***Payments Pros – The Payments Law Podcast*: Regulation Through Enforcement: Insights From the BlueSnap Lawsuit**
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Keith Barnett:

Welcome to another episode of *Payments Pros*, a Troutman Pepper Podcast, focusing on the highly regulated and ever-evolving payments industry. This podcast features insights for members of our FinTech and payments practice as well as guest commentary from business leaders and regulatory experts in the payments industry. My name is Keith Barnett, I'm one of the hosts of the podcast.

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Today, I am going to talk about a lawsuit and settlement that the FTC filed against a PayFac. In particular, on May 1st, 2024, the Federal Trade Commission publicly released a complaint and settlement about an enforcement action against a PayFac named BlueSnap, and two of its senior executives arising out of allegations that the PayFac and the executives aided and abetted violations of the Telemarketing Sales Rule by BlueSnap's customer ACRO, which is a debt relief service provider.

The complaint alleges violations of Section Five of the FTC Act, as well. Just also by way of background, these transactions were both credit and debit transactions. Now, let's keep in mind, if you already know about this case, or new information for people who don't know about this case, the Federal Trade Commission had already sued the debt relief service provider in November of 2022. And the final orders were issued in that case, and the FTC's favor in 2023. So here, it's just a lawsuit and settlement against the PayFac that had been involved in the payment processing, the underlying payment processing related to the DRSP's lawsuit. In this particular case, the PayFac agreed to pay the FTC $10 million and stop processing for debt relief service providers. So, they're completely out of that industry.

I want to talk about the allegations concerning the onboarding and ongoing due diligence because these allegations give some insight as to what the FTC is looking for when it investigates processors for debt relief service providers, when the debt relief service providers are believed to violate the Telemarketing Sales Rule, or just some sort of UDAP violation in general.

So, let's first start with the onboarding due diligence allegations and the due diligence of the principals of the debt relief service provider. What I found interesting here are several things. First, the complaint alleges that the PayFac knew before opening the account that consumers have reported being scammed by businesses with the same name when they were trying to cancel timeshares. I know what you're saying. This has nothing to do with timeshares. But follow where I'm going here for a second.

In 2018, according to the complaint, when BlueSnap was conducting underwriting for the merchant account application, BlueSnap searched for the account name that was being submitted as its merchant. So, they searched for that account name online, and found several consumer complaints about companies with the same name. From that, the Federal Trade Commission deduced that it was the same principals running the company under a same name. It's just the company's focus was different.

Now, keep in mind here that these other businesses were not debt relief service providers. These other businesses appeared in the due diligence because of the overlapping principals. Even though these were not government enforcement actions against the DRSP or the principals, the FTC considered this to be significant enough to place in the complaint. So, it's just a reminder of the fact that the FTC looks at everything when it is doing some form of investigation or enforcement action.

The complaint goes on to allege that the debt relief service providers' various entities, and their principals were sued several times for deceptive and fraudulent acts, while BlueSnap was opening the merchant accounts for them, and BlueSnap nonetheless continued to process for them. In the complaint, the FTC gave several examples. Seven to be exact of prior lawsuits against the DRSP and/or the principals of the DRSP.

I looked through all of this and all of these lawsuits were filed by consumers in private complaints. I mean, in other words, it was not a government entity alleging some sort of fraudulent violations by the DRSPs or their principals. These lawsuits did not concern anything that had to do with the FTC's complaint. These lawsuits concerned primarily two things. One, I mentioned the whole timeshare thing earlier, one was a lawsuit concerning a timeshare cancellation issue. Again, that has nothing to do with the debt relief service providing business. And the other lawsuits concerned calling a person without permission in violation of the Telephone Consumer Protection Act.

Once again, the FTC brought up things in its complaint that had nothing to do with the present issue at hand. But it shows that they are looking at everything. In fact, based upon my experience, the regulators, so not only the FTC, but the CFPB, they usually look at government enforcement actions as indicators and not private lawsuits. Here, it appears that the FTC took into account this private litigation as a sign that things may not have been above board with the DRSP. That's just something to also consider for you payment processors or money transmitters or PayFacs out there that might be onboarding DRSPs.

