IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF TEXAS
TYLER DIVISION

CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA; LONGVIEW CHAMBER OF COMMERCE; AMERICAN BANKERS ASSOCIATION; CONSUMER BANKERS ASSOCIATION; INDEPENDENT BANKERS ASSOCIATION OF TEXAS; TEXAS ASSOCIATION OF BUSINESS; and TEXAS BANKERS ASSOCIATION. *Plaintiffs*, v. CONSUMER FINANCIAL PROTECTION BUREAU; and ROHIT CHOPRA, in his official capacity as Director of the Consumer Financial Protection Bureau, *Defendants.*	Case No. 6:22cv381

COMPLAINT

Plaintiffs—Chamber of Commerce of the United States of America, Longview Chamber of Commerce, American Bankers Association, Consumer Bankers Association, Independent Bankers Association of Texas, Texas Association of Business, and Texas Bankers Association—bring this action for equitable relief against Defendants, Consumer Financial Protection Bureau (CFPB) and Rohit Chopra in his official capacity as Director of the CFPB. Plaintiffs primarily challenge the CFPB's recent update to the Unfair, Deceptive, or Abusive Acts or Practices (UDAAP) section of its examination manual.

INTRODUCTION

1. The CFPB is an agency with "vast authority." *Seila L. LLC v. Consumer Fin. Prot. Bureau*, 140 S. Ct. 2183, 2210 (2020). That vast authority makes the legal constraints that do exist all the more

important. Yet the CFPB's recent update is violating its statutory authority and the Administrative Procedure Act in three main ways:

2. ***First***, the CFPB is exceeding its statutory authority outlined in the Dodd-Frank Act. The recent update to its examination manual adopts the novel position that the CFPB can examine entities for alleged discriminatory conduct under its UDAAP authority. *See* CFPB Supervision and Examination Manual, Unfair, Deceptive, or Abusive Acts or Practices Section at 11, 13, 14, 17 (revised Mar. 16, 2022) (Exhibit A). But the CFPB cannot regulate discrimination under its UDAAP authority at all because Congress declined to give the CFPB authority to enforce anti-discrimination principles except in specific circumstances. The CFPB's statutory authorities consistently treat "unfairness" and "discrimination" as distinct concepts. *E.g.*, 12 U.S.C. §5511(b); §5481(13); §5493(c)(2)(A); §5531(c); §5536(a)(1).

3. ***Second***, the updated manual is "arbitrary" and "capricious." 5 U.S.C. §706(2)(A). Despite admitting that its UDAAP authority is modeled on the FTC's similar authority, Ex. A at 1 n.2, 2 n.4, the CFPB did not grapple with Congress's decision to narrowly define the FTC's unfairness authority to screen out the same kind of power that the CFPB is now claiming for itself.

4. Worse, the CFPB reads Dodd-Frank as giving it the broadest possible authority to regulate both disparate treatment and disparate *impacts*. In touting the update, the CFPB stated that "[c]onsumers can be harmed by discrimination regardless of whether it is intentional," so examiners will consider "discriminatory outcomes." *See* Halperin & Salas, *Cracking Down on Discrimination in the Financial Sector*, CFPB (Mar. 16, 2022) (Exhibit B). While Plaintiffs support the enforcement of existing nondiscrimination statutes, Dodd-Frank is not such a statute and does not come close to authorizing the CFPB's action.

5. ***Third***, the CFPB's updated manual violates the APA's procedural requirements because it constitutes a legislative rule that failed to go through notice and comment. 5 U.S.C. §553.

6. To be clear, the Chamber of Commerce of the United States of America, Longview Chamber of Commerce, American Bankers Association, Consumer Bankers Association, Independent Bankers Association of Texas, Texas Association of Business, Texas Bankers Association, and their respective members fully support the fair enforcement of nondiscrimination laws. Yet they cannot stand by while a federal agency exceeds its statutory authority, creates regulatory uncertainty, and imposes costly burdens on the business community. Especially when the CFPB did not even give the public an opportunity to raise concerns through the APA's notice-and-comment process.

7. This Court's intervention is needed to ensure that the CFPB is accountable to legal constraints, the rule of law, and the public as it pursues an aggressive agenda with far-reaching implications for the American economy, Plaintiffs, and their members.

JURISDICTION AND VENUE

8. This Court has subject-matter jurisdiction because this case arises under the Constitution and laws of the United States. *See* U.S. Const. art III, §2; 28 U.S.C. §§1331, 2201; 5 U.S.C. §§701-706.

9. This Court is authorized to award the requested relief under 5 U.S.C. §706; 28 U.S.C. §1361; and 28 U.S.C. §§2201-02.

10. Venue is proper in this district because Defendants include United States agencies and officers sued in their official capacities and because one of Plaintiffs resides here. *See* 28 U.S.C. §1391(e)(1).

PARTIES

11. Plaintiff Chamber of Commerce of the United States of America is the world's largest business federation. It represents approximately 300,000 direct members and indirectly represents the interests of more than 3 million companies and professional organizations of every size, in every

industry sector, and from every region of the country. An important function of the U.S. Chamber is to represent the interests of its members before Congress, the executive branch, and the courts.

12. Plaintiff Longview Chamber of Commerce is a voluntary representative organization of business and professionals who have joined together for the betterment of business, development of tourism, development of downtown Longview potential, and the overall quality of life in Longview.

13. Plaintiff American Bankers Association (ABA) is the voice of the nation's $23.7 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard $19.6 trillion in deposits and extend $11.8 trillion in loans. ABA advocates for banks before Congress, regulatory agencies and the courts to drive pro-growth policies that help customers, clients and communities thrive.

14. Plaintiff Consumer Bankers Association (CBA) is the only national trade association focused exclusively on retail banking. Established in 1919, the association is a leading voice in the banking industry and Washington, representing members who employ nearly two million Americans, extend roughly $3 trillion in consumer loans, and provide $270 billion in small business loans. Part of its mission includes representing its members interests in various government settings.

15. Plaintiff Independent Bankers Association of Texas (IBAT) is the largest state community banking organization in the nation, with membership comprised of more than 2,000 banks and branches in 700 Texas communities. Providing safe and responsible financial services to all Texans, IBAT member bank assets range in size from $27 million to $39 billion with combined assets statewide of nearly $256 billion. IBAT member banks are committed to supporting and investing in their local communities. IBAT advocates for and represents the interests of its members in various settings.

16. Plaintiff Texas Association of Business (TAB) is the largest general business association in the state as well as the Texas State Chamber of Commerce. TAB represents member

companies, large and small, to create a policy, legal, and regulatory environment that allows them to thrive in business.

17. Plaintiff Texas Bankers Association (TBA) is America's oldest and largest state banking organization. TBA advocates for 400 member banks in Austin and Washington and invests in Texas communities through financial literacy, scholarship, and charitable activities. TBA has a member median asset size of approximately $357 million and our banks employ over 150,000 Texans. TBA is dedicated to representing Texas community banks as well as institutions of all sizes and charter types before the Texas Legislature, U.S. Congress, state and federal regulatory agencies, and, when necessary, the courts.

18. Defendant CFPB is an agency of the United States. 12 U.S.C. §5491(a).

19. Defendant Rohit Chopra is the Director of the CFPB. Director Chopra is sued in his official capacity.

I. Federal rulemaking must comply with the Administrative Procedure Act.

20. The APA broadly waives the sovereign immunity of the United States and its federal agencies. It lets parties who are adversely affected or aggrieved by agency action seek judicial review. 5 U.S.C. §§702, 704.

21. Under the APA, agency action must be vacated if it is "not in accordance with law" or is "in excess of statutory jurisdiction, authority, or limitations." 5 U.S.C. §706(2)(A) & (C).

22. The APA further dictates that a court "shall hold unlawful and set aside agency action, findings, and conclusions found to be arbitrary, capricious, an abuse of discretion." 5 U.S.C. §706(2)(A). To meet this standard, "[f]ederal administrative agencies are required to engage in 'reasoned decisionmaking.' This necessarily means that '[n]ot only must an agency's decreed result be within the scope of its lawful authority, but the process by which it reaches that result must be logical

and rational.'" *Texas v. United States*, 524 F. Supp. 3d 598, 652 (S.D. Tex. 2021) (quoting *Allentown Mack Sales & Serv., Inc. v. NLRB*, 522 U.S. 359, 374 (1998)).

23. The APA also requires that an agency action be set aside if it is promulgated "without observance of procedure required by law." 5 U.S.C. §706(2)(D). Unless covered by an exception, all agency rules must go through the APA's notice-and-comment process. *Texas*, 524 F. Supp. 3d at 657. A "rule" is "an agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy," including "the approval or prescription . . . of valuations, costs, or accounting, or practices bearing on any of the foregoing." 5 U.S.C. §551(4). This definition includes "virtually every statement an agency can make." *Avoyelles Sportsmen's League, Inc. v. Marsh*, 715 F.2d 897, 908 (5th Cir. 1983).

24. To that end, the APA distinguishes between "legislative rules" and "interpretive rules." The former are subject to the Act's notice-and-comment requirements. 5 U.S.C. §553(b)(3)(A). In determining whether a rule is legislative or interpretive, the agency's label is not dispositive. Rather, any rules that operate as "substantive agency regulations" are deemed legislative. *Chrysler Corp. v. Brown*, 441 U.S. 281, 295, 313-15 (1979). "Legislative or substantive rules are those which 'affect individual rights and obligations.'" *Shell Offshore Inc. v. Babbitt*, 238 F.3d 622, 628 (5th Cir. 2001).

25. Notice and comment provides a crucial and necessary safeguard against the consequences of an unchecked federal administrative state. *See Free Enterprise Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 499 (2010) ("The growth of the Executive Branch, which now wields vast power and touches almost every aspect of daily life, heightens the concern that it may slip from the Executive's control, and thus from that of the people.").

II. The CFPB attempts to regulate discriminatory conduct under UDAAP violates the APA.

A. The CFPB has broad jurisdiction.

26. In Dodd-Frank, Congress established the CFPB as an independent agency to "implement and … enforce Federal consumer financial law." 12 U.S.C. §5511(a). The CFPB's discrete purpose is to "ensur[e] that all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive." 12 U.S.C. §5511(a).

27. "Congress transferred the administration of 18 existing federal statutes to the CFPB, including the Fair Credit Reporting Act, the Fair Debt Collection Practices Act, and the Truth in Lending Act." *Seila Law*, 140 S. Ct. at 2193. Congress also made it unlawful for entities, like Plaintiffs' members, "to engage in any unfair, deceptive, or abusive act or practice." 12 U.S.C. §5536(a)(1)(B).

28. Among other things, Congress gave the CFPB authority to "conduct investigations, issue subpoenas and civil investigative demands, initiate administrative adjudications, and prosecute civil actions in federal court." *Seila Law*, 140 S. Ct. at 2193 (citing 12 U.S.C. §§5562, 5564(a), (f)). Through those processes, the CFPB can seek penalties including restitution, rescission of contracts, disgorgement, and injunctive relief. 12 U.S.C. §5565.

29. The CFPB was also granted the authority to "require reports and conduct examinations on a periodic basis" of certain entities, including members of each Plaintiff, in order to "assess[] compliance with the requirements of Federal consumer financial law," and "obtain[] information about the activities and compliance systems or procedures" of the examined entity. 12 U.S.C. §§5514-15.

30. Plaintiffs each have members regulated by the CFPB under these statutes and enforcement processes.

B. The CFPB uses examinations and enforcement actions to exercise its UDAAP authority.

31. Dodd-Frank gave the CFPB authority to prohibit "unfair" acts or practices by covered entities, among other laws that the CFPB enforces. *See* 12 U.S.C. §5536(a)(1)(B) (giving the CFPB the authority to enforce a statute that makes it unlawful for a covered entity "to engage in any unfair, deceptive, or abusive act or practice"). But in enacting Dodd-Frank, Congress chose not to provide the CFPB with authority over alleged discrimination, except in specific circumstances.

32. Dodd-Frank authorized the CFPB to "prescribe rules applicable to a covered person or service provider identifying as unlawful, unfair, deceptive, or abusive acts or practices in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service," including "requirements for the purpose of preventing such acts or practices." 12 U.S.C. §5531(b). In some cases, the CFPB has done so. *See, e.g.*, 12 C.F.R. §1041.7 & Supp. I.

33. But here, the CFPB has elected simply to announce its exercise of UDAAP authority, without notice or an opportunity for public comment, through its nearly 2,000-page Supervision and Examination Manual. *See* CFPB, *Supervision and Examination Manual* (Mar. 2022), bit.ly/2HYQXLW. The Supervision and Examination Manual explains that Dodd-Frank "authorizes it to supervise certain financial companies and large depository institutions and their affiliates for consumer protection purposes." CFPB Supervision and Examination Manual, Overview Section at 1 (revised Oct. 12, 2012) (Exhibit C). As a result, the CFPB "has the responsibility to implement, examine for compliance with, and enforce 'Federal consumer financial law.'" *Id.* This law includes the requirement that CFPB monitor compliance with Dodd-Frank's prohibitions on "unfair, deceptive, or abusive acts and practices in connection with consumer products and services." *Id.*

34. CFPB's examination of regulated entities is far-reaching. After going "onsite to observe, conduct interviews, and review … documents and information," the CFPB decides whether the

examination "indicates potential unfair, deceptive, or abusive acts or practices"; evaluates "the regulated entity's compliance management and its statutory and regulatory compliance"; and decides whether there should be any "corrective actions that the institution should take, whether through informal agreement or a formal enforcement action." *Id.* at 5-6.

