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CREDIT REPAIR CLOUD, AND DANIEL ROSEN

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

WESTERN DIVISION

CONSUMER FINANCIAL PROTECTION BUREAU,

Plaintiff,

v.

DANIEL A. ROSEN, INC., D/B/A CREDIT REPAIR CLOUD, AND DANIEL ROSEN,

Defendants.

Case No.: 2:21-cv-07492 VAP (JDEx)

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS PLAINTIFF'S COMPLAINT

Date: February 14, 2022
Time: 2:00 p.m.
Location: Courtroom 8A, 8th Floor
350 West 1st Street
Los Angeles, CA 90012
Judge: Honorable Virginia A Phillips

Complaint Filed: September 20, 2021
Trial Date: None Set

TABLE OF CONTENTS

Page(s)

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Other Authorities

I. INTRODUCTION

This lawsuit is an exercise in enforcement overreach by the Consumer Financial Protection Bureau ("CFPB" or "Plaintiff"). Defendants Credit Repair Cloud ("CRC") and Daniel Rosen ("Mr. Rosen") operate a law-abiding business that does nothing more than provide word processing and customer management software along with educational resources to small credit repair businesses, none of which the CFPB has specifically accused of violating the Telemarketing Sales Rule ("TSR"). Nevertheless, the CFPB has gone beyond its statutory authority and filed a Complaint that fails to allege sufficient facts to give Defendants fair notice of a legally cognizable claim and the grounds on which it rests. The Court should be vigilant from the outset of the CFPB's jurisdictional overreach and failure to comply with the pleading requirements of Rule 8.

As a threshold matter, the CFPB does not have authority to enforce the TSR against Defendants because they are neither a "covered person," nor "service provider," and the product/services at issue are not a "consumer financial product or service," as defined under 12 U.S.C. § 5481. CRC is a software company that provides business owners access to software and educational resources to build and operate a credit repair business. CRC does not provide any type of financial product or service to consumers. Moreover, CRC does not participate in designing, operating, or maintaining a consumer financial product or service.

Second, the Complaint fails to state a plausible claim for relief. The CFPB fails to plead the well-settled elements of what is, in essence, an aiding and abetting claim. The Complaint does not (1) identify a specific CRC User that allegedly violated the TSR or any precise primary violation to which any secondary liability may attach; (2) allege facts demonstrating how CRC's software or educational resources rise to the level of providing "substantial assistance or support" to any specific CRC User allegedly violation the TSR; and (3) allege facts establishing that

Defendants knew or consciously avoided knowing that a specific CRC User is violating the TSR. The Complaint plainly fails to allege any facts sufficient to state a plausible claim or to give Defendants notice of the nature and grounds of the claims asserted against them.

Third, the CFPB's claims cannot proceed because the Credit Repair Organization Act's ("CROA") statutory provision regarding payment terms for credit repair businesses trumps the application of the TSR's "advance fee" rule in the credit repair industry.

This is not the first time the CFPB has filed a lawsuit that lacked any basis in fact. In *Consumer Fin. Prot. Bureau v. Universal Debt Solutions, LLC*, No. 1:15-CV-859-RWS, 2017 WL 3887187 (N.D. Ga. Aug. 25, 2017), the district court struck four counts from the complaint, including two counts against five defendants for substantial assistance in violation of the Consumer Financial Protection Act (the "CFPA") – a legally similar claim to Counts I and II asserted against Defendants here. The district court found that

> the CFPB willfully violated the Court's repeated instructions to identify for Defendants the factual bases for its claims and that, in each deposition, it willfully failed to present a knowledgeable 30(b)(6) witness. In light of the CFPB's pattern of conduct in this case, the Court is not optimistic that reopening the depositions would be fruitful. That is especially true given the CFPB's continued use of privilege objections in response to questions that the Court expressly identified as permissible.

Id. at *8.

That order was issued almost two and a half years into the case, long after the CFPB had pleaded a bare-bones complaint and then refused to provide the evidence upon which they supposedly brought the case. The Complaint here already falls short of alleging facts sufficient to render the CFPB's claims plausible. If the Court allows the CFPB's factually deficient Complaint to proceed, Defendants will be forced to

endure the same harassment and exorbitant costs of litigation that the five businesses faced at the hands of the CFPB in *Universal Debt*.[1]

Because the CFPB cannot state a claim under any of its three counts and will not be able to cure those defects, the Complaint should be dismissed with prejudice.

II. FACTUAL BACKGROUND

A. Daniel Rosen and Credit Repair Cloud

Daniel Rosen, is the Founder and CEO of CRC. When a bank error ruined Mr. Rosen's credit and nearly devastated his life, he was inspired to create a software that would help to empower people who were facing challenges with their credit. In 2013, Mr. Rosen founded CRC, a company that creates, develops, and markets software designed to address the needs of small credit repair businesses (the "Software").