Going on, in the complaint, the FTC also discussed ongoing due diligence and pointed out issues that the FTC believed should have been signs for the PayFac to stop processing for the DRSP after onboarding. The first thing that I want to talk about that was mentioned concerning the ongoing due diligence is the FTC's allegation that throughout the processing relationship, there were high chargeback rates that ranged from 6.39% to over 30%. The FTC goes on to allege that there were numerous emails sent to the PayFac by its processor about the chargeback rates and the response from the PayFac was that they were working to get them down. But according to the complaint, they did not get them down.

The complaint goes on to allege that the merchant was placed on a credit card's fraud monitoring program. At least according to the complaint, the fraud to sales ratio was 17.24% on average, in some months reached up to 40%. The complaint made sure to allege that the threshold for this particular card was 0.90%. So, it was much lower than that 17.24% or up to that 40%.

The complaint went on to allege that the credit card imposed a $75,000 fine on the acquirer bank under the credit card's fraud monitoring program, due to the excessive levels of alleged fraud on a certain account. The PayFac's processor notified the PayFac that it would be responsible for paying that fine. The complaint pointed out that despite notice of the fine, the PayFac did not terminate that particular account that had the alleged excessive levels of fraud.

So, this is not only a message to the PayFac, but this also may be a message to banks and processors in a nested relationship, which is what this appears to be. The FTC uses as a data point fines from the credit card when conducting investigations and filing complaints. In the complaint, the FTC goes on to allege that in addition to all of the warnings based upon the chargebacks and the fraud monitoring programs, the PayFac and its principals were presented with direct evidence that the DRSP services had been, in the FTC's words, defrauding customers and engaging in what the FTC considered to be unlawful activity. And there, the complaint lists several more examples.

For example, when one of, at least according to the complaint, one of the PayFac's principals was reviewing and signing the credit cards fraud monitoring program, remediation plans on behalf of the DRSP, and according to the complaint, the PayFac's principal reviewed direct evidence that the DRSP was engaged in, and I'm quoting here, "unlawful and deceptive practices in connection with the sale of debt relief services via telemarketing."

According to the complaint, the PayFac's principal saw references to the DRSP services website, and a copy of a purported DRSP services customer agreement. According to the complaint, the PayFac's principal saw references to the DRSP's services website, and a copy of the purported DRSP's services customer agreement. According to the complaint, those two things were inconsistent, and according to the FTC, should have been an indication of the "deceptive nature of the business."

I want to go on and say one more thing about the complaint before I give you my thoughts on this. The complaint goes on to say that the website and customer service agreement contradicted each other and even contradict themselves. But by way of example, the complaint alleges that the DRSP's website claimed that the company, "provided financial coaching with coaches certified through the National Association of Certified Credit Counselors." But the customer agreement, according to the complaint, made no mention of financial coaching. That's where I want to stop here, before moving on with respect to other interesting things that I've found in this complaint.

I don't know if you all see what the FTC is doing here. It is defining as contradictory. The act of mentioning this service in one document, and the failure to mention the service in another document. While that's not contradictory to me, it is an indication from the FTC, that this is something to look out for when conducting your onboarding or ongoing due diligence are things mentioned in one document, and not mentioned in another. So, from there, you may want to – it looks like the FTC wants to know the why there. This is just me speculating as to why they felt it was important to put that in the complaint.

So, the complaint goes on to talk about other parts of the website, and advertisements in the website versus the customer agreement. The website advertised whether or not someone needed debt relief, and if so, the debt relief service provider was their “lifeboat.” But the customer agreement itself said that it is, “not for debt relief services.”

I have the same comment as before, right? The FTC is looking for both express and implied contradictions when conducting investigations against payment companies, especially when you're dealing with debt relief service providers, or quite frankly, any other industry that is covered by the Telemarketing Sales Act. The FTC alleges also that the agreement further stated that the company is experienced in disputing debts using federal and state statutory authority. According to the complaint, the company made misleading claims about consumer’s ability to invalidate their debts using this statutory authority.

My comment here is that the FTC is indicating that statements concerning legal issues will also be scrutinized. Keep in mind that this is something that was on the DRSP's website or within their customer agreement. The point I'm trying to make here is that this information was not on the PayFac’s website. It's not in the PayFac’s agreement, but this is raised in the complaint against the PayFac because the FTC saw this as a data point that was indicative of possible violations of the Telemarketing Sales Rule or the FTC Act.

Getting back to the complaint, the complaint also alleges that the agreement also included contradictory claims regarding legal representation, and at one point, describing the scope of legal services provided and what the consumer owed for legal fees, costs, and expenses, while elsewhere in their agreement stating that the company is not a law firm and provides no legal work.