35. In other words, the CFPB examiners extensively review the regulated entity's compliance with UDAAP and the other federal laws that the CFPB enforces. But CFPB examiners do more than just decide whether a regulated entity has violated federal law. They also review whether the entity has adequate policies and procedures in place to *prevent* violations.

36. For UDAAP in particular, compliance requires substantial resources. To start with, examiners "assess the quality of the regulated entity's compliance risk management systems, including internal controls and policies and procedures, for avoiding unfair, deceptive, or abusive acts or practices." Ex. A at 11. They also "identify acts or practices" that examiners believe "materially increase the risk of consumers being treated in an unfair, deceptive, or abusive manner." *Id.*

37. To conduct that review and assess the entity's compliance, examiners have carte blanche to obtain and review copies of the entity's internal documents, including: "Training materials," "Procedure manuals and written policies"; "Internal control monitoring and auditing materials"; and "Minutes of the meetings of the Board of Directors and of management committees, including those related to compliance." *Id.* Examiners' evaluations also include "reviewing all relevant written policies and procedures" and "internal and external audit reports." *Id.* at 12.

38. The examiners then make determinations on dozens of vaguely worded factors, including whether the entity's own compliance audits "include[] a review of potential unfair, deceptive, or abusive acts or practices"; "Management and the Board of Directors are made aware of and review significant deficiencies and their causes"; "Management has taken corrective actions to follow up on any identified deficiencies"; and "[t]he entity's compliance program includes an established process

for periodic analysis and monitoring of all decision-making processes used in connection with consumer financial products and services, and a process to take corrective action to address any potential UDAAP concerns." *Id.* at 12-13.

39. The examiners also "determine whether the entity's internal controls are adequate to prevent unfair, deceptive or abusive acts or practices." *Id.* at 13. That determination is based on whether the "compliance management program includes measures aimed at avoiding unfair, deceptive, or abusive practices"; "The entity conducts prior UDAAP reviews on advertising and promotional materials"; "The entity reviews new products and changes in terms and conditions of existing products for potential UDAAP concerns"; "The entity has established policies and procedures to review, test, and monitor any decision-making processes it uses for potential UDAAP concerns"; and "[t]he entity has established policies and procedures to mitigate potential UDAAP concerns arising from the use of its decision-making processes." *Id.* at 13-14.

40. If the CFPB concludes that a regulated entity has violated UDAAP or that its compliance program is inadequate, it may issue a "Matter Requiring Attention." Supervision and Examination Manual, Examinations and Targeted Reviews Section at 17 (revised Feb. 2019) (Exhibit D). A "Matter Requiring Attention" will identify "specific goals to be accomplished" including "timeframes for periodic reporting of efforts taken to address these matters, as well as expected timeframes for implementation." *Id.*

41. Until recently, the CFPB would also issue "Supervisory Recommendations." A "Supervisory Recommendation" did not "include provisions for periodic reporting or expected timelines for implementation," but the CFPB "[would] review through monitoring the steps institutions have taken to address" a Supervisory Recommendation. *Id.* In March 2021, the CFPB eliminated the use of Supervisory Recommendations, noting that "MRAs will more effectively convey our supervisory expectations." CFPB Bulletin 2021-01 at 2 (Mar. 31, 2021), https://bit.ly/3LEJy4D.

42. In some cases, the CFPB will refer a matter to its "Action Review Committee," which determines "whether matters that originate from examinations will be resolved through confidential supervisory action, such as a board resolution or memorandum of understanding, or through a public enforcement action." CFPB, *Supervisory Highlights* at 27 (Summer 2015), bit.ly/3SuNhnL; *see also* CFPB, *Supervisory Highlights* at 37-38 (Sept. 2017), bit.ly/3Srdgwk ("about one-third" of matters referred to the Action Review Committee result in public enforcement proceedings).

43. The CFPB treats the entire process as producing confidential information that belongs to the agency. Regulated entities are largely prohibited from disclosing information about the process "without the prior written permission of the Director" of the CFPB. 12 C.F.R. §1070.47(a)(2). By any name, this is regulation without any opportunity for public scrutiny and typifies the CFPB's transparency and accountability problems.

44. Although a Matter Requiring Attention is not itself legally enforceable, the CFPB considers a regulated entity's "response ... when assessing an institution's Compliance rating, or otherwise considering the risks that an institution poses to consumers and to markets," which "may be used by the Bureau when prioritizing future supervisory work or assessing the need for potential enforcement action." Ex. D at 17. Draft examination reports are also shared with the entity's prudential regulator, which can take any number of actions against the entity based on the CFPB's conclusions, including adjustment to ratings, penalties, and enforcement actions. As a result, the CFPB's examination findings are not-so-confidential communications that can have significant public consequences.

45. If the CFPB chooses to bring an enforcement action based on findings it made during the examination process, it may issue expansive penalties, including "civil monetary penalties," "disgorgement" of profits, "restitution," and "[p]ublic notification regarding the violation." Ex. A at 7.

C. The CFPB misinterprets its UDAAP authority to include discrimination.

46. Before this year, the CFPB had never interpreted its UDAAP authority to include the power to regulate discriminatory conduct. Since its first iteration in October 2012, the manual made no mention of discrimination in the UDAAP section. *See* CFPB, *Unfair, Deceptive, or Abusive Acts or Practices Examination Manual* (revised Oct. 2012) (Exhibit E). To the contrary, the manual repeatedly treated UDAAP and discrimination separately.

47. That changed earlier this year. *See CFPB Targets Unfair Discrimination in Consumer Finance*, CFPB (Mar. 16, 2022) (Exhibit F). On March 16, the CFPB updated several portions of its examination manual to claim authority to regulate discrimination under its UDAAP authority.

48. First, the updated manual claims that its examination objectives include identifying "acts or practices that materially increase the risk of consumers being treated in an unfair, deceptive, or abusive manner, *including discriminatory* acts or practices." Ex. A at 11 (emphasis added).

49. Second, the manual now dictates requirements that a regulated "entity's compliance program includes an established process for periodic analysis and monitoring of all decision-making processes used in connection with consumer financial products or services, and a process to take corrective action to address any potential UDAAP concerns related to their use, *including discrimination*." *Id.* at 13 (emphasis added)

50. Third, the manual now requires that a regulated "entity has established policies and procedures to review, test, and monitor any decision-making processes it uses for potential UDAAP concerns, *including discrimination*." *Id.* at 14 (emphasis added). It also requires that a regulated "entity has established policies and procedures to mitigate potential UDAAP concerns arising from the use of its decision-making processes, *including discrimination*." *Id.* (emphasis added). It instructs examiners specifically to evaluate if an "entity has a process to take prompt corrective action if the decision-making processes it uses produce deficiencies or discriminatory results." *Id.* at 18.

51. Fourth, the manual now requires that a regulated "entity ensures that employees and third parties who market or promote products or services are adequately trained so that they do not engage in unfair, deceptive, or abusive acts or practices, *including discrimination*." *Id.* at 17 (emphasis added). Regulated entities must also ensure "that employees and third party contractors refrain from engaging in servicing or collection practices that lead to differential treatment or disproportionately adverse impacts on a discriminatory basis." *Id.* at 18.

52. Fifth, the manual instructs its examiners to obtain documentation from regulated entities "regarding the use of models, algorithms, and decision-making processes used in connection with consumer financial products and services"; "[i]nformation collected, retained or used regarding customer demographics, including the demographics of customers using various products or services"; and "any demographic research or analysis relating to marketing or advertising of consumer financial products or services." *Id.* at 12.

53. The CFPB did not hide its decision; it proclaimed that, after the update, "[d]iscrimination or improper exclusion can trigger liability under [the] ban on unfair acts or practices." Ex. F. As the CFPB explained things: "We will be *expanding* our anti-discrimination efforts to combat discriminatory practices *across the board* in consumer finance." *Id.* (emphases added). The CFPB also "will examine for discrimination in all consumer finance markets, including credit, servicing, collections, consumer reporting, payments, remittances, and deposits." *Id.*

D. The CFPB's "update" is causing significant compliance costs.

54. In its blog post published after the update, the CFPB stated that this update would impose new obligations on regulated entities. CFPB examiners now "will require supervised companies to show their processes for assessing risks *and discriminatory outcomes [i.e., "disparate impact"]*, including documentation of customer demographics and the impact of products and fees on different demographic groups." *Id.* (emphasis added). And the CFPB "will look at how companies test and

monitor their decision-making processes for unfair discrimination, *as well as discrimination* under [the ECOA]." *Id.* (emphasis added).

55. The CFPB has redefined the unfairness prong of UDAAP. This redefinition means that the CFPB can now examine for and enforce its novel interpretation. As a matter of course, the CFPB shares violations it finds in examinations with the Enforcement Division, which results in Enforcement opening investigations and lawsuits. The update is thus not a change that attempts to explain how the CFPB will examine an institution. Rather, it is a dictate that institutions *must* comply with or face legal action.

56. All financial services companies are affected by the CFPB's exercise of enforcement authority in this new area. In fact, CFPB has already said that it will use the updated manual to do just that. *See* Ex. B ("Under the updated examination guidelines, we will continue to scrutinize any conduct of covered institutions that violates the federal prohibition against unfair practices, including determining if an entity has unfairly discriminated against certain people.").

57. The CFPB's addition of discrimination-related compliance issues adds to the already burdensome UDAAP compliance regime. Yet the CFPB provided no instruction for the regulated communities on what might constitute unfair discrimination or actionable disparate impacts. Several points illustrate the confusion:

a. The CFPB did not identify any protected classes or characteristics, as essentially all nondiscrimination statutes must do. For example, ECOA prohibits discrimination on the basis of race, color, religion, national origin, sex, marital status, age, receipt of public assistance, or good faith exercise of any rights under the Consumer Credit Protection Act. But other federal antidiscrimination laws protect classes with different characteristics. *See, e.g.*, 29 C.F.R. §37.1 (implementing the "nondiscrimination …

provisions of the Workforce Investment Act of 1998" which include "age, disability, [and] political affiliation or belief," among other unique criteria).

b. ECOA expressly identifies certain activities that are *not* discrimination, such as inquiring about an applicant's age or whether the applicant's income derives from public assistance programs if such inquiries are "for the purpose of determining the amount and probable continuance of income levels, credit history, or other pertinent element[s] of credit-worthiness as provided in regulations of the Bureau." 15 U.S.C. §1691(b)(2). The CFPB included no such guidance for its pronouncement.

c. Nor did the CFPB explain how regulated entities, which are prohibited in some instances from collecting customer demographic information, are supposed to conduct the sort of assessments that the agency appears to be contemplating. *See, e.g.*, 12 C.F.R. §1002.5(b)-(d).

58. These amendments to the manual harm Plaintiffs' members by imposing heavy compliance costs that are ultimately passed down to consumers in the form of higher prices and reduced access to products. In fact, that's the point. Director Chopra recently stated that the CFPB informs industry how it will "exercise its supervisory authority and enforcement authority" by "publish[ing] our examination manuals, which is essentially guidance to our examiners about what they might look at when they decide in the scope of an exam to dig into a specific set of complaints or issues." Jon Hill, *From Crypto to Apps, CFPB's Chopra Has Payments in Focus*, Law360 (July 27, 2022) (Exhibit G).

59. To come into compliance with these new directives, Plaintiffs' members have no choice but to update their UDAAP compliance policies and programs, at significant cost, and they will perpetually incur costs to remain in compliance.

60. Plaintiffs also have members who are not supervised by the CFPB but will be affected by the updated manual. The CFPB is the agency charged by Congress with enforcing the UDAAP

provision of the Dodd-Frank Act, 12 U.S.C. §5536(a)(1)(B), so any entity subject to the Dodd-Frank provisions governing UDAAP is affected by the CFPB's pronouncements. Plaintiffs each have members not primarily regulated by the CFPB who provide consumer financial products and/or are service providers for such products. Such entities are thus subject to Dodd-Frank's prohibitions on UDAAP. *Compare* 12 USC §5481(6) (defining a "covered person" for the purpose of the exercise of UDAAP authority under Dodd-Frank as "(A) any person that engages in offering or providing a consumer financial product or service; and (B) any affiliate of a person described in subparagraph (A) if such affiliate acts as a service provider to such person"), *with* Ex. C at 1 n.2 (The CFPB claims "supervisory authority" over "(1) non-depository consumer financial service companies and their service providers; (2) large insured depository institutions, large insured credit unions, and their affiliates, as well as service providers to these entities; and (3) service providers to a substantial number of small insured depository institutions or small insured credit unions." (citing 12 U.S.C. §5514-5517)).