As alleged in the Complaint, the Software allows users to track and organize customer details and activity, including customer names, contact information, the date they signed up for credit repair services, and whether customers are up-to-date on their payments for credit repair services. Compl. ¶ 14. The Software allows CRC Users to import and review their customers' credit reports, and the Software will automatically flag negative items on customers' credit reports for Users. *Id.* ¶ 15. The Software contains a database of over 100 template-dispute letters that the Software will automatically pre-populate with customer information. *Id.* ¶ 16. The Software allows CRC Users to track whether a particular disputed item on a consumer's credit report has been validated, whether it has been found to be inaccurate or incomplete or whether it cannot be verified. *Id.* ¶ 17. The Software also contains template contracts for CRC Users to supply to their customers. *Id.* ¶ 18. The Software does not have a built in phone dialer and does not provide a billing

[1] Indeed, this lawsuit and a related press release published by the CFPB has already damaged Defendants' reputation, hurt the business and caused them to incur thousands of dollars in legal fees.

platform. *See Id*. ¶¶ 11-21. CRC's Software has empowered people from virtually all walks of life to launch, run, and grow their own credit repair business, including from their home, and often as a side business.

B. CRC Users

CRC Users are credit repair businesses that purchase credit repair business software and other tools from CRC. Compl. ¶ 6. CRC's Users are 60% women and 80% people of color. Many are single mothers and many have been homeless in their lives. CRC Users are not large companies in the credit repair space with rooms full of telemarketers calling people they have never met. To the contrary, CRC Users are tiny mom and pop companies located in the communities that they serve and that generate business in person (such as by networking through friends, professional groups or other local businesses, speaking at local community gatherings, and the like). To illustrate how small these businesses are: 80% of CRC's user base is likely making less than $48,000/year and 68% of the paid user base is likely making less than $24,000/year.

C. Plaintiff's Allegations

In relevant part, the CFPB alleges that "[a]t least *some, and likely many*, Users are engaged in telemarketing" (Compl. ¶ 32), and "[a]t least *some, and likely many*, Users have been charging fees to consumers well in advance of the waiting period imposed by the TSR." Compl. ¶ 33. However, despite being premised upon assisting and facilitating violations of the TSR's "advance fee" rule, the Complaint does not allege that: (a) CRC provides a dialer platform or otherwise offer the ability to initiate or answer telephone calls; (b) CRC processes payments; (c) CRC offers assistance in requesting or collecting payments; (d) CRC conducts business with or interacts with consumers; (e) CRC provides credit repair services; (f) any identified CRC User engages in telemarketing; (g) any identified CRC User demanded or charged payment in alleged violation of the TSR; (h) CRC knows or was reckless in

not learning any identified CRC User engaged in telemarketing; or (i) CRC knows or was reckless in not learning any identified CRC User demanded or charged payment in alleged violation of the TSR and also charges advance fees.

III. THE CFPB HAS NO AUTHORITY OVER DEFENDANTS

As an initial matter, the Complaint should be dismissed because the CFPB does not have authority to file an enforcement action against Defendants. "Agencies cannot exceed the scope of their authority as circumscribed by Congress." *Planned Parenthood of Greater Washington & N. Idaho v. U.S. Dep't of Health & Human Servs.*, 946 F.3d 1100, 1112 (9th Cir. 2020). "[A]n agency literally has no power to act . . . unless and until Congress confers power upon it." *La. Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 374 (1986). Thus, when agencies "act beyond their jurisdiction, what they do is ultra vires." *City of Arlington, Tex. v. F.C.C.*, 569 U.S. 290, 297 (2013). That is the case here.

The CFPB's authority is limited. While "the Bureau may enforce a rule prescribed under the Federal Trade Commission Act," such as the TSR, "as if it were a rule prescribed under section 5531 of this title," its enforcement power is limited "to the extent that such rule applies to a covered person or service provider with respect to the offering or provision of a consumer financial product or service . . . ." 12 U.S.C. § 5581(b)(5)(B)(ii); 12 U.S.C. § 5531(a); *see also* 12 U.S.C. §§ 5511, 5481(14) (further defining the laws under CFPB's jurisdiction). This case does not involve a "covered person," "service provider," or a "consumer financial product or service" as defined under 12 U.S.C. § 5481.

A. Neither Defendants Nor CRC Users Are a "Covered Person"

Count III of the Complaint alleges in a conclusory fashion that the CRC Users are "covered persons." Compl. at ¶ 84.[2] Yet none of the factual allegations in the

[2] The CFPB does not allege that either Defendant is a "covered person," nor could it. Defendants do not, and are not alleged to, offer or provide any financial products or

Complaint support that conclusion. *See* Compl. at ¶¶ 8, 9, 31-32, 33, 36 (alleging CRC Users offer "credit-repair services"). A "covered person" is defined as "any person that engages in offering or providing a consumer financial product or service" or an "affiliate" of such a person. 12 U.S.C. § 5481(6). A "consumer financial product or service," in turn, is defined to include an array of products or services that are set out in the CFPA, which include loans, extending credit, engaging in deposit taking activity, providing financial advisory services, debt management, debt settlement, or collection of debt. *See* 12 U.S.C. §§ 5481(5) & (15).