My point in reading that to you all, is same comments as before. The FTC uses what it believes to be contradictory statements as data points for a section five violation, and everything that the FTC sees as being contradictory, no matter how innocuous that might seem to be when looked at alone, the FTC will find all of these things and put them in a complaint so they can tell their story.

Going back to the complaint. Finally, the agreement disclosed that the debt relief service provider was charging advance fees for the debt relief services. Now, the complaint does not actually attach the agreement. But that is what it alleges. As all of us know, who deal with these things, that is a violation of the Telemarketing Sales Rule for a DRSP to take advanced fees for their services. So, this is something for the payment processors and PayFacs to look for when you are providing services for the debt relief service providers.

Now, getting back to the complaint. According to the complaint, one of the principles of the PayFac received multiple emails from a credit card company about the DRSP reportedly scamming consumers. According to the complaint in each email, the credit card company stated that it was “requiring cancellation of this account within 48 hours.” The complaint goes on to allege that the PayFac did not cancel the account within 48 hours and waited a month. Also, according to the complaint, the PayFac’s fraud prevention team obtained what the FTC considered to be direct evidence of consumers being deceived by the debt relief service provider, including at least one recording of a telephone conversation between the DRSP's representative and a consumer.

According to the complaint, in the recording, the DRSP's representative told the consumer that they could "invalidate the consumers credit card debt, and the FTC refer to the statement by the DRSP's representative as an utterly bogus claim." So, that's straight out of the complaint. The FTC's complaint goes on to say that the representative also told the customer that they could provide the service after charging $1,200 to the consumers credit card, which the FTC pointed out is a violation of the Telemarketing Sales Rule prohibition on advanced fees. The complaint also pointed out that online sources reviewed by the PayFac should have been indicative of some sort of notion that the DRSP was not a model for compliance.

More specifically, the complaint alleges that the Better Business Bureau webpage for the debt relief service provider displayed numerous consumer complaints about the company's deceptive promises to resolve or remove credit card debt.

I want to add the comments about this because this is pretty significant to me. And the reason why this is a significant allegation is because online sources such as the Better Business Bureau, these online sources are hearsay. They would not hold up in a regular court of law as indicative of any type of rule violation. And as we know, anyone can write anything about someone on the internet. This is not, for example, a government enforcement action, a pleading that the FTC is using as a data point. These are allegations from people who claim to be customers of the debt relief service provider, but we really do not know who they are. And I also find it ironic that the FTC used this as a data point notwithstanding that the FTC proposed a rule that seeks to broadly prohibit businesses from using anti-consumer review and endorsement practices, such as posting fake reviews, or suppressing negative reviews that might be honest, or paying third parties for positive reviews, while the FTC does not know if these negative reviews are actually legitimate. So, there's a stroke of irony there.

Almost wrapping up here, but I want to bring up a couple of more things. The complaint alleges that a fraud investigator from the bank sponsor made an unannounced visit to the DRSP's headquarters to inquire about millions of dollars in disputed charges involving the bank's card holders. The DRPS's owners then reported the incident to the PayFac's director of fraud strategy, stating that they misled the investigator about whether or not they were actually present. The fraud director then sent an email to the principals of the PayFac warning them about multiple indicators and flags that the DRSP could get shut down for illegal activity. The PayFac's director of fraud strategy, allegedly further reported that he had listened to consumer call recordings with the DRSP, where, according to the complaint, this director of fraud strategy said that he heard that the DRSP purposefully speak fast and make confusing for senior citizens, one of which did not give his authorization to make a purchase.

So, finally, the complaint alleges that the PayFac only stopped processing for the DRSP when other payment processors and credit card networks forced it to stop. They did not just do it on their own.

I want to reiterate here in closing, that the purpose of discussing this enforcement action during this podcast is to remind the payment processors, money transmitters, and the PayFacs, and others along the payments continuum, that the FTC is looking at certain things that you may not be thinking about during the onboarding process with respect to due diligence or even ongoing due diligence. Even though the DOJ stated several years ago, that operation choke point was over, this enforcement action and other enforcement actions against processors arising out of the conduct of their customers, indicates that the federal regulators expect processors to stop processing under certain circumstances, including the ones raised in this enforcement action that I just discussed.

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