E. The CFPB's updated manual exceeds its statutory authority.

61. The CFPB has stretched its UDAAP authority beyond the bounds carefully set by Congress. In describing the update, the CFPB's mistaken notion that "[d]iscrimination … can trigger liability under [the] ban on unfair acts or practices" ignores the text, structure, and history of Dodd-Frank, as well as similar legislation addressing agencies' authority to regulate unfairness. Ex. F.

62. Dodd-Frank discusses "unfairness" and "discrimination" as two distinct concepts, and it defines "unfairness" without making any reference to "discrimination" or disparate impact liability. *See Mtn. States Legal Found. v. Bush*, 306 F.3d 1132, 1136 (D.C. Cir. 2002) ("The responsibility of determining the limits of statutory grants of authority … is a judicial function entrusted to the courts by Congress by the statutes establishing courts and marking their jurisdiction." (quoting *Stark v. Wickard*, 321 U.S. 288, 310 (1944))). Further, given the substantial "economic and political significance" the CFPB's interpretation would have, courts have "reason to hesitate before concluding that Congress

meant to confer such authority." *West Virginia v. Env't Prot. Agency*, 142 S. Ct. 2587, 2608 (2022) (internal quotation marks omitted).

F. The CFPB's updated manual is arbitrary and capricious.

63. The CFPB's implementation of its expansive view of "unfairness" is also arbitrary and capricious because it contradicts the historical use and understanding of the term. *See Texas*, 524 F. Supp. 3d at 652 (requiring "reasoned decisionmaking").

64. In 1938, Congress authorized the Federal Trade Commission (FTC) to protect consumers from "unfair or deceptive acts or practices in or affecting commerce." Pub. L. No. 75-447, 52 Stat. 111 (1938) (codified as amended at 15 U.S.C. §45(a)(1)). After initially leaving the term "unfair" undefined, Congress later curtailed the Commission's use of its unfairness authority. *See* Pub. L. No. 96-252, 94 Stat. 374 (1980) (codified as amended in scattered sections of 15 U.S.C.). It codified a constrained definition of unfairness—that does not include discrimination—to limit the Commission's ability to use unfairness to pursue unlimited public-policy goals. 15 U.S.C. §45(n). These efforts confirm that the "unfairness" authority conferred by Congress did not extend to discrimination.

65. This context is important because Congress borrowed the unfairness definition that governs the CFPB from the Federal Trade Commission Act. *See* Ex. A at 1 n.2, 2 n.4. As Director Chopra conceded in recent testimony, "'[U]nfairness' … derive[s] from the FTC Act. It is identical language." *The Consumer Financial Protection Bureau's Semi-Annual Report to Congress, Hearing before the Senate Comm. on Banking, Hous., and Urb. Affairs*, 117th Cong. (2022) (statement of Rohit Chopra, Director of the CFPB). Where Congress borrows terms of art from other acts, it presumably conveys the same meaning. *Morissette v. United States*, 342 U.S. 246, 263 (1952).

66. What's more, the CFPB's contemplation of *disparate-impact* liability—a specific form of liability that not even most antidiscrimination laws create—flouts congressional intent and Supreme Court precedent. *See* Ex. A at 15 (addressing determinations "that result in discrimination").

67. CFPB has confirmed several times that its updated manual covers disparate-impact liability. For example, the CFPB stated that "[c]onsumers can be harmed by discrimination regardless of whether it is intentional," so CFPB examiners now consider "discriminatory outcomes." Ex. F. And the CFPB stated elsewhere that actions producing "disparate treatment or a discriminatory outcome … fall squarely within our mandate to address and eliminate unfair practices." Ex. B. Yet neither Director Chopra (Ex. F) nor his colleagues (Ex. B) root this expansion of the agency's authority in anything besides existing UDAAP authority.

68. This position cannot be squared with the Supreme Court's admonition that statutes can authorize disparate-impact liability only in narrow circumstances. *Tex. Dep't of Hous. & Cmty. Affairs v. Inclusive Communities Proj., Inc.*, 576 U.S. 519, 534 (2015). Namely, the Supreme Court has required two conditions to imply disparate-impact liability is permissible: the statute must be an antidiscrimination law, and the statute must contain results-oriented language demonstrating that it is designed to impose liability for disparate-impact claims. *Id.*

69. Dodd-Frank has neither characteristic: It is not an antidiscrimination statute, and neither it nor any of the other relevant statutes have any results-oriented language showing that Congress intended for the CFPB to address disparate-impact claims. Accordingly, Dodd-Frank provides no textual support for the notion that Congress authorized the CFPB to pursue disparate-impact claims under its UDAAP authority.

70. Additionally, the CFPB's manual update also ignores the reliance interests which have grown up around its prior approach to UDAAP authority. *See Encino Motorcars, LLC v. Navarro*, 136 S. Ct. 2117, 2126 (2016) ("In explaining its changed position, an agency must also be cognizant that

longstanding policies may have 'engendered serious reliance interests that must be taken into account.'").[*]

71. This unreasoned change does not clear the APA's arbitrary-and-capricious standard. It fails to consider the CFPB's prior position on UDAAP authority, provides no well-founded reasons for the update, and does not consider reliance interests. *See Dep't of Homeland Sec. v. Regents of the Univ. of California*, 140 S. Ct. 1891, 1913 (2020) ("*State Farm* teaches that when an agency rescinds a prior policy its reasoned analysis must consider the "alternative[s]" that are "within the ambit of the existing [policy]."); *F.C.C. v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009) ("[T]he requirement that an agency provide reasoned explanation for its action would ordinarily demand that it display awareness that it is changing position.").

72. The manual update is thus arbitrary and capricious. 5 U.S.C. §706(2)(A).

G. The updated manual violates the APA's notice-and-comment requirement.

73. With exceptions not relevant here, the APA requires legislative rules to go through the rigors of notice and comment. *Perez v. Mortg. Bankers Ass'n*, 575 U.S. 92, 96 (2015); *U.S. Dep't of Labor v. Kast Metals Corp.*, 744 F.2d 1145, 1153 n.17 (5th Cir. 1984) ("'Section 553 was enacted to give the public an opportunity to participate in the rule-making process. It also enables the agency promulgating the rule to educate itself before establishing rules and procedures which have a substantial impact on those who are regulated.'").

[*] Even if UDAAP authority could be interpreted to include discrimination claims, due process would bar the CFPB from attempting to hold companies responsible under this new UDAAP definition for conduct *before* the CFPB announced its new definition. *PHH Corp. v. CFPB*, 839 F.3d 1, 44 (D.C. Cir. 2016) *reh'g en banc granted, order vacated* (Feb. 16, 2017), *on reh'g en banc*, 881 F.3d 75 (D.C. Cir. 2018) ("But change becomes a problem—a fatal one—when the Government decides to turn around and retroactively apply that new interpretation to proscribe conduct that occurred before the new interpretation was issued.").

74. The updated manual is a legislative rule subject to the APA's notice-and-comment requirement because it "change[s] the legal status of regulated parties" by subjecting them to supervision and examination on discrimination under UDAAP. *Mann Constr., Inc. v. United States*, 27 F.4th 1138, 1143 (6th Cir. 2022); *see also Texas v. United States*, 809 F.3d 134, 171 (5th Cir. 2015) (exceptions to notice and comment "must be narrowly construed").

75. Indeed, the update sets out a substantive rule that the CFPB will carry out when regulating. *See Prof'ls. & Patients for Customized Care v. Shalala*, 56 F.3d 592, 595 (5th Cir. 1995) (the focus is "primarily on whether the rule has binding effect on agency discretion or severely restricts it"). Put another way, the update "marks the consummation of the agency's decisionmaking process," and "legal consequences" will flow from it. *U.S. Army Corps of Eng'rs v. Hawkes Co.*, 136 S. Ct. 1807, 1813 (2016).

76. The update specifically "impose[s] new … duties" on businesses by empowering examiners to investigate—and thus requiring businesses to keep—certain records and policies. *Mann Constr.*, 27 F.4th at 1143; *see also* Ex. F (confirming the update's finality and explaining that discrimination can presently "trigger liability" for regulated entities under the UDAAP authority).

77. That the CFPB was revising the previous manual does not excuse the CFPB from the APA's procedural requirements. *See Clean Water Action v. United States Envtl. Prot. Agency*, 936 F.3d 308, 312 (5th Cir. 2019) (An agency must "follow the same process to revise a rule as it used to promulgate it." (citing *Perez*, 575 U.S. at 100)).

78. The update is not a mere clarification of existing rules, but imposes new substantive obligations on regulated entities without going through the required notice-and-comment procedure under the APA.

79. The CFPB's action, taken without legislative authority, opens the door to uncertain and excessive regulation in the financial marketplace that imposes significant financial burdens on Plaintiffs, their members, and the public.

CLAIMS FOR RELIEF
COUNT I
Updated Manual
Violation of the APA: Exceeds Statutory Authority
(5 U.S.C. §706(2)(A), (C); 12 U.S.C. §5536)

80. Plaintiffs repeat and reincorporate all their prior allegations.

81. Under the APA, a "reviewing court shall … hold unlawful and set aside agency action ... found to be ... not in accordance with law" or "in excess of statutory jurisdiction, authority, or limitations." 5 U.S.C. §706(2)(A), (C).

82. Dodd-Frank created the CFPB and gave it authority to enforce a statute that makes it unlawful for an entity "to engage in any unfair, deceptive, or abusive act or practice." 12 U.S.C. §5536(a)(1)(B).

83. The CFPB's March 2022 updated manual exceeds the CFPB's statutory authority by adding discrimination to its UDAAP authority. Dodd-Frank does not authorize the CFPB to regulate discrimination under that distinct authority.

84. The updated manual is final agency action under the APA because it imposes concrete obligations on Plaintiffs' members.

85. Because the updated manual contravenes the limits of the CFPB's power under Dodd-Frank, the update violates the APA and should be set aside.

COUNT II
Updated Manual
Violation of the APA: Arbitrary and Capricious
(5 U.S.C. §706(2)(A))

86. Plaintiffs repeat and reincorporate all their prior allegations.

87. A "reviewing court shall ... hold unlawful and set aside agency action ... found to be arbitrary, capricious, [or] an abuse of discretion." 5 U.S.C. §706(2)(A).

88. Despite acknowledging that its UDAAP authority is modeled on the FTC's unfairness authority, the CFPB failed to grapple with Congress's decision to narrow the FTC's authority in a way that does not include discrimination. The updated manual is thus arbitrary and capricious because it contradicts the historical use and understanding of the term "unfair."

89. The CFPB also failed to adopt safeguards that are essential for pursuing disparate-impact liability.

90. Because the updated manual is arbitrary and capricious with respect to its expansion of UDAAP authority, it is invalid and should be set aside.

COUNT III
Updated Manual
Violation of the APA: Notice and Comment
(5 U.S.C. §553)

91. Plaintiffs repeat and reincorporate all their prior allegations.

92. The updated manual is a legislative rule subject to the APA's notice-and-comment requirement.

93. The CFPB did not submit the updated manual for notice and comment.

94. Because the updated manual violates the APA, it is invalid and should be set aside.

COUNT IV
CFPB's Funding Structure
Violation of the Appropriations Clause
(U.S. Const. art I, §9, cl. 7)

95. Plaintiffs repeat and reincorporate all their prior allegations.

96. In addition to all the defects with the manual update noted above, it was also issued with funds not properly appropriated in accordance with law.

97. The Appropriations Clause requires legislative appropriations prior to executive expenditures. U.S. Const. art I, §9, cl. 7.

98. Contrary to the ordinary process for annual appropriations from Congress, the CFPB has an unprecedented level of budgetary independence, under which it requisitions funds directly from the Federal Reserve, without involvement or oversight by Congress. For an agency that exercises vast executive authority, such budgetary independence defies the separation of powers. *See Consumer Fin. Prot. Bureau v. All Am. Check Cashing, Inc.*, 33 F.4th 218, 232 (5th Cir. 2022) (Jones, J., concurring) ("The CFPB's budgetary independence makes it unaccountable to Congress and the people. An agency that wields vast amounts of executive, legislative, and adjudicatory power and is completely unaccountable to Congress is inimical to the Constitution's structural checks and balances.").

99. The CFPB's funding scheme is distinct from other financial regulators that enjoy some level of self-funding. *See id.* at 235-36 (distinguishing the CFPB's unique funding structure from that of the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency because (1) "the mission and corresponding authority of those agencies is more targeted"; (2) "both the Federal Reserve and the Federal Deposit Insurance Corporation operate as independent agencies"; (3) each agency maintains "some level of political accountability" through "multimember leadership" and its relationship with regulated entities; and (4) no other agency with some measure of budgetary independence "wields enforcement or regulatory authority remotely comparable to the authority the CFPB may exercise throughout the economy").

100. The CFPB relies on this unconstitutional funding scheme to carry out its overly expansive UDAAP authority to Plaintiffs' detriment.

101. Because the CFPB's funding structure violates the Appropriations Clause, this Court should declare that structure unconstitutional and set aside the manual update. A narrow ruling

regarding the CFPB's unique funding structure would not affect other agencies who lack the same markers of vast regulatory power without political accountability.