To shoehorn the conduct of CRC Users within the statutory definition of "consumer financial product or service," and thus within the CFPB's jurisdiction, the CFPB alleges in conclusory fashion that the CRC Users provide "financial-advisory services, including credit counseling," as well as "collecting, analyzing, maintaining, or providing consumer report information or other account information, including information relating to the credit history of consumers . . . ." Compl. at ¶ 84 (citing 12 U.S.C. § 5481(15)(A)(viii) & (ix)). Taking the factual allegations in the Complaint as true, CRC Users do not provide such financial advisory services.

First, as alleged in the Complaint, CRC Users provide consumers "credit-repair services," not "credit counseling" *See* Compl. at ¶¶ 8, 9, 31-32, 33, 36.[3] Second, "collecting, analyzing, maintaining, or providing consumer report information or other account information, including information relating to the credit history of consumers" qualifies as a "consumer financial product or service" ***only if*** the information was "used or expected to be used in connection with any decision regarding the offering or provision of a consumer financial product or service . . . ."

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services, and certainly not to consumers. *See generally* Complaint. Instead, the Complaint alleges that Defendants are "service providers." Compl. at ¶ 85.

[3] "Courts have noted that the CROA makes a distinction between 'credit counseling' services, which are prospective in nature, and 'credit repair' services," which apply "retrospectively" to "past credit sins." *Jackson v. Tel. Chrysler Jeep, Inc.*, No. 07-10489, 2009 WL 928224, *6 (E.D. Mich. Mar. 31, 2009).

12 U.S.C. § 5481(15)(A)(ix). The Complaint does not allege that CRC Users used or expected any credit history information to be used in that manner. Instead, the Complaint alleges that "CRC Users" offer credit repair services in the nature of "challeng[ing] or disput[ing] negative items that appear on consumer reports on consumers' behalf." Compl. at ¶ 9. Those services alone do not qualify as a "consumer financial product or service" as defined under 12 U.S.C. §§ 5481(5) & (15). Accordingly, CRC Users are not "covered persons" under the TSR.

B. Defendants Are Not "Service Providers" Under 12 U.S.C. § 5481

Furthermore, neither CRC nor Rosen is a "service provider" as defined by the TSR. The definition of "service provider" includes a person that "(i) participates in designing, operating, or maintaining the consumer financial product or service. 12 U.S.C. § 5481(26). In a conclusory fashion, the CFPB alleges both CRC and Rosen are service providers because they "participate in designing, operating, or maintaining CRC Users' provision of credit-repair services." *See* Compl. at ¶ 85. However, as discussed above, the credit repair services provided by CRC Users are not consumer financial products or services.

Notably, Congress expressly excluded from the definition of "service provider" a "person offering or providing to a covered person a support service of a type provided to businesses generally or a similar ministerial service . . . ." *Id.* at § 5481(26)(B)(i). "The plain meaning of the term 'ministerial' describes 'an act that involves obedience to instructions or laws instead of discretion, judgment, or skill.'" *Consumer Fin. Prot. Bureau v. Universal Debt & Payment Sols.*, LLC, No. 1:15-CV-00859-RWS, 2015 WL 11439178, *16 (N.D. Ga. Sept. 1, 2015) (quoting "Ministerial," *Black's Law Dictionary* 1086 (9th ed. 2009)). The court in *Universal Debt* held that because the defendant "performed underwriting and screening services and was supposed to monitor for risk," its "duties involved discretion, judgment, and skill," and thus did not qualify for this exemption as a matter of law. Another court,

from this District, similarly ruled that because the defendant broker for short-term and payday lenders was obligated under CFPB guidance "to vet and monitor 'covered persons,' like the lenders with which it does business," it failed to qualify for the "support service" exemption. *CFPB v. D & D Mktg*., No. CV 15-9692 PSG (EX), 2016 WL 8849698, *2, 8 (C.D. Cal. Nov. 17, 2016).

Here, Defendants do not provide any of the services provided by defendants in *D & D Mktg.* and *Universal Debt*. To the contrary, CRC provides the exact type of "support service" – software that is generally provided to businesses to organize their customers – that Congress expressly exempted from the definition of "service provider" to avoid overreach. *See* Compl. at ¶¶ 14-20. Unlike in *D & D Mktg*, Defendants do not have the obligation to vet and monitor any CRC Users. And unlike in *Universal Debt* Defendants are not providing underwriting or any other screening service. Instead, Defendants operate like Microsoft, which is under no obligation to vet and monitor how any licensed user uses Microsoft Word, Outlook, Excel or its database management software, Access.

Because Defendants are not "covered persons," or "service providers," and this case does not involve provision of a "consumer financial product or service," the CFPB does not have the authority to assert any claims against Defendants. The Complaint must be dismissed on this ground alone.

IV. THE COMPLAINT FAILS TO STATE A CLAIM FOR RELIEF

Even if this Court finds that the CFPB has the authority to proceed with this action, the Complaint should be dismissed for failure to state a plausible claim for relief against Defendants. It is axiomatic that a complaint must allege facts sufficient to "to give the defendant fair notice of what the . . . claim is and the grounds upon which it rests . . . ." *Bell v. Twombly*, 550 U.S. at 555 (2007) (internal quotation omitted). "To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its

face.'" *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quoting *Twombly*, 550 U.S. at 555). "A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Id.* This standard "asks for more than a sheer possibility that a defendant has acted unlawfully." *Id.* Each of the three claims in the Complaint falls well short of this requirement.

