading of the laws governing DFPI's authority.² In these cases, the licensees had stopped the violative conduct prior to the hearings, and current law is ambiguous as to whether an ODV can be made final in these situations.

A deeper look into one of the two cases (Commissioner of Business Oversight v. Bela Capital LLC, OAH No. 2020030213) highlights the undermining impact this ambiguity can have on DFPI's enforcement capabilities. This case involved an investment advisor who did not properly maintain an e-mail address to receive documents and communications from DFPI, as required by the Financial Code, and did not maintain and update required documentation, as required under the Corporations Code. The licensee cured some of these deficiencies prior to the case being heard, and the ALJ notes the following conflict:

Before the Commissioner can make the Order to Discontinue final under Corporations Code section 25251, the Commissioner must find that the respondent "is conducting" business in an unsafe and injurious manner or "is violating" any applicable law or rule binding upon respondent. Unlike the Corporations Code section 25249, drafted in the past tense, Corporations Code section 25251 requires evidence of a present and continuing injurious business practice or an ongoing violation of the law or regulation before ordering an investment adviser to immediately discontinue the practices named in the order.

In response to this inconsistency, AB 2433 updates a number of sections in the Financial Code and the Corporations Code to align ODV authority so that it applies to both the past behavior and current, ongoing behavior. This makes DFPI's authority consistent across its various enforcement and licensure programs.

4) **AB 2433's proposed changes are consistent with other enforcement authorities.**

Importantly, the ambiguities in DFPI's ODV authority do not exist for DFPI's other administrative enforcement actions, such as citations or desist and refrain orders. Existing law grants DFPI the ability to take these other type of enforcement actions for past and present violations. For example:

¹ For more information on DFPI and the administrative hearing process, see <https://dfpi.ca.gov/actions-orders-and-administrative-hearing-decisions/>.

² Commissioner of Business Oversight v. Bela Capital LLC, OAH No. 2020030213, available at <https://dfpi.ca.gov/enf-b/bela-capital-llc/> and Commissioner of Business Oversight V. Ridgegate Escrow, Inc., OAH No. 2019020097, available at <https://dfpi.ca.gov/enf-r/ridgegate-escrow-inc/>

- a) The Corporate Securities Act of 1968 authorizes DFPI to issue an order to desist and refrain for a person that “has engaged, is engaging, or is about to engage in an act, practice, or course of business constitution a violation...”³
- b) The California Consumer Financial Protection Law (CCFPL) states that it is unlawful for a covered person or service provider to “engage, have engaged, or propose to engage in any unlawful, unfair, deceptive, or abusive act or practice with respect to consumer financial products or services,” a definition that is directly tied to DFPI’s authority to issue an order to desist and refrain.⁴
- c) Finally, other areas of the Financial Code and Corporations Code applicable to DFPI’s enforcement authority clearly apply to past conduct, including: Financial Code Section 14304 (a), applying to credit unions and cease and desist orders; Financial Code Section 30606(b), applying to securities depositories and revocation of a license; Financial Code Section 50321, applying to CRMLA licensees.

REGISTERED SUPPORT / OPPOSITION:

Support

California Low-income Consumer Coalition

Opposition

None on file.

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³ Corporations Code Section 25532 (d)

⁴ Financial Code Section 90003 (a)(1)