PRAYER FOR RELIEF

Plaintiffs ask this Court to enter judgment in their favor and to provide the following relief:

a. a declaration that the CFPB's March 2022 update to its manual exceeds the agency's statutory authority;

b. a declaration that the CFPB's March 2022 update to its manual is arbitrary and capricious;

c. a declaration that the CFPB's March 2022 update to its manual is invalid because the CFPB failed to submit it through proper notice-and-comment rulemaking procedures;

d. a declaration that the CFPB's funding structure, upon which it relies to exercise its UDAAP authority, violates the Appropriations Clause;

e. an injunction setting aside the CFPB's March 2022 update to the manual;

f. an injunction preventing the CFPB from pursuing any examinations or enforcement actions based on the interpretation of its UDAAP authority announced in the March 2022 update;

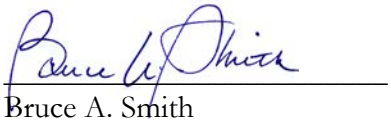
g. an injunction ordering the CFPB to cease accepting funds in violation of the Appropriations Clause;

h. attorney's fees and costs incurred in relation to this case; and

i. all other relief to which Plaintiffs are entitled that the Court deems just and proper.

Dated: September 28, 2022

Respectfully Submitted,



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JS 44 (Rev. 04/21)

CIVIL COVER SHEET

The JS 44 civil cover sheet and the information contained herein neither replace nor supplement the filing and service of pleadings or other papers as required by law, except as provided by local rules of court. This form, approved by the Judicial Conference of the United States in September 1974, is required for the use of the Clerk of Court for the purpose of initiating the civil docket sheet. *(SEE INSTRUCTIONS ON NEXT PAGE OF THIS FORM.)*

I. (a) PLAINTIFFS

Chamber of Commerce of the United States of America; Longview Chamber of Commerce; et al.

(b) County of Residence of First Listed Plaintiff District of Columbia
(EXCEPT IN U.S. PLAINTIFF CASES)

(c) Attorneys *(Firm Name, Address, and Telephone Number)*
Bruce A. Smith, Ward, Smith & Hill PLLC
P. O. Box 1231, Longview, Texas 75606
(903) 757-6400

DEFENDANTS

Consumer Financial Protection Bureau; and Rohit Chopra, in his official capacity as Director of CFPB

County of Residence of First Listed Defendant
(IN U.S. PLAINTIFF CASES ONLY)

NOTE: IN LAND CONDEMNATION CASES, USE THE LOCATION OF THE TRACT OF LAND INVOLVED.

Attorneys *(If Known)*

II. BASIS OF JURISDICTION *(Place an "X" in One Box Only)*

- ☐ 1 U.S. Government Plaintiff
- ☐ 3 Federal Question *(U.S. Government Not a Party)*
- ☒ 2 U.S. Government Defendant
- ☐ 4 Diversity *(Indicate Citizenship of Parties in Item III)*

III. CITIZENSHIP OF PRINCIPAL PARTIES *(Place an "X" in One Box for Plaintiff and One Box for Defendant)*

(For Diversity Cases Only)

	PTF	DEF		PTF	DEF
Citizen of This State	☐ 1	☐ 1	Incorporated *or* Principal Place of Business In This State	☐ 4	☐ 4
Citizen of Another State	☐ 2	☐ 2	Incorporated *and* Principal Place of Business In Another State	☐ 5	☐ 5
Citizen or Subject of a Foreign Country	☐ 3	☐ 3	Foreign Nation	☐ 6	☐ 6

IV. NATURE OF SUIT *(Place an "X" in One Box Only)*

Click here for: Nature of Suit Code Descriptions.

CONTRACT	TORTS		FORFEITURE/PENALTY	BANKRUPTCY	OTHER STATUTES
☐ 110 Insurance	PERSONAL INJURY	PERSONAL INJURY	☐ 625 Drug Related Seizure of Property 21 USC 881	☐ 422 Appeal 28 USC 158	☐ 375 False Claims Act
☐ 120 Marine	☐ 310 Airplane	☐ 365 Personal Injury - Product Liability	☐ 690 Other	☐ 423 Withdrawal 28 USC 157	☐ 376 Qui Tam (31 USC 3729(a))
☐ 130 Miller Act	☐ 315 Airplane Product Liability	☐ 367 Health Care/ Pharmaceutical Personal Injury Product Liability		INTELLECTUAL PROPERTY RIGHTS	☐ 400 State Reapportionment
☐ 140 Negotiable Instrument	☐ 320 Assault, Libel & Slander	☐ 368 Asbestos Personal Injury Product Liability		☐ 820 Copyrights	☐ 410 Antitrust
☐ 150 Recovery of Overpayment & Enforcement of Judgment	☐ 330 Federal Employers' Liability	PERSONAL PROPERTY	LABOR	☐ 830 Patent	☐ 430 Banks and Banking
☐ 151 Medicare Act	☐ 340 Marine	☐ 370 Other Fraud	☐ 710 Fair Labor Standards Act	☐ 835 Patent - Abbreviated New Drug Application	☐ 450 Commerce
☐ 152 Recovery of Defaulted Student Loans (Excludes Veterans)	☐ 345 Marine Product Liability	☐ 371 Truth in Lending	☐ 720 Labor/Management Relations	☐ 840 Trademark	☐ 460 Deportation
☐ 153 Recovery of Overpayment of Veteran's Benefits	☐ 350 Motor Vehicle	☐ 380 Other Personal Property Damage	☐ 740 Railway Labor Act	☐ 880 Defend Trade Secrets Act of 2016	☐ 470 Racketeer Influenced and Corrupt Organizations
☐ 160 Stockholders' Suits	☐ 355 Motor Vehicle Product Liability	☐ 385 Property Damage Product Liability	☐ 751 Family and Medical Leave Act	SOCIAL SECURITY	☐ 480 Consumer Credit (15 USC 1681 or 1692)
☐ 190 Other Contract	☐ 360 Other Personal Injury		☐ 790 Other Labor Litigation	☐ 861 HIA (1395ff)	☐ 485 Telephone Consumer Protection Act
☐ 195 Contract Product Liability	☐ 362 Personal Injury - Medical Malpractice		☐ 791 Employee Retirement Income Security Act	☐ 862 Black Lung (923)	☐ 490 Cable/Sat TV
☐ 196 Franchise				☐ 863 DIWC/DIWW (405(g))	☐ 850 Securities/Commodities/ Exchange
				☐ 864 SSID Title XVI	☐ 890 Other Statutory Actions
				☐ 865 RSI (405(g))	☐ 891 Agricultural Acts
REAL PROPERTY	CIVIL RIGHTS	PRISONER PETITIONS	IMMIGRATION	FEDERAL TAX SUITS	☐ 893 Environmental Matters
☐ 210 Land Condemnation	☐ 440 Other Civil Rights	**Habeas Corpus:**	☐ 462 Naturalization Application	☐ 870 Taxes (U.S. Plaintiff or Defendant)	☐ 895 Freedom of Information Act
☐ 220 Foreclosure	☐ 441 Voting	☐ 463 Alien Detainee	☐ 465 Other Immigration Actions	☐ 871 IRS—Third Party 26 USC 7609	☐ 896 Arbitration
☐ 230 Rent Lease & Ejectment	☐ 442 Employment	☐ 510 Motions to Vacate Sentence			☒ 899 Administrative Procedure Act/Review or Appeal of Agency Decision
☐ 240 Torts to Land	☐ 443 Housing/ Accommodations	☐ 530 General			☐ 950 Constitutionality of State Statutes
☐ 245 Tort Product Liability	☐ 445 Amer. w/Disabilities - Employment	☐ 535 Death Penalty			
☐ 290 All Other Real Property	☐ 446 Amer. w/Disabilities - Other	**Other:** ☐ 540 Mandamus & Other ☐ 550 Civil Rights ☐ 555 Prison Condition ☐ 560 Civil Detainee - Conditions of Confinement			
	☐ 448 Education				

V. ORIGIN *(Place an "X" in One Box Only)*

☒ 1 Original Proceeding ☐ 2 Removed from State Court ☐ 3 Remanded from Appellate Court ☐ 4 Reinstated or Reopened ☐ 5 Transferred from Another District *(specify)* ☐ 6 Multidistrict Litigation - Transfer ☐ 8 Multidistrict Litigation - Direct File

VI. CAUSE OF ACTION

Cite the U.S. Civil Statute under which you are filing ***(Do not cite jurisdictional statutes unless diversity)***:
5 U.S.C. §706

Brief description of cause:
Violations of the Administrative Procedure Act

VII. REQUESTED IN COMPLAINT:

☐ CHECK IF THIS IS A **CLASS ACTION** UNDER RULE 23, F.R.Cv.P.

DEMAND $

CHECK YES only if demanded in complaint:
JURY DEMAND: ☐ Yes ☐ No

VIII. RELATED CASE(S) IF ANY

(See instructions): JUDGE _____ DOCKET NUMBER _____

DATE
Sep 28, 2022

SIGNATURE OF ATTORNEY OF RECORD
/s/ Bruce A. Smith

FOR OFFICE USE ONLY

RECEIPT # _____ AMOUNT _____ APPLYING IFP _____ JUDGE _____ MAG. JUDGE _____

Exhibit A

Unfair, Deceptive, or Abusive Acts or Practices

Unfair, deceptive, or abusive acts and practices (UDAAPs) can cause significant financial injury to consumers, erode consumer confidence, and undermine the financial marketplace. Under the Dodd-Frank Act, it is unlawful for any provider of consumer financial products or services or a service provider to engage in any unfair, deceptive or abusive act or practice.[1] The Act also provides CFPB with rule-making authority and, with respect to entities within its jurisdiction, enforcement authority to prevent unfair, deceptive, or abusive acts or practices in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service.[2] In addition, CFPB has supervisory authority for detecting and assessing risks to consumers and to markets for consumer financial products and services.[3]

As examiners review products or services, such as deposit products or lending activities, they generally should identify the risks of harm to consumers that are particular to those activities. Examiners also should review products that combine features and terms in a manner that can increase the difficulty of consumer understanding of the overall costs or risks of the product and the potential harm to the consumer associated with the product.

These examination procedures provide general guidance on:

- The principles of unfairness, deception, and abuse in the context of offering and providing consumer financial products and services;
- Assessing the risk that an institution's practices may be unfair, deceptive, or abusive;
- Identifying unfair, deceptive or abusive acts or practices (including by providing examples of potentially unfair or deceptive acts and practices); and
- Understanding the interplay between unfair, deceptive, or abusive acts or practices and other consumer protection and antidiscrimination statutes.

Unfair Acts or Practices

The standard for unfairness in the Dodd-Frank Act is that an act or practice is unfair when:

(1) It causes or is likely to cause substantial injury to consumers;

(2) The injury is not reasonably avoidable by consumers; and

[1] Dodd-Frank Act, Title X, Subtitle C, Sec. 1036; PL 111-203 (July 21, 2010).

[2] Sec. 1031 of the Dodd-Frank Act. The principles of "unfair" and "deceptive" practices in the Act are similar to those under Sec. 5 of the Federal Trade Commission Act (FTC Act). The Federal Trade Commission (FTC) and federal banking regulators have applied these standards through case law, official policy statements, guidance, examination procedures, and enforcement actions that may inform CFPB.

[3] Dodd-Frank Act, Secs. 1024; 1025(b)(1); 1026(b) of the Act.

(3) The injury is not outweighed by countervailing benefits to consumers or to competition.[4]

- ***The act or practice must cause or be likely to cause substantial injury to consumers.***
  Substantial injury usually involves monetary harm. Monetary harm includes, for example, costs or fees paid by consumers as a result of an unfair practice.[5] An act or practice that causes a small amount of harm to a large number of people may be deemed to cause substantial injury. Foregone monetary benefits or denial of access to products or services, like that which may result from discriminatory behavior, may also cause substantial injury.

  Actual injury is not required in every case. A significant risk of concrete harm is also sufficient. However, trivial or merely speculative harms are typically insufficient for a finding of substantial injury. Emotional impact and other more subjective types of harm also will not ordinarily amount to substantial injury. Nevertheless, in certain circumstances, such as unreasonable debt collection harassment or discriminatory conduct, emotional impacts or dignitary harms may amount to or contribute to substantial injury.

- ***Consumers must not be reasonably able to avoid the injury.***
  An act or practice is not considered unfair if consumers may reasonably avoid injury. Consumers cannot reasonably avoid injury if the act or practice interferes with their ability to effectively make decisions or to take action to avoid injury. Normally the marketplace is self-correcting; it is governed by consumer choice and the ability of individual consumers to make their own private decisions without regulatory intervention. If material information about a product, such as pricing, is modified after the consumer has committed to purchasing the product, or withheld, the consumer cannot reasonably avoid the injury. Moreover, consumers cannot avoid injury if they are coerced into purchasing unwanted products or services or if a transaction occurs without their knowledge or consent. Consumers cannot reasonably avoid discrimination.

  A key question is <u>not</u> whether a consumer could have made a better choice. Rather, the question is whether an act or practice hinders a consumer's decision-making. For example, not having access to important information could prevent consumers from comparing available alternatives, choosing those that are most desirable to them, and avoiding those that are inadequate or unsatisfactory. In addition, if almost all market participants engage in a practice, a consumer's incentive to search elsewhere for better terms is reduced, and the practice may not be reasonably avoidable.[6]

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[4] The standard for unfairness in the Dodd-Frank Act has the same three-part test as the FTC Act. This standard was first stated in the FTC Policy Statement on Unfairness (Dec. 17, 1980), *available at*: http://www.ftc.gov/bcp/policystmt/ad-unfair.htm. Congress later amended the FTC Act to include this specific standard in the Act itself. 15 U.S.C. § 45(n).