A. Counts I and II Fail to State a Claim for Relief

Count I of the Complaint asserts a claim against CRC for "provid[ing] substantial assistance or support to CRC Users" in violation of 16 C.F.R. § 310.3(b) and asserts the claim derivatively against Rosen as a control person of CRC. *See* Compl. at ¶¶ 66-74. Count II of the Complaint asserts the same claim directly against Rosen. *See id.* at ¶¶ 75-80. Both counts fail to state a plausible claim for relief.

The TSR prohibits a person from "provid[ing] substantial assistance or support to any seller or telemarketer when that person knows or consciously avoids knowing that the seller or telemarketer is engaged in any act or practice that violates §§ 310.3(a), (c), or (d), or § 310.4." 16 C.F.R. § 310.3(b). To state such a claim, the CFPB must allege three elements: "(1) there must be an underlying violation of the TSR; (2) the person must provide substantial assistance or support to the seller or telemarketer violating the TSR; and (3) the person must know or consciously avoid knowing that the seller or telemarketer is violating the TSR." *Fed. Trade Comm'n v. Lake*, 181 F. Supp. 3d 692, 700–01 (C.D. Cal. 2016). The FTC has taken the position that aider-abettor principles from securities laws apply to substantial assistance claims under the TSR, and the courts have agreed, in part because that kind of claim has the same elements. *See Fed. Trade Comm'n v. WV Universal Mgmt., LLC*, 877 F.3d 1234, 1240-41 (11th Cir. 2017). *Cf., e.g., Ponce v. Sec. & Exch. Comm'n*, 345 F.3d 722, 737 (9th Cir. 2003) (stating elements for aiding and abetting liability under securities laws). None of the elements is sufficiently alleged here.

1. The CFPB Does Not Allege an Underlying Violation of the TSR

The CFPB has not sufficiently alleged a single underlying violation of the TSR. While the CFPB broadly alleges that CRC Users have requested and received fees in violation of the TSR's "advance fee" rule, (16 C.F.R. § 310.4(a)(2)), remarkably, it does not identify even one such CRC User or a single violation of the TSR. Instead, the Complaint is riddled with vague and conclusory references to the alleged conduct of "[a]t least some, and likely many, Users," or just "CRC Users" as an undifferentiated group. *See, e.g.*, Compl. at ¶¶ 32, 33, 48. Such vague and conclusory allegations of primary violations *per se* fail to state a plausible claim or give Defendants notice of the claims asserted against them.

It is black letter law that "aiding and abetting pleadings should specifically reference the primary violations allegedly aided or abetted." *Reingold v. Deloitte Haskins & Sells*, 599 F. Supp. 1241, 1270 (S.D.N.Y. 1984). The Complaint fails to identify any specific violation of the TSR (or even a specific wrongdoer) for whom secondary liability should attach. As such, Defendants cannot possibly defend against the accusation that they should be held secondarily liable for knowing about and aiding and abetting a purported violation of the TSR. Counts I and II of the Complaint should be dismissed for this reason alone. *See United States Sec. & Exch. Comm'n v. Wey*, 246 F. Supp. 3d 894, 927–28 (S.D.N.Y. 2017) (dismissing aiding and abetting securities claims where the complaint "does not identify which primary violations Uchimoto allegedly knew about"); *In re WorldCom, Inc. Sec. Litig.*, No. 02 CIV.3288(DLC), 2006 WL 1047a130, at *5 (S.D.N.Y. Apr. 21, 2006) ("Without the identification and adequate pleading of the underlying substantive violation of Section 33A . . ., there is no liability for aiding and abetting that violation. Because IQ Holdings has not pleaded a violation of Section 33A, neither Andersen nor any

other defendant named in Count VII can be held liable for aiding and abetting that violation.").

2. The CFPB Fails to Allege Substantial Assistance

Under securities law (and by extension TSR) aiding and abetting principles, "substantial assistance" requires evidence that "the defendant in some sort associated himself with the venture, that he participated in it as in something that he wished to bring about, and that he sought by his action to make it succeed." *Sec. & Exch. Comm'n v. Apuzzo*, 689 F.3d 204, 206 (2d Cir. 2012) (cleaned up). *See also D & D Mktg.*, 2016 WL 8849698 at *12. The Complaint does not allege that Defendants engaged in any such conduct or had any such involvement. Defendants operate a business that allows people to more efficiently run *their own* credit repair business, even from their home. Defendants are not alleged to (nor do they) associate themselves with any venture, perform any credit repair work, interact with any credit repair end-users/consumers, provide telemarketing support, or provide payment processing services. Indeed, the Complaint alleges separate third-party billing is required for CRC Users to set up billing for their customers. Compl. at ¶ 19. Defendants have arms-length relationships with other businesses whereby CRC provides software and web hosting in exchange for a monthly fee. CRC does not partner or associate itself with any CRC User to ensure the success of any type of billing arrangement in connection with telemarketing or otherwise.