[5] FTC Policy Statement on Unfairness, at p. 3.

[6] *See* Credit Practices Rule, 49 Fed. Reg. 7740, 7746 (1984).

For an injury to be reasonably avoidable, consumers must have practical means to avoid it, and the actions that a consumer is expected to take to avoid injury must be reasonable. While a consumer might avoid harm by hiring independent experts to test products in advance or by bringing legal claims for damages in every case of harm, these actions generally would be too expensive to be practical for individual consumers and, therefore, are not reasonable. There are many instances where consumers simply have no mechanism to avoid the injury. For example, consumers typically cannot avoid the harms of discrimination.

- ***The injury must not be outweighed by countervailing benefits to consumers or competition.***

  To be unfair, the act or practice must be injurious in its net effects — that is, the injury must not be outweighed by any offsetting consumer or competitive benefits that also are produced by the act or practice. Offsetting consumer or competitive benefits of an act or practice may include lower prices to the consumer or a wider availability of products and services resulting from competition.

  Costs that would be incurred for measures to prevent the injury also are taken into account in determining whether an act or practice is unfair. These costs may include the costs to the institution in taking preventive measures and the costs to society as a whole of any increased burden and similar matters.

Public policy, as established by statute, regulation, judicial decision, or agency determination, may be considered with all other evidence to determine whether an act or practice is unfair. However, public policy considerations by themselves may not serve as the primary basis for determining that an act or practice is unfair.

Examples

The examples described below stem from federal enforcement actions. They provide insight into practices that have been alleged to be unfair by other regulators and may inform CFPB's determinations. However, the particular facts in a case are crucial to a determination of unfairness. It is important to bear in mind that a change in facts could change the appropriate determination. Moreover, the brief summaries below do not present all of the material facts relevant to the determinations in each case. The examples show how the unfairness standard may be applied.

Refusing to release lien after consumer makes final payment on a mortgage.[7] The Federal Trade Commission (FTC) brought an enforcement action against a mortgage company based on allegations, described below, that the company repeatedly failed to release liens after consumers fully paid the amount due on their mortgages.

[7] *FTC v. Capital City Mortgage Corp.*, Civil No. 98 CV-237 (D.D.C. Feb. 2005), *available at* http://www.ftc.gov/opa/2005/02/capitalcity.shtm.

- Substantial injury. Consumers sustained economic injury when the mortgage servicer did not release the liens on their properties after the consumers had repaid the total amount due on the mortgages.

- Not outweighed by benefits. Countervailing benefits to competition or consumers did not result from the servicer's alleged failure to appropriately service the mortgage loan and release the lien promptly.

- Not reasonably avoidable. Consumers had no way to know in advance of obtaining the loan that the mortgage servicer would not release the lien after full payment. Moreover, consumers generally cannot avoid the harm caused by an improper practice of a mortgage servicer because the servicer is chosen by the owner of the loan, not the borrower. Thus, consumers cannot choose their loan servicer and cannot change loan servicers when they are dissatisfied with the quality of the loan servicing.

Dishonoring credit card convenience checks without notice.[8] The Office of Thrift Supervision (OTS) and Federal Deposit Insurance Corporation (FDIC) brought enforcement actions against a credit card issuer that sent convenience checks with stated credit limits and expiration dates to customers. For a significant percentage of consumers, the issuer reduced credit lines after the checks were presented, and then the issuer dishonored the consumers' checks.

- Substantial injury. Consumers paid returned-check fees and may have experienced a negative impact on credit history.

- Not outweighed by benefits. The card issuer later reduced credit limits based on credit reviews. Based on the particular facts involved in the case, the harm to consumers from the dishonored convenience checks outweighed any benefit of using new credit reviews.

- Not reasonably avoidable. Consumers reasonably relied on their existing credit limits and expiration dates on the checks when deciding to use them for a payment. Consumers had received no notice that the checks they used were being dishonored until they learned from the payees. Thus, consumers could not reasonably have avoided the injury.

Processing payments for companies engaged in fraudulent activities.[9] The Office of the Comptroller of the Currency (OCC) brought an enforcement action in a case involving a bank that maintained deposit account relations with telemarketers and payment processors, based on the following allegations. The telemarketers regularly deposited large numbers of remotely created checks drawn against consumers' accounts. A large percentage of the checks were not authorized by consumers. The bank failed to establish appropriate policies and procedures to prevent, detect, or remedy such activities.

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[8] *In re American Express Bank, FSB* (Cease and Desist Order WN-09-016, and Order of Assessment of a Civil Money Penalty for $250,000, WN-09-017, June 29, 2009) OTS Docket No. 15648; *In re American Express Centurion Bank*, (Cease and Desist Order, June 30, 2009) Docket FDIC-09-251b, available at http://www.fdic.gov/news.

[9] *In re Wachovia Bank, National Association*, available at http://www.occ.treas.gov

- Substantial injury. Consumers lost money from fraudulent checks created remotely and drawn against their accounts.
- Not outweighed by benefits. The cost to the bank of establishing a minimum level of due diligence, monitoring, and response procedures sufficient to remedy the problem would have been far less than the amount of injury to consumers that resulted from the bank's avoiding those costs.
- Not reasonably avoidable. Consumers could not avoid the harm because the harm resulted principally from transactions to which the consumers had not consented.

Deceptive Acts or Practices

A representation, omission, act, or practice is deceptive when

(1) The representation, omission, act, or practice misleads or is likely to mislead the consumer;

(2) The consumer's interpretation of the representation, omission, act, or practice is reasonable under the circumstances; and

(3) The misleading representation, omission, act, or practice is material.[10]

- ***There must be a representation, omission, act, or practice that misleads or is likely to mislead the consumer.***

  Deception is not limited to situations in which a consumer has already been misled. Instead, an act or practice may be deceptive if it is *likely to mislead* consumers.

  It is necessary to evaluate an individual statement, representation, or omission not in isolation, but rather in the context of the entire advertisement, transaction, or course of dealing, to determine whether the overall net impression is misleading or deceptive. A representation may be an express or implied claim or promise, and it may be written or oral. If material information is necessary to prevent a consumer from being misled, it may be deceptive to omit that information.

  Written disclosures may be insufficient to correct a misleading statement or representation, particularly where the consumer is directed away from qualifying limitations in the text or is counseled that reading the disclosures is unnecessary. Likewise, oral or fine print disclosures or contract disclosures may be insufficient to cure a misleading headline or a prominent written representation. Similarly, a deceptive act or practice may not be cured by subsequent truthful disclosures.

  Acts or practices that may be deceptive include: making misleading cost or price claims; offering to provide a product or service that is not in fact available; using bait-and-switch

[10] *See* FTC Policy Statement on Deception, available at http://www.ftc.gov/bcp/policystmt/ad-decept.htm. Examiners should be informed by the FTC's standard for deception.

techniques; omitting material limitations or conditions from an offer; or failing to provide the promised services.

The FTC's "four Ps" test can assist in the evaluation of whether a representation, omission, act, or practice is likely to mislead:

- Is the statement prominent enough for the consumer to notice?
- Is the information presented in an easy-to-understand format that does not contradict other information in the package and at a time when the consumer's attention is not distracted elsewhere?
- Is the placement of the information in a location where consumers can be expected to look or hear?
- Finally, is the information in close proximity to the claim it qualifies?[11]

- ***The representation, omission, act, or practice must be considered from the perspective of the reasonable consumer.***

  In determining whether an act or practice is misleading, one also must consider whether the consumer's interpretation of or reaction to the representation, omission, act, or practice is reasonable under the circumstances. In other words, whether an act or practice is deceptive depends on how a reasonable member of the target audience would interpret the representation. When representations or marketing practices target a specific audience, such as older Americans, young people, or financially distressed consumers, the communication must be reviewed from the point of view of a reasonable member of that group.

  Moreover, a representation may be deceptive if the majority of consumers in the target class do not share the consumer's interpretation, so long as a significant minority of such consumers is misled. When a seller's representation conveys more than one meaning to reasonable consumers, one of which is false, the seller is liable for the misleading interpretation.

  Exaggerated claims or "puffery," however, are not deceptive if the claims would not be taken seriously by a reasonable consumer.

- ***The representation, omission, or practice must be material.***

  A representation, omission, act, or practice is material if it is likely to affect a consumer's choice of, or conduct regarding, the product or service. Information that is important to consumers is material.

  Certain categories of information are presumed to be material. In general, information about the central characteristics of a product or service – such as costs, benefits, or

[11] FTC, *Dot Com Disclosures, Information about On-Line Advertising*, available at: http://business.ftc.gov/documents/bus41-dot-com-disclosures-information-about-online-advertising.pdf.

restrictions on the use or availability – is presumed to be material. Express claims made with respect to a financial product or service are presumed material. Implied claims are presumed to be material when evidence shows that the institution intended to make the claim (even though intent to deceive is not necessary for deception to exist).

Claims made with knowledge that they are false are presumed to be material. Omissions will be presumed to be material when the financial institution knew or should have known that the consumer needed the omitted information to evaluate the product or service.

If a representation or claim is not presumed to be material, it still would be considered material if there is evidence that it is likely to be considered important by consumers.

Examples

The examples described below stem from federal enforcement actions. They provide insight into practices that have been alleged to be deceptive by other regulators and may inform CFPB's determinations. However, as with unfairness, the particular facts in a case are crucial to a determination of deception. It is important to bear in mind that a change in facts could change the appropriate determination. Moreover, the brief summaries below do not present all of the material facts relevant to the determinations in each case. The examples show how the deception standard may be applied.

Inadequate disclosure of material lease terms in television advertising.[12] The FTC brought actions against vehicle leasing companies alleging that their television advertisements represented that consumers could lease vehicles for "$0 down" when advertising a monthly lease payment. However, the FTC alleged that the "blur" of "unreadable fine print" that flashed on the screen at the end of the advertisement disclosed costs of at least $1,000. The settlements prohibited the vehicle leasing companies from misrepresenting the amount consumers must pay when signing the lease.

In addition, the FTC required that if the companies make any representation about the amounts due at lease signing, or that there is "no down payment," the companies must make an equally prominent (readable and audible) disclosure of the total amount of all fees due when consumers sign the lease.

- Representation or omission likely to mislead. The television advertisements featured prominent statements of "no money down" or "$0 down" at lease signing. The advertisement also contained, at the bottom of the screen, a "blur" of small print in which disclosures of various costs required by Regulation M (the Consumer Leasing Act) were made. The FTC alleged that the disclosures were inadequate because they were not clear, prominent, or audible to consumers.

[12] *In the matters of Mazda Motor of America, Inc.; Mitsubishi Motor Sales of America, Inc.; American Honda Motor Company, Inc.; General Motors Corporation; American Isuzu Motors, Inc.*, available at http://www.ftc.gov/opa/1997/02/petapp09.shtm.

- Reasonable consumer perspective. A reasonable consumer would believe that he did not have to put any money down and that all he owed was the regular monthly payment.

- Material representation. The stated "no money down" or "$0 down" plus the low monthly lease payment were material representations to consumers. The fact that the additional, material costs were disclosed at signing of the lease did not cure the deceptive failure to disclose in the television advertising, the FTC claimed.

Misrepresentation about loan terms.[13] In 2004, the FTC sued a mortgage broker advertising mortgage refinance loans at "3.5% fixed payment 30-year loan" or "3.5% fixed payment for 30 years," implying that the offer was for a 30-year loan with a 3.5% fixed interest rate. Instead, the FTC claimed that the broker offered adjustable rate mortgages (ARMs) with an option to pay various amounts, including a minimum monthly payment that represented only a portion of the required interest. As a result, unpaid interest was added to the principal of the loan, resulting in negative amortization.[14]

- Practice likely to mislead. The FTC claimed that the advertisements were misleading because they compared payments on a mortgage that fully amortized to payments on a non-amortizing loan with payments that increased after the first year. In addition, the FTC claimed that after application, the broker provided Truth in Lending Act (TILA) disclosures that misstated the annual percentage rate (APR) and that failed to state that the loan was a variable rate loan.

- Reasonable consumer perspective. It was reasonable for consumers to believe that they would obtain fixed-rate mortgages, based on the representations.

- Material representation. The representations were material because consumers relied on them when making the decision to refinance their fully amortizing 30-year fixed loans. As a result, the consumers ended up with adjustable rate mortgages that would negatively amortize if they made payments at the stated 3.5% payment rate.

[13] FTC v. Chase Financial Funding, Inc., No. SACV04-549 (C.D.Cal. 2004), Stipulated Preliminary Injunction, available at http://www.ftc.gov/os/caselist/0223287/0223287.shtm.