In fact, the Complaint never identifies any specific or particular venture, so it is unclear to whom or for what the substantial assistance of any TSR violation would have been provided. All that is alleged on this issue is the following:

> CRC . . . provid[ed] CRC Users with telemarketing scripts; template marketing materials; training on credit repair; advice on how and when to collect fees; and the Software, which automatically flags negative items on consumers' credit reports, generates pre-populated dispute letters, integrates with other companies' subscription-billing systems to facilitate the collection of advance fees, and includes a CRM system.
>
> * * * * *

> Rosen . . . conduct[ed] training on how to use the Software, how to convert prospective customers to paying customers, and how much to charge customers; email[ed] CRC Users with tips on how to remove items from consumers' credit reports; and provid[ed] CRC Users with telemarketing scripts and advice on how and when to collect fees.

Compl. at ¶¶ 69, 78. In other words, Defendants provided software, a customer management system, and training to credit repair business customers for ***their*** use in ***their*** lawful credit repair businesses. CRC and Rosen did not associate with or participate in telemarketing or any billing or charging. The Complaint expressly alleges third-party billing platforms were required for that. *See* Compl. at ¶ 19.

Thus, to the extent some (unspecified) CRC Users may have allegedly used the Software or other CRC goods or services to violate the TSR – something that is never plausibly alleged – such use would be no more incidental to any alleged TSR violation than the dialing platform, telephone service, or billing system used in that hypothetical (none of which Defendants are alleged to have provided). "Assistance" of that minimal nature is far from what courts or the FTC have deemed sufficient to allege substantial assistance of a violation of the TSR or other law. *See, e.g.*, *Fed. Trade Comm'n v. Chapman*, 714 F.3d 1211, 1216-17 (10th Cir. 2013) (finding defendant provided substantial assistance of violation of TSR where "she was the one who provided the services and products [the other defendants] marketed to consumers in misleading ways"); *Apuzzo*, 689 F.3d at 214 (defendant chief financial officer negotiated, approved, and signed agreements that were part of fraudulent accounting scheme); *Levine v. Diamanthuset, Inc.*, 950 F.2d 1478, 1484 (9th Cir. 1991) (defendant provided substantial assistance by "issu[ing] confirmations to investors which deceptively repeated the value of the diamonds originally attributed to them by Investia"); *Sec. & Exch. Comm'n v. Premier Holding Corp.*, No. CV1800813CJCKESX, 2019 WL 8167920, *7 (C.D. Cal. Dec. 10, 2019) ("By preparing and filing Premier Holding's Forms 10-K and 10-Q—both of which contained the materially misleading $869,000 preliminary valuation—Greenblatt

associated himself with the violation, participated in it, and sought to make it succeed."); *Federal Trade Commission v. Lake*, 181 F. Supp. 3d 692, 699-700, 701 (C.D. Cal. 2016) (defendant interacted with consumers and performed the contracted-for mortgage assistance relief services).

Although not squarely stated, the Complaint suggests that Defendants' substantial assistance was in the form of ***not*** "instruct[ing] or encourag[ing] Users to wait to charge fees until after they have provided the consumer a consumer report, issued more than six months after the promised results have been achieved." Compl. at ¶ 44. This omission-based theory fails to state a substantial assistance claim as a matter of law because while "[a]n aider and abettor may be liable . . . even though his assistance of the scheme consists of mere silence or inaction," "[t]hat liability arises, however, only when a duty to disclose has arisen." *Strong v. France*, 474 F. 2d 747, 752 (9th Cir. 1973). The CFPB alleges no such duty between Defendants and the CRC Users, nor could it. Defendants transacted business at an arms-length basis with the CRC Users. Thus, this theory of "substantial assistance by silence" also fails to state a plausible claim.

The CFPB's references to statements in Rosen's "blog posts," "book," and "podcast" also fail to establish substantial assistance. *See* Compl. at ¶¶ 28-29, 38, 49-50. These are all instances of free speech protected by the First Amendment that cannot furnish the basis for liability. Rosen's opinions about optimal approaches and strategies for credit repair businesses concern lawful activity and are not misleading – credit repair businesses can charge enrollment and monthly performance fees, (15 U.S.C. § 1679b(b)) – and are protected under the First Amendment even though they are a form of commercial speech. *See Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n of N.Y.*, 447 U.S. 557 (1980). *See also L. G. Balfour Co. v. F. T. C.*, 442 F.2d 1, 24 (7th Cir. 1971) ("The Commission may, of course, prohibit false statements or true statements which in total effect are misleading. But, the

Commission may not prohibit the telling of a true statement even if that representation perpetuates the dominance of a monopolist.") (internal citations omitted).

As the Third Circuit observed eighty years ago in vacating a cease and desist order issued by the FTC prohibiting the dissemination of pamphlets against the use of aluminum utensils as poisonous, "[s]urely Congress did not intend to authorize the Federal Trade Commission to foreclose expression of honest opinion in the course of one's business of voicing opinion." *Sci. Mfg. Co. v. Fed. Trade Comm'n*, 124 F.2d 640, 644 (3d Cir. 1941). Indeed, given the First Amendment issues, the FTC for decades had a policy of not challenging advertising claims that promoted the sale of books or other publications when they mirrored the opinion of the author or quoted the contents of the book or publication. *See Advertising in Books: Enforcement Policy*, 36 Fed. Reg. 13414 (July 21, 1971).[4] Just as such statements cannot form the basis of a claim for deceptive or misleading advertising under the FTC Act, they also cannot serve as the basis for establishing the "substantial assistance" element of an aiding and abetting claim under the TSR.

3. The CFPB Fails to Allege Knowledge or Conscious Avoidance

The Complaint also fails to plausibly allege that either CRC or Rosen knew or consciously avoided knowledge of a (unidentified) violation of the TSR. The CFPB alleges such knowledge only in vague and conclusory terms regarding some unnamed "CRC Users." *See* Compl. at ¶¶ 51-55, 70, 79. The Complaint merely states that: (1) Defendants know that some unnamed CRC Users "conduct telephone sales calls with consumers in more than one state," (*id.* at ¶ 53); and (2) Defendants know some

[4] This policy was known as the "mirror image" doctrine, and it was rescinded only because the FTC deemed it "unnecessary in light of the Supreme Court's commercial speech jurisprudence developed since the [doctrine's] adoption" because "[t]he Court's commercial speech cases, not the [doctrine], delimit the constitutional constraints on challenges to deceptive advertising claims for books and other publications that are commercially marketed." *Advertising in Books: Enforcement Policy*, 74 Fed. Reg. 8542 (Feb. 25, 2009).

unidentified CRC Users charge "advance fees." *Id.* at ¶ 54. Significantly, nothing in the Complaint plausibly alleges that Defendants know that even one "CRC User" – again, none is ever named – does ***both***. Moreover, it appears that the CFPB posits such disjointed knowledge from the implausible contention that Defendants can, "[t]hrough the back-end of the Software," intrude upon private and confidential information posted in the Software to learn everything about a consumer's file and the CRC User that the consumer pays for credit repair services. Given the numerous privacy and consumer protection considerations that apply to consumer financial information, the CFPB's assertion that CRC and Rosen should simply have reviewed – without any plausibly stated warning flags – any credit repair customer's information defies common sense and cannot be credited. *See Iqbal*, 556 U.S. at 679 ("Determining whether a complaint states a plausible claim for relief will . . . be a context-specific task that requires the reviewing court to draw on its judicial experience and common sense.").

In any event, "aiding and abetting liability cannot rest on the proposition that the person 'should have known' he was assisting violations of the securities laws" or any other relevant law. *Premier Holding*, 2019 WL 8167920 at *6 (quoting *Howard v. S.E.C.*, 376 F.3d 1136, 1143 (D.C. Cir. 2004)). Either actual knowledge or recklessness – *i.e.*, conscious avoidance of knowledge – must be shown. *Id.* Recklessness in this context is "a highly unreasonable omission, involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger" of a violation of law "that is either known to the defendant or is so obvious that the actor must have been aware of it." *Id.* (quoting *Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1569 (9th Cir. 1990)).

The Complaint does not allege anything approaching the recklessness standard. The vague allegations that Defendants knew that "some CRC Users" charged enrollment and monthly performance fees and that "some" – not necessarily the same

– CRC Users engaged in telephone sales calls are insufficient. Even those calls, however, are not subject to the TSR's "advance fee," only upon success rule if a "face-to-face" presentation precedes the signing of any credit repair services contract. *See* 16 C.F.R. § 310.6(b)(3). Nothing in the Complaint plausibly alleges that the "face-to-face" exemption obviously did not apply or that Defendants knew or engaged in highly unreasonable conduct to avoid knowing there were no "face-to-face" presentations so as to raise a warning flag for Defendants of TSR violations. Indeed, the Complaint does not even allege that Defendants received any complaints from consumers that they had been charged "advance fees" improperly. Thus, even assuming the Complaint's sparse allegations are true, that would not trigger "the conscious-avoidance concept," which

> is used where a "defendant was aware of a high probability of the [relevant] fact . . . and consciously avoided confirming that fact." Most of the facts that [P]laintiff[ ] deem[s] so "suspicious" that the [Defendants] should be found to have known, "and/or" to have consciously avoided knowing, that [unnamed and disparate CRC Users] w[ere] engaged in [TSR violations] are instead quite commonplace.

Krys v. Pigott, 749 F.3d 117, 132 (2d Cir. 2014) (finding that each short-term loan was for a large amount in round figures that increased over time and had identified repayment dates was "entirely consistent with normal, lawful business practices") (quoting *United States v. Ebbers*, 458 F.3d 110, 124 (2d Cir. 2006)).