[14] In 2008, amendments to the Truth in Lending Act's Regulation Z were adopted to prohibit certain advertising practices, such as misleading advertising of fixed rates and payments, for credit secured by a dwelling. Similar practices could be identified as deceptive in other product lines. See 73 Fed. Reg. 44522 (July 30, 2008) (promulgating 12 CFR 226.24), which has since been recodified as 12 CFR 1026.24.

Abusive Acts or Practices

The Dodd-Frank Act makes it unlawful for any covered person or service provider to engage in an "abusive act or practice."[15] An abusive act or practice:

- Materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service or
- Takes unreasonable advantage of:
  - A lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service;
  - The inability of the consumer to protect its interests in selecting or using a consumer financial product or service; or
  - The reasonable reliance by the consumer on a covered person to act in the interests of the consumer.

Although abusive acts also may be unfair or deceptive, examiners should be aware that the legal standards for abusive, unfair, and deceptive each are separate.

The Role of Consumer Complaints in Identifying Unfair, Deceptive, or Abusive Acts or Practices

Consumer complaints play a key role in the detection of unfair, deceptive, or abusive practices. Consumer complaints have been an essential source of information for examinations, enforcement, and rule-making for regulators. As a general matter, consumer complaints can indicate weaknesses in elements of the institution's compliance management system, such as training, internal controls, or monitoring.

While the absence of complaints does not ensure that unfair, deceptive, or abusive practices are not occurring, complaints may be one indication of UDAAPs. For example, the presence of complaints alleging that consumers did not understand the terms of a product or service may be a red flag indicating that examiners should conduct a detailed review of the relevant practice. This is especially true when numerous consumers make similar complaints about the same product or service. Because the perspective of a reasonable consumer is one of the tests for evaluating whether a representation, omission, act, or practice is potentially deceptive, consumer complaints alleging misrepresentations or misunderstanding may provide a window into the perspective of the reasonable consumer.

When reviewing complaints against an institution, examiners should consider complaints lodged against subsidiaries, affiliates, and third parties regarding the products and services offered through the institution or using the institution's name. In particular, examiners should determine

[15] Dodd-Frank Act, Sec. 1036(a)(1)(B), 12 U.S.C. § 5536(a)(1)(B).

whether an institution itself receives, monitors, and responds to complaints filed against subsidiaries, affiliates, and third parties. Consumers can file complaints at a number of entities: the institution itself, the Better Business Bureau, State Attorneys General, the FTC's Consumer Sentinel, the CFPB Consumer Response Center, other Federal and State agencies, or on-line consumer complaint boards such as www.ripoffreport.com or www.complaints.com.

Analyzing Complaints

Analysis of consumer complaints may assist in the identification of potential unfair, deceptive, or abusive practices. Examiners should consider the context and reliability of complaints; every complaint does not indicate violation of law. When consumers repeatedly complain about an institution's product or service, however, examiners should flag the issue for possible further review. Moreover, even a single substantive complaint may raise serious concerns that would warrant further review. Complaints that allege, for example, misleading or false statements, or missing disclosure information, may indicate possible unfair, deceptive, or abusive acts or practices needing review.

Another area that could indicate potential unfair, deceptive, or abusive acts or practices is a high volume of charge-backs or refunds for a product or service. While this information is relevant to the consumer complaint analysis, it may not appear in the institution's complaint records.

Relationship to Other Laws

An unfair, deceptive, or abusive act or practice may also violate other federal or state laws. For example, pursuant to the TILA, creditors must "clearly and conspicuously" disclose the costs and terms of credit. An act or practice that does not comply with these provisions of TILA may also be unfair, deceptive, or abusive. Similarly, a discriminatory act or practice that is unfair, deceptive, or abusive may also violate other antidiscrimination laws, such as ECOA.

Conversely, a transaction that is in technical compliance with other federal or state laws may nevertheless violate the prohibition against UDAAPs. For example, an advertisement may comply with TILA's requirements, but contain additional statements that are untrue or misleading, and compliance with TILA's disclosure requirements does not insulate the rest of the advertisement from the possibility of being deceptive. A discriminatory act or practice is not shielded from the possibility of being unfair, deceptive or abusive even when fair lending laws do not apply to the conduct. For example, not allowing African-American consumers to open deposit accounts, or subjecting African-American consumers to different requirements to open deposit accounts, may be an unfair practice even in those instances when ECOA does not apply to this type of transaction.

Unfair, Deceptive, or Abusive Acts and Practices

Exam Date:	[Click & type]
Prepared By:	[Click & type]
Reviewer:	[Click & type]
Docket #:	[Click & type]
Entity Name:	[Click & type]

Examination Objectives

- To assess the quality of the regulated entity's compliance risk management systems, including internal controls and policies and procedures, for avoiding unfair, deceptive, or abusive acts or practices (UDAAP).
- To identify acts or practices that materially increase the risk of consumers being treated in an unfair, deceptive, or abusive manner, including discriminatory acts or practices.
- To gather facts that help determine whether a regulated entity engages in acts or practices when offering or providing consumer financial products or services that are likely to be unfair, deceptive, or abusive.
- To determine, in consultation with Headquarters, whether an unfair, deceptive or abusive act or practice has occurred and whether further supervisory or enforcement actions are appropriate.

General Guidance

Based on the results of the risk assessment of the entity, examiners should review for potential unfair, deceptive, or abusive acts or practices, taking into account an entity's marketing programs, product and service mix, customer base, and other factors, as appropriate. Even if the risk assessment has not identified potential unfair, deceptive, or abusive acts or practices, examiners should be alert throughout an examination for situations that warrant review.

1. Document Review

To initially identify potential areas of UDAAP concerns, obtain and review copies of the following to the extent relevant to the examination

a. Training materials.

b. Lists of products and services, including descriptions, fee structure, disclosures, notices, agreements, and periodic and account statements.

c. Procedure manuals and written policies, including those for servicing and collections.

d. Minutes of the meetings of the Board of Directors and of management committees, including those related to compliance.

e. Internal control monitoring and auditing materials.

f. Compensation arrangements, including incentive programs for employees and third parties.

g. Documentation related to new product development, including relevant meeting minutes of Board of Directors, and of compliance and new product committees.

h. Marketing programs, advertisements, and other promotional material in all forms of media (including print, radio, television, telephone, Internet, or social media advertising).

i. Scripts and recorded calls for telemarketing and collections.

j. Organizational charts, including those related to affiliate relationships and work processes.

k. Agreements with affiliates and third parties that interact with consumers on behalf of the entity.

l. Consumer complaint files.

m. Documentation related to software development and testing, as applicable.

n. Documentation regarding the use of models, algorithms, and decision-making processes used in connection with consumer financial products and services.

o. Information collected, retained or used regarding customer demographics, including the demographics of customers using various products or services, and the breakdown of consumer demographics for various product uses, fees, revenue sources and costs, or the impacts of various products and services on specific demographics.

p. Any demographic research or analysis relating to marketing or advertising of consumer financial products or services.

Management and Policy-Related Examination Procedures

1. Identify potential UDAAP concerns by reviewing all relevant written policies and procedures, customer complaints received by the entity or by the CFPB, internal and external audit reports, statistical and management reports, and examination reports. Determine whether:

a. The scope of the entity's compliance audit includes a review of potential unfair, deceptive, or abusive acts or practices.

b. The compliance audit work is performed consistent with the audit plan and scope.

c. The frequency and depth of audit review is appropriate to the nature of the activities and size of the entity.

d. Management and the Board of Directors are made aware of and review significant deficiencies and their causes.

e. Management has taken corrective actions to follow up on any identified deficiencies.

f. The entity's compliance programs ensure that policies are being followed through its sampling of relevant product types and decision centers, including sales, processing, and underwriting.

g. The entity has a process to respond to consumer complaints in a timely manner and determine whether consumer complaints raise potential UDAAP concerns.

h. The entity has been subject to any enforcement actions or has been investigated by a regulatory or law enforcement agency for violations of consumer protection laws or regulations that may indicate potential UDAAP concerns.

i. The entity has a process to prevent discrimination in relation to all aspects of consumer financial products or services the entity offers or provides, which includes the evaluation of all policies, procedures and processes for discrimination prior to implementation or making changes, and continued monitoring for discrimination after implementation.

j. The entity's compliance program includes an established process for periodic analysis and monitoring of all decision-making processes used in connection with consumer financial products or services, and a process to take corrective action to address any potential UDAAP concerns related to their use, including discrimination.

2. Through discussions with management and a review of available information, determine whether the entity's internal controls are adequate to prevent unfair, deceptive or abusive acts or practices. Consider whether:

a. The compliance management program includes measures aimed at avoiding unfair, deceptive, or abusive practices, including:

- Organization charts and process flowcharts;
- Policies and procedures; and
- Monitoring and audit procedures.

b. The entity conducts prior UDAAP reviews of advertising and promotional materials, including promotional materials and marketing scripts for new products.

c. The entity evaluates initial and subsequent disclosures, including customer agreements and changes in terms, for potential UDAAP concerns.

d. The entity reviews new products and changes in the terms and conditions of existing products for potential UDAAP concerns.

e. The entity has a thorough process for receiving and responding to consumer complaints and has a process to receive complaints made to third parties, such as the Better Business Bureau or the CFPB.

f. The entity evaluates servicing and collections for UDAAP concerns.

g. The entity has established policies and controls relating to employee and third-party conduct, including:
   - Initial and ongoing training;
   - Performance reviews or audits;
   - Discipline policies and records of disciplinary actions;
   - Third-party agreements and contractual performance standards;
   - Compensation programs; and
   - Monitoring.

h. The entity's internal control processes are documented.

i. Computer programs are tested and documented to ensure accurate and timely disclosures to consumers.

j. The entity has established policies and procedures to review, test, and monitor any decision-making processes it uses for potential UDAAP concerns, including discrimination.

k. The entity has established policies and procedures to mitigate potential UDAAP concerns arising from the use of its decision-making processes, including discrimination.

l. The entity's policies, procedures and practices do not target or exclude consumers from products and services, or offer different terms and conditions, in a discriminatory manner.

m. The entity has appropriate training for customer service personnel to prevent discrimination.

3. Potential Areas for Transaction Testing

Through a high-level assessment of the entity's products, services, and customer base, identify areas for potential transaction testing. This process should determine whether:

a. The entity does not underwrite a given credit product on the basis of ability to repay.

b. A product's profitability depends significantly on penalty fees or "back-end" rather than upfront fees.

c. A product has high rates of repricing or other changes in terms.

d. A product combines features and terms in a manner that can increase the difficulty of consumer understanding of the overall costs or risks of the product and the potential harm.

e. Penalties are imposed when a customer terminates the relationship with the entity.

f. Fees or other costs are imposed on a consumer to obtain information about the account.

g. A product is targeted to particular populations, without appropriate tailoring of marketing, disclosures, and other materials designed to ensure understanding by the consumers.

h. The entity improperly gives inferior terms to one customer demographic as compared to other customer demographics.

i. The entity improperly offers or provides more products or services to one customer demographic as compared to other customer demographics.

j. Customer service representatives improperly treat customers of certain demographics worse or provide extra assistance or exceptions to customers of certain demographics.

k. The entity engages in targeted advertising or marketing in a discriminatory way.

l. The entity uses decision-making processes in its eligibility determinations, underwriting, pricing, servicing or collections that result in discrimination.

m. The entity fails to evaluate and make necessary adjustments and corrections to prevent discrimination.

Transaction-Related Examination Procedures

If upon conclusion of the management and policy-related examination procedures, procedural weaknesses, or other UDAAP risks require further investigation, conduct transaction testing, as necessary, using the following examination procedures. Use judgment in deciding to what extent to sample individual products, services, or marketing programs. Increase the sample size to achieve confidence that all aspects of the entity's products and services are reviewed sufficiently. Consult with Headquarters to obtain assistance with the sampling process.

1. Marketing and Disclosures

Through a review of marketing materials, customer agreements, and other disclosures, determine whether, before the consumer chooses to obtain the product or service:

a. All representations are factually based.

b. All materials describe clearly, prominently, and accurately:

- costs, benefits, and other material terms of the products or services being offered;
- related products or services being offered either as an option or required to obtained certain terms; and

- material limitations or conditions on the terms or availability of products and services, such as time limitations for favorable rates, promotional features, expiration dates, prerequisites for obtaining particular products or services, or conditions for canceling services.

c. The customer's attention is drawn to key terms, including limitations and conditions, that are important to enable the consumer to make an informed decision.

d. All materials clearly and prominently disclose the fees, penalties, and other charges that may be imposed and the reason for the imposition.

e. Contracts clearly inform customers of contract provisions that permit changes in terms and conditions of the product or service.

f. All materials clearly communicate the costs, benefits, availability, and other terms in language that can be understood when products are targeted to particular populations, such as reverse mortgage loans for the elderly.

g. Materials do not misrepresent costs, conditions, limitations, or other terms either affirmatively or by omission.

h. The entity avoids advertising terms that are generally not available to the typical targeted consumer.

i. Marketing or advertising do not improperly target or exclude consumers on a discriminatory basis, including through digital advertising.

2. Availability of Terms or Services as Advertised

Evaluate whether product(s) and service(s) that consumers are receiving are consistent with the disclosures and policies. For each product and service being reviewed, select a sample that:

a. Is sufficient in size to reach a supportable conclusion about such consistency;

b. Includes, as appropriate, transactions from different origination and underwriting channels — for example, different geographical areas or different sectors of the entity's organization structure;

c. Includes approved and/or denied accounts; and

d. Identifies the decision-making processes used to determine approval or denial for a product and the terms of the offer, as well as the corresponding inputs used in the decision-making processes for each account in the sample.

Determine whether:

a. Consumers are reasonably able to obtain the products and services, including interest rates or rewards, as represented by the entity.

b. The entity offers products and services to consumers in a manner that prevents discrimination.

c. Consumers receive the specific product or service that they request.

d. Counter-offers clearly, prominently, and accurately explain the difference between the original product or services requested and the one being offered.

e. Actual practices are consistent with stated policies, procedures, or account disclosures.

3. Availability of Actual Credit to the Consumer

Evaluate whether the entity represents the amount of useable credit that the consumer will receive in a truthful way. Consider whether:

a. The available credit is sufficient to allow the consumer to use the product as advertised and disclosed to the consumer.

b. The fees and charges, typically imposed on the average targeted customer, both initially and throughout the term of the loan, remain in a range that does not prevent the availability of credit.

c. The entity honors convenience checks when used by the customer in a manner consistent with introductory or promotional materials and disclosures.

4. Employees and Third Parties Interacting with Consumers

Evaluate how the entity monitors the activities of employees and third-party contractors, marketing sales personnel, vendors, and service providers to ensure they do not engage in unfair, deceptive, or abusive acts or practices with respect to consumer interactions. Interview employees and third parties, as appropriate. Specifically, consider whether:

a. The entity ensures that employees and third parties who market or promote products or services are adequately trained so that they do not engage in unfair, deceptive, or abusive acts or practices, including discrimination.

b. The entity conducts periodic evaluations or audits to check whether employees or third parties follow the entity's training and procedures and has a disciplinary policy in place to deal with any deficiencies.

c. The entity reviews compensation arrangements for employees, third-party contractors, and service providers to ensure that they do not create unintended incentives to engage in unfair, deceptive, or abusive acts or practices, particularly with respect to product sales, loan originations, and collections.

d. Performance evaluation criteria do not create unintended incentives to engage in unfair, deceptive, or abusive acts or practices, including criteria for sales personnel based on sales volume, size, terms of sale, or account performance.

e. The entity implements and maintains effective risk and supervisory controls to select and manage third-party contractors and service providers.

f. The entity has a process to take prompt corrective action if the decision-making processes it uses produce deficiencies or discriminatory results.

5. Servicing and Collections

Evaluate whether servicing and collections practices raise potential UDAAP concerns, by considering whether**:**

a. The entity has policies detailing servicing and collections practices and has monitoring systems to prevent unfair, deceptive or abusive acts or practices.

b. Call centers, either operated by the entity itself or by third parties, effectively respond to consumers' calls, including calls from consumers with limited English proficiency.

c. The entity ensures that employees and third party contractors:

- represent fees or charges on periodic statements in a manner that is not misleading;
- post and credit consumer payments in a timely manner;
- apply payments in a manner that does not unnecessarily increase customer payments, without clear justification;
- only charge customers for products and services, such as insurance or credit protection programs, that are specifically agreed to;
- mail periodic statements in time to provide the consumer ample opportunity to avoid late payments; and
- do not represent to consumers that they may pay less than the minimum amount without clearly and prominently disclosing any fees for paying the reduced amount.

d. The entity ensures that employees and third party contractors refrain from engaging in servicing or collection practices that lead to differential treatment or disproportionately adverse impacts on a discriminatory basis.

e. The entity has policies to ensure compliance with the standards under the Fair Debt Collections Practices Act to prevent abusive, deceptive, or unfair debt collection practices.

f. Employees and third party contractors clearly indicate to consumers that they are calling about the collection of a debt.

g. Employees and third party contractors do not disclose the existence of a consumer's debt to the public without the consent of the consumer, except as permitted by law.

h. The entity avoids repeated telephone calls to consumers that annoy, abuse, or harass any person at the number called.

6. Interviews with Consumers

If potential UDAAP issues are identified that would necessitate interviews with consumers, consult with regional management who will confer with Headquarters.

Exhibit B

Consumer Financial Protection Bureau (cfpb.gov/)

Cracking down on discrimination in the financial sector

By Eric Halperin and Lorelei Salas – MAR 16, 2022

Discrimination has a long and ugly history in our nation—and blatant acts of discrimination continue to occur every day. New manifestations of discrimination, embedded within systems and technologies, harm communities even where such acts are not visible. The COVID-19 pandemic brought into sharper focus the inequities that continue to plague the country, and the Consumer Financial Protection Bureau will fight to end discrimination in the financial sector.

We enforce a number of laws that can target discriminatory practices, including the Consumer Financial Protection Act (CFPA). The CFPA empowers us to identify, prohibit, and prosecute unfair, deceptive, and abusive acts or practices committed by any covered person or service provider in connection with any transaction for, or offer of, a consumer financial product or service. The CFPA defines an act or practice as unfair when 1) it causes or is likely to cause substantial injury to consumers that is not reasonably avoidable, and 2) such substantial injury is not outweighed by countervailing benefits to consumers or competition.

When people of color suffer racist conduct in the financial marketplace, it can cause substantial monetary and non-monetary harms. Depending on how the conduct occurs (face-to-face, digital, systematic, etc.), many individuals may be unaware they received disparate treatment or a discriminatory outcome. Even when they are aware, there can be a feeling of unavoidability or powerlessness to stop the discrimination.

However, such practices fall squarely within our mandate to address and eliminate unfair practices. For example, Director Chopra has spoken (https://www.consumerfinance.gov/about-us/newsroom/remarks-of-director-rohit-chopra-at-a-joint-doj-cfpb-and-occ-press-conference-on-the-trustmark-national-bank-enforcement-action/) about the work the CFPB will undertake to focus on the widespread and growing reliance on machine learning models throughout the financial industry and their potential for perpetuating biased outcomes.

Additionally, certain targeted advertising and marketing, based on machine learning models, can harm consumers and undermine competition. Consumer

advocates, investigative journalists, and scholars have shown how data harvesting and consumer surveillance fuel complex algorithms that can target highly specific demographics of consumers to exploit perceived vulnerabilities and strengthen structural inequities. We will be closely examining companies' reliance on automated decision-making models and any potential discriminatory outcomes.

As part of our broad efforts to identify and address unfair acts and practices, we recently announced changes to the manual we use to guide our supervision of covered financial institutions. Under the updated examination guidelines, we will continue to scrutinize any conduct of covered institutions that violates the federal prohibition against unfair practices, including determining if an entity has unfairly discriminated against certain people.

The updated manual guides examiners in looking beyond discrimination directly connected to fair lending laws, asking them to review any policies or practices that exclude individuals from products and services, or offer products or services with different terms, in an unfairly discriminatory manner. For example, not allowing people of color to open deposit accounts may be an unfair practice even in those instances when the Equal Credit Opportunity Act (ECOA) does not apply to this type of transaction.

However, vigorous enforcement of the ECOA continues to be essential for us to achieve broader equity and opportunity. Under Director Chopra, we will prioritize enforcement of the ECOA to ensure that no one suffers discrimination with respect to any aspect of a credit transaction. In the area of housing for example, we have gone after **companies for alleged redlining practices** (https://www.consumerfinance.gov/about-us/newsroom/remarks-of-director-rohit-chopra-at-a-joint-doj-cfpb-and-occ-press-conference-on-the-trustmark-national-bank-enforcement-action/), and outlined options to prevent **algorithmic bias** (https://www.consumerfinance.gov/about-us/newsroom/cfpb-outlines-options-to-prevent-algorithmic-bias-in-home-valuations/) in home valuations.

We know enforcement actions and supervisory examinations are not enough to create a fair and competitive market free from discrimination. Other steps we can take are efforts that build community wealth in historically underserved areas through supporting small businesses.

Through the beginning of 2022, we collected public comments on a proposed rule, under section 1071 of the CFPA, that would require lenders to collect and report certain data with respect to small business loan applicants and applications. This rule would help provide valuable information to the CFPB, other government agencies, lenders, and the public to identify areas of business and community development needs, and to facilitate enforcement of fair lending laws. We will be reviewing the comments that are provided to

inform a final rule that will fulfill the important small business and community development purposes of section 1071.

There is no one solution to ending both individual and systemic discrimination, so we will continue to use every tool at our disposal to ensure markets are free from discrimination and that every person can participate in financial markets on fair, competitive, and equal terms.

FURTHER READING

Blog

It's illegal to penalize borrowers for being religious (cfpb.gov/about-us/blog/its-illegal-penalize-borrowers-being-religious/)

JAN 14, 2022

Ang kahalagahan ng patas at pantay na pag-access sa kredito para sa mga minorya at negosyo na pag-aari ng kababaihan (cfpb.gov/about-us/blog/credit-access-minority-women-owned-businesses-tl/)

MAY 22, 2020

The importance of fair and equitable access to credit for minority and women-owned businesses (cfpb.gov/about-us/blog/fair-equitable-access-credit-minority-women-owned-businesses/)

APR 27, 2020

Newsroom

CFPB, DOJ Order Trident Mortgage Company to Pay More Than $22 Million for Deliberate Discrimination Against Minority Families (cfpb.gov/about-us/newsroom/cfpb-doj-order-trident-mortgage-company-to-pay-more-than-22-million-for-deliberate-discrimination-against-minority-families/)

JUL 27, 2022

Director Chopra's Prepared Remarks at a Joint DOJ, CFPB Press Event on the Trident Enforcement Action (cfpb.gov/about-us/newsroom/director-chopras-prepared-remarks-at-a-joint-dof-cfpb-press-event-on-the-trident-enforcement-action/)

JUL 27, 2022

CFPB Affirms Ability for States to Police Credit Reporting Markets (cfpb.gov/about-us/newsroom/cfpb-affirms-ability-for-states-to-police-credit-reporting-markets/)

JUN 28, 2022

Events

Building a bridge to credit visibility (cfpb.gov/about-us/events/archive-past-events/building-bridge-credit-visibility/)

SEP 17, 2018

View more (cfpb.gov/activity-log/?topics=discrimination&topics=fair-lending)

An official website of the United States government

Exhibit C

CFPB Supervision and Examination Process Overview

Background

Title X of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the Act)[1] established the Consumer Financial Protection Bureau (CFPB) and authorizes it to supervise certain consumer financial services companies and large depository institutions and their affiliates for consumer protection purposes.[2] The Bureau's purpose is set forth by Section 1021 of the Act:

> (a) **PURPOSE.—The Bureau shall seek to implement and, where applicable, enforce Federal consumer financial law consistently for the purpose of ensuring that all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive.**[3]

Federal consumer financial law

Subject to the provisions of the Act, the CFPB has responsibility to implement, examine for compliance with, and enforce "Federal consumer financial law."[4] Those laws include, among other things, Title X itself, which prohibits unfair, deceptive, or abusive acts and practices in connection with consumer financial products and services,[5] and the following "enumerated consumer laws"[6] and the implementing regulations.[7]

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[1] The Act can be found here: http://www.gpo.gov/fdsys/pkg/PLAW-111publ203/pdf/PLAW-111publ203.pdf.

[2] Sec. 1024 of the Act authorizes CFPB to supervise certain entities and individuals that engage in offering or providing a consumer financial product or service and their service providers that are not covered by Secs. 1025 or 1026 of the Act. Specifically, Sec. 1024 applies to those entities and individuals who offer or provide mortgage-related products or services and payday and private student loans as well as larger participants of other consumer financial service or product markets as defined by a CFPB rule, among others, plus their service providers. Sec. 1025 authorizes CFPB to supervise those entities that are large insured depository institutions and credit unions with more than $10 billion in total assets and all their affiliates (including subsidiaries), as well as service providers for such entities. Sec. 1026 provides the prudential regulators with consumer compliance examination authority for smaller depository institutions ($10 billion or less in total assets) not covered by Sec. 1025. The Bureau may, under Sec. 1026, include its examiners on a sampling basis at examinations of smaller insured depository institutions to assess compliance with the requirements of Federal consumer financial law. Under Sec. 1026, the Bureau has supervisory authority over a service provider to a substantial number of smaller depository institutions. "Insured depository institutions" include banks and savings associations. Under Sec. 1029, the Bureau may not exercise any authority over certain dealers predominantly engaged in the servicing and sale or leasing of motor vehicles. For ease of reference for purposes of this manual, entities and individuals within the scope of Sec. 1024 are referred to as "non-depository consumer financial service companies," and those within the scope of Sec. 1025 are referred to as "large depository institutions and their affiliates." The following are referred to as "supervised entities": (1) non-depository consumer financial service companies and their service providers; (2) large insured depository institutions, large insured credit unions, and their affiliates, as well as service providers to these entities; and (3) service providers to a substantial number of small insured depository institutions or small insured credit unions.

[3] Emphasis added. See also Sec. 1021(b)(4).

[4] *See* Sec. 1002(14) for the definition of "Federal consumer financial law."

[5] *See* Sec. 1036; *see also* 1031.

[6] *See* Sec. 1002(12). Parts of Title XIV of the Act are also designated as enumerated consumer laws. *See* Sec. 1400(b).

[7] *See* Sec. 1002(12).

- Alternative Mortgage Transaction Parity Act of 1982 (12 U.S.C. 3801 et seq.);
- Consumer Leasing Act of 1976 (15 U.S.C. 1667 et seq.);
- Electronic Fund Transfer Act (15 U.S.C. 1693 et seq.), except with respect to Section 920 of that Act;
- Equal Credit Opportunity Act (15 U.S.C. 1691et seq.);
- Fair Credit Billing Act (15 U.S.C. 1666 et seq.);
- Fair Credit Reporting Act (15 U.S.C. 1681et seq.), except with respect to Sections 615(e) and 628 of that Act (15 U.S.C. 1681m(e), 1681w);
- Home Owners Protection Act of 1998 (12 U.S.C. 4901 et seq.);
- Fair Debt Collection Practices Act (15 U.S.C. 1692 et seq.);
- Subsections (b) through (f) of Section 43 of the Federal Deposit Insurance Act (12 U.S.C. 1831t(b)–(f));
- Sections 502 through 509 of the Gramm-Leach-Bliley Act of 2009 [Privacy of Consumer Financial Information](15 U.S.C. 6802–6809) except for Section 505 as it applies to Section 501(b);
- Home Mortgage Disclosure Act of 1975 (12 U.S.C. 2801 et seq.);
- Home Ownership and Equity Protection Act of 1994 (15 U.S.C. 1601 note);
- Real Estate Settlement Procedures Act of 1974 (12 U.S.C. 2601 et seq.);
- S.A.F.E. Mortgage Licensing Act of 2008 (12 U.S.C. 5101 et seq.);
- Truth in Lending Act (15 U.S.C. 1601 et seq.);
- Truth in Savings Act (12 U.S.C. 4301 et seq.);
- Section 626 of the Omnibus Appropriations Act of 2009, Public Law 111–8; and
- Interstate Land Sales Full Disclosure Act (15 U.S.C. 1701).

In addition, the CFPB may enforce the following rules issued by the Federal Trade Commission:

- Telemarketing Sales Rule (16 CFR Part 310);[8]
- Use of Prenotification Negative Option Plans (16 CFR Part 425);
- Rule Concerning Cooling-Off Period for Sales Made at Homes or at Certain Other Locations (16 CFR Part 429);
- Preservation of Consumers' Claims and Defenses (16 CFR Part 433);
- Credit Practices (16 CFR Part 444);
- Mail or Telephone Order Merchandise (16 CFR Part 435);
- Disclosure Requirements and Prohibitions Concerning Franchising (16 CFR Part 436);
- Disclosure Requirements and Prohibitions Concerning Business Opportunities (16 CFR Part 437).

Supervision and examination

The statutory frameworks for supervision of large depository institutions and their affiliates and for non-depository consumer financial service companies are largely the same,[9] although the supervision authority for each is found in separate sections of the Act. The frameworks include:

- The purpose of supervision, including examination, to:
  - assess compliance with Federal consumer financial laws,
  - obtain information about activities and compliance systems or procedures, and
  - detect and assess risks to consumers and to markets for consumer financial products and services;
- The requirement to coordinate with other Federal and state regulators; and
- The requirement to use where possible publicly available information and existing reports to Federal or state regulators pertaining to supervised entities.

[8] The CFPB may enforce the Telemarketing and Consumer Fraud and Abuse Prevention Act.

[9] Most of the differences in the grants of supervision and examination authority will not be relevant for examiners in their daily work; supervised entities will be examined consistent with the applicable statutory provision.

Supervision and Examination Principles

Three main principles guide the CFPB supervision process.

Focus on consumers

The CFPB will focus on risks to consumers when it evaluates the policies and practices of a financial institution. We expect that institutions will offer consumer financial products and services in accordance with Federal consumer financial laws and will maintain effective systems and controls to manage their compliance responsibilities. As we conduct our reviews, we will focus on an institution's ability to detect, prevent, and correct practices that present a significant risk of violating the law and causing consumer harm.[10]

Data Driven

Like all CFPB activities, the supervision function rests firmly on analysis of available data about the activities of entities it supervises, the markets in which they operate, and risks to consumers posed by activities in these markets. Supervision staff (examiners and analysts) will use data from a wide range of sources: data obtained from the entity and through direct observation during monitoring and examination; information provided by the CFPB's Research, Markets and Regulations and Consumer Education and Engagement divisions, the Office of Fair Lending and Equal Opportunity, the Enforcement division, Consumer Response Center, and Offices addressing the special needs of students, Older Americans, Service members, and the underserved; and other state and Federal regulatory agencies.

Consistency

The CFPB will supervise both depository institutions that offer a wide variety of consumer financial products and services and non-depository consumer financial services companies that offer one or more such products. In order to fulfill its statutory mandate to consistently enforce Federal consumer financial law, the CFPB will apply consistent standards in its supervision of both types of entities, to the extent possible. To help accomplish this, the CFPB will use the same procedures to examine all supervised entities that offer the same types of consumer financial products or services, or conduct similar activities.

Such consistency, however, does not dictate uniformity in supervisory expectations. While all of the firms under our jurisdiction must follow the law, we understand that the means that they employ to achieve that goal will – and likely should – differ. We recognize that large, complex entities necessarily have different compliance oversight and management systems than smaller entities or those offering a more limited number of products or services.

[10] The discussion of the Risk Assessment under Pre-examination Planning in this Manual describes more fully what the CFPB means by risks or potential risks of consumer harm.

Examination Scheduling

Non-depository consumer financial services companies will be identified for examination on the basis of risks to consumers, including consideration of the company's asset size, volume of consumer financial transactions, extent of state oversight, and other factors determined relevant by CFPB. Examinations will be coordinated with State and prudential regulators as applicable.[11]

Regular examination schedules for large depository institutions and affiliates will depend on two considerations: (1) an assessment of risks to consumers and (2) ensuring consistency with statutory requirements that CFPB and prudential regulators coordinate the scheduling of examinations of large depository institutions and affiliates and conduct "simultaneous" examinations of depository institutions, as well as coordinating examinations with State regulators.[12]

Supervised entities will generally be notified in advance of an upcoming examination.

General Description of Examinations

Examiners will coordinate throughout the supervision and examination process with Supervision managers, and analysts, experts, and attorneys from Supervision, Research, Markets and Regulations, the Office of General Counsel, and other CFPB divisions at Headquarters. Supervision will work especially closely with the Office of Fair Lending and Equal Opportunity (OFLEO) and the Enforcement division when reviewing fair lending compliance and evaluating other potential violations of Federal consumer financial laws. In this Manual the coordination process will generally be referred to as "consulting internally." Alternatively, "Headquarters" will be used to signify the involvement of multiple divisions or offices in addition to Supervision.

Specific examination procedures will be similar to those of the prudential and, in some instances, State regulators.[13]As appropriate and in accordance with CFPB policy, examiners and Supervision managers will generally do the following in the course of an examination:

- Collect and review available information (from within the CFPB, from other Federal and state agencies, and from public sources), consistent with statutory requirements;
- Request and review supplementary documents and information from the entity to be examined;
- Develop and obtain internal approval for a preliminary risk focus and scope for the onsite portion of the examination;
- Go onsite to observe, conduct interviews, and review additional documents and information;

[11] *See* Sec. 1024(b)(3).

[12] *See* Sec. 1025(e).

[13] Prudential regulators refer to the Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, National Credit Union Association, and Office of the Comptroller of the Currency.

- Consult internally if the examination indicates potential unfair, deceptive, or abusive acts or practices; discrimination; or other violations of law;
- Draw preliminary conclusions about the regulated entity's compliance management and its statutory and regulatory compliance;
- Consult internally about follow-up corrective actions that the institution should take, whether through informal agreement or a formal enforcement action, if warranted by findings;
- Draft the examination report;
- Obtain appropriate internal review and approval for the examination work and draft examination report;
- Share the draft report with the prudential regulator and obtain and consider any comments they may offer, consistent with statutory requirements; and
- After final internal clearance, finalize and transmit the report to the supervised entity.

During the examination, the Examiner in Charge will communicate with appropriate supervised entity personnel about preliminary findings and conclusions. CFPB will seek cooperation from the entity to correct any problems identified.

The CFPB considers all supervisory information, including examination reports and ratings, highly confidential. Requirements for the handling of supervisory information not only by CFPB employees, but also by supervised institutions are described in its regulation on the *Disclosure of Records and Information*.[14]

Detailed examination procedures are located in Part II of this Manual.

Examination Follow-up

How the CFPB addresses negative examination findings will depend, among other things, on the individual facts and circumstances at issue. Whether informal supervisory measures or formal enforcement action is necessary will depend on the type of problem(s) found and the severity of harm to consumers. Self-correction will be encouraged, but some circumstances may nevertheless be sufficiently serious to warrant a public enforcement action. With respect to large depository institutions and their affiliates, CFPB will share draft examination reports and consult with prudential regulators regarding supervisory action, consistent with statutory requirements.[15]

[14] 12 CFR Part 1070 (76 FR 45372) (July 28, 2011)).

[15] *See* Sec.1025(e).

Target and Horizontal Reviews

In addition to regularly scheduled examinations, CFPB expects to conduct Target and Horizontal Reviews. Target Reviews will generally involve a single entity and will focus on a particular situation such as significant volume of particular customer complaints or a specific concern that has come to CFPB's attention. Horizontal Reviews will look across multiple entities to examine issues arising from particular products or practices and determine whether supervisory measures or enforcement actions are needed.

Enforcement Authority

CFPB is authorized to conduct investigations to determine whether any person is, or has, engaged in conduct that violates Federal consumer financial law.[16] Investigations may be conducted jointly with other regulators,[17] and may include subpoenas or civil investigative demands for testimony, responses to written questions, documents, or other materials.[18]

CFPB may bring administrative enforcement proceedings[19] or civil actions in Federal district court.[20] The Bureau can obtain "any appropriate legal or equitable relief with respect to a violation of Federal consumer financial law," including, but not limited to:

- Rescission or reformation of contracts.
- Refund of money or return of real property.
- Restitution.
- Disgorgement or compensation for unjust enrichment.
- Payment of damages or other monetary relief.
- Public notification regarding the violation.
- Limits on the activities or functions of the person against whom the action is brought.
- Civil monetary penalties (which can go either to victims or to financial education).

CFPB has no criminal enforcement authority.

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[16] Sec. 1051

[17] Sec. 1052(a)

[18] Sec. 1052(b) and (c)

[19] Sec. 1053

[20] Sec. 1054

Referral of Matters or Information to Other Agencies

Criminal Activity

In the course of their work, examiners may obtain evidence that a regulated entity or a customer has engaged in conduct that may constitute a violation of Federal criminal law. The CFPB is required by the Act[21] to refer such findings to the Department of Justice (DOJ) for further review and action. Examiners who, during the course of conducting their examination duties, believe they have found evidence of criminal conduct should consult internally to discuss their findings and the appropriate next steps. Headquarters will handle referral of appropriate matters to DOJ.

Some examples of fact scenarios that may necessitate a referral to the DOJ include, but are not limited to, the following:

- Based on documented information that the examiner has obtained, a regulated entity's financial records are comprised of data that appear to be false.
- A regulated entity's records or files show that it has direct business relationships with individuals or businesses based in a country that is the target of one or more types of United States government sanctions. (See sanctioned country lists at www.treasury.gov and www.state.gov.)
- A loan file or other type of file or record concerning a customer of a regulated entity contains one or more of the following documents that may indicate that the customer has engaged in potentially criminal conduct:
    - Bank statements that show that the customer has one or more bank accounts in a country that is a target of United States government sanctions. (*See* sanctioned country lists at www.treasury.gov and www.state.gov.)
    - Based on documented information in a loan file, (1) a loan application appears to contain false information, (2) an appraisal for real property appears to contain false information, or (3) a document used to verify loan eligibility appears to contain false information. (Documents used to verify loan eligibility include but are not limited to bank statements, Forms 1099, Forms W-2, and/or federal income tax returns.)

Tax Law Non-Compliance

The CFPB is also required under the Act to refer information identifying possible tax law non-compliance to the Internal Revenue Service (IRS).[22] Examiners who, during the course of conducting their examination duties, believe they have found evidence of tax law non-compliance should consult internally about the appropriate next steps. Headquarters will handle referral of matters to the IRS.

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[21] *See* Sec. 1056

[22] *See* Secs. 1024(b)(6) and 1025(b)(5).

Some examples of fact scenarios that may necessitate a referral to the IRS include, but are not limited to, the following:

- Based on documented information that the examiner has obtained, a regulated entity's tax returns are comprised of data that appear false.
- A loan file or other type of file or record concerning a customer of a regulated entity contains one or more of the following documents that may indicate that the customer has failed to comply with the tax laws:
  - Documents used to verify loan eligibility that clearly document that the customer has substantially greater income than the income that the customer reported on Federal income tax returns. Documents used to verify loan eligibility include statements showing a customer's investment portfolio, bank statements, and/or Forms 1099.

ECOA/pattern or practice

The Equal Credit Opportunity Act (ECOA) requires the CFPB to