Moreover, the Complaint does not identify any specific violation or violator that Defendants know of, or have consciously avoided knowing of. Defendants' choice to not go snooping through entries in the Software in the absence of any red flags can hardly be deemed "an extreme departure from the standards of ordinary care . . . ." so as to give rise to conscious avoidance of knowing about a TSR violation. *Hollinger*, 914 F.2d at 1569.[5] The CFPB generally alleges that Defendants

[5] It would not strain credulity to suggest that a government agency, perhaps even the CFPB, would take issue with a software provider and data host, absent any specific or particular cause, combing through customer entries containing personal and sensitive

could have snooped through the data in the Software to learn these generally alleged violations, presumably by reading every entry by every CRC User since, again, no specific primary violator is ever suggested in the Complaint. But simply having access to software that could be combed through to find indicia of violations is not enough to impute knowledge on the software provider, especially when the data is understandably confidential, private, and sensitive. *Cf. Solomon v. Peat, Marwick, Main & Co.*, 976 F.2d 738, *4 & n.3 (9th Cir. 1992) (unpublished opinion) (holding evidence that defendant re-wrote and improved client's accounting software did not "show that [defendant] knew of [client's] fraud" or consciously avoided knowledge of it). Moreover, the data in the Software does not identify whether CRC Users are meeting with their customers over the phone, zoom, or in person. The Software does not record how CRC Users communicate with their current or prospective customers.

B. Count III Fails to State a Claim

Plaintiff's third count arises under the CFPA, which makes it "unlawful for any covered person or service provider to offer or provide to a consumer a financial product or service not in conformity with Federal consumer financial law, or otherwise commit any act or omission in violation of a Federal consumer law." 12 U.S.C. § 5536(a)(1)(A). Count III is premised on the allegation that CRC and Rosen are "service providers," and their alleged "violations of the TSR, described in Counts I and II." Compl. at ¶¶ 85-87.

Count III fails for two independent reasons. First, because the Complaint fails to state a plausible claim for relief in Counts I or II, the derivative Count III must also fail. *See e.g., Consumer Fin. Prot. Bureau v. Prime Mktg. Holdings, LLC,* No. CV1607111BROJEMX, 2016 WL 10516097, at *7 (C.D. Cal. Nov. 15, 2016) (holding plaintiff's CFPA claim fails because it is tethered entirely to the TSR claims,

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financial information without the consent of the business customer that posted the data onto the database or that of the consumer.

which also fail). Second, even if Counts I or II survive, the CFPA claim fails because Defendants are not "service providers" and the CRC Users are not "covered persons." *See* discussion at 6-8, *supra*.

V. THE CLAIMS SHOULD ALSO BE DISMISSED BECAUSE THE TSR, UPON WHICH THEY ARE BASED, IS TRUMPED BY CROA

The claims against Defendant are also due to be dismissed because the regulatory rule upon which they are based, the TSR, is in conflict with and trumped by CROA, a ***statute*** that specifies the use of written contracts with payment terms disclosed and that expressly permits credit repair organizations to bill in the manner being challenged by the CFPB, *i.e.*, as the charged services are performed, including on a monthly basis. *See* 15 U.S.C. § 1679b(b).

"[A] regulation does not trump an otherwise applicable statute unless the regulation's enabling statute so provides." *United States v. Maes*, 546 F.3d 1066, 1068 (9th Cir. 2008). *See also, e.g.*, *Texas v. E.P.A.*, 726 F.3d 180, 195 (D.C. Cir. 2013) ("A valid statute always prevails over a conflicting regulation, and a regulation can never trump the plain meaning of a statute.") (internal quotations and brackets omitted). "A federal regulation in conflict with a federal statute is *invalid* as a matter of law." *In re Watson*, 161 F.3d 593, 598 (9th Cir. 1998).

The "advance fee" and only upon success provision of the TSR, a regulation issued by the FTC, conflicts with CROA. The TSR prohibits, as an "abusive telemarketing act or practice,"

> [r]equesting or receiving payment of any fee or consideration for goods or services represented to remove derogatory information from, or improve, a person's credit history, credit record, or credit rating until [t]he seller has provided the person with documentation in the form of a consumer report from a consumer reporting agency demonstrating that the promised results have been achieved, *such report having been issued more than six months after the results were achieved*.

16 C.F.R. § 310.4(a)(2)(ii) (emphasis added). That effectively means a credit repair business cannot seek payment for credit repair services obtained by telemarketing

until *at least six months* after those services have been rendered, *and only if those services are successful*. A credit reporter or credit reporting agency, of course, can deny a dispute. *See generally* 15 U.S.C. § 1681i. Even if a consumer fails to provide the credit repair organization accurate information, and that company relies on the consumer to fulfill the promised services, it may be penalized through no fault of its own and not be able to collect a fee for the services it rendered.

In drafting CROA (which was after the TSR was issued), Congress elected not to adopt the TSR's approach. Congress expressly provided for a totally different set of rules as to how credit repair organizations may bill the work they perform and how that must be disclosed in writing in the service contract. CROA provides that "[n]o credit repair organization may charge or receive any money or other valuable consideration for the performance of any service which the credit repair organization has agreed to perform for any consumer *before such service is fully performed*." 15 U.S.C. § 1679b(b) (emphasis added). *See also* 15 U.S.C. § 1679d(b) (specifying written contract requirements). Congress did not require the passage of six months' time, nor did it require credit repair businesses to be paid only upon a successful result. CROA's provisions that allow billing for services upon performance trump the TSR's six months "advance fee," only upon success rule.

Indeed, members of Congress highlighted this conflict and confirmed Congress's intent in a letter to the CFPB. *See* Request for Judicial Notice ("RJN") Ex. A. These members observed that while "the Federal Trade Commission, which enforces CROA, instructed credit repair organizations (CROs) and consumers that CROA is the law of the land with respect to billing regulations," the CFPB "now attempts to subject credit repair organizations to an interpretation of a single clause in the [TSR], which was implemented via rulemaking process by the FTC and before Congress passed CROA." *Id.* They wrote, "[t]hese dueling mandates seem contradictory; with CROA's standard being the most recent and derived from

congressional authority, one would assume ***with regard to CROs, the TSR is no longer operative*** . . . ." *Id.* (emphasis added).

The fact that only CROA can be said to reflect any Congressional intent further supports the conclusion that CROA trumps the TSR's "advance fee." When Congress directed the FTC to issue rules respecting "abusive telemarketing acts or practices," (15 U.S.C. § 6102(a)(3)(C)), it did not authorize the FTC to issue rules restricting the time and manner in which a "person engaged in telemarketing" is compensated for the services being offered.[6] It is also difficult to square the longstanding ability of a credit reporting agency to deny a report dispute, (Pub. L. 91-508, § 611, 84. Stat. 1132 (Oct. 26, 1970)), with any Congressional authorization for a rule conditioning payment for credit repair services not only upon achievement of a successful result, but one that has endured for six months (free of any other intervening incidents damaging to the consumer's credit).

The TSR's "advance fee" rule is therefore not authorized rulemaking. *Accord Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 213-14 (1976) ("The rulemaking power granted to an administrative agency charged with the administration of a federal statute is not the power to make law. Rather, it is the power to adopt regulations to carry into effect the will of Congress as expressed by the statute. Thus, despite the broad view of the Rule advanced by the Commission in this case, its scope cannot exceed the power granted the Commission by Congress . . . .") (internal quotation omitted). The TSR's "advance fee," only upon success rule is thus entitled to no application contrary to CROA's provisions with respect to credit repair organizations.

[6] The closest Congress came to authorizing anything approximating the "advance fee," only upon success rule was when it imposed "a requirement that any person engaged in telemarketing for the sale of goods or services shall promptly and clearly disclose to the person receiving the call that the purpose of the call is to sell goods or services and make such other disclosures as the Commission deems appropriate, including the nature and price of the goods and services . . . ." *Id.* Disclosure of the price of a service, of course, is different from the time and manner in which payment can be sought.

As Plaintiff's claims are all based on such alleged violations of the TSR, they are invalid as a matter of law and must be dismissed. *See Schneider v. Bank of Am. N.A.*, No. CIV. S-11-2953 LKK, 2014 WL 2118327, *5 (E.D. Cal. May 21, 2014) ("This court knows of no principle that would permit an implementing regulation to create a liability that is broader than, or not even contemplated by, the governing statute.").[7]

VI. CONCLUSION

This Court should not allow the CFPB to proceed with this lawsuit based on a freestanding and unspecified "substantial assistance" claim, which fails to name or identify a single primary violation or violator. The pleading deficiencies in the CFPB's Complaint demonstrate that it has not diligently investigated specific and particular violations of the TSR or sought redress from the alleged violators. Instead, the CFPB seeks to bring down CRC – the software company that provides a word processing and a customer management system to a large number of small credit repair companies. But operating a credit repair business or providing a valued service that allows such businesses to streamline operations is not unlawful.

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[7] Defendants acknowledge that the few courts that have considered the issue of whether CROA's provisions regarding billing and payment trump the TSR's "advance fee," rule have found that the statutory provisions of CROA do not override the TSR's rule that applies only to telemarketers. *See Consumer Fin. Prot. Bureau v. Commonwealth Equity Grp., LLC*, No. 20-CV-10991, 2021 WL 3516690, *2 (D. Mass. Aug. 10, 2021); *Consumer Fin. Prot. Bureau v. Prime Mktg. Holdings, LLC*, No. CV1607111BROJEMX, 2016 WL 10516097, *8-9 (C.D. Cal. Nov. 15, 2016); *State v. Lexington L. Firms*, No. 3:96-0344, 1997 WL 367409, *6 (M.D. Tenn. May 14, 1997). However those courts have not considered whether the TSR's rule, is authorized rulemaking that could be considered on par with Congressional intent expressly stated in CROA. As noted, several members of Congress have said it is not. *See* RJN Ex. A ("[W]ith CROA's standard being the most recent and derived from congressional authority, one would assume with regard to CROs, the TSR is no longer operative . . . .").

This Court should put a stop to the CFPB's lawsuit, which is designed to put a lawful company and by extension a lawful industry, out of business. For all of the foregoing reasons the Court should grant the instant Motion pursuant to Rule 12(b)(6) and dismiss the Complaint in its entirety with prejudice.

Dated: December 17, 2021

Respectfully submitted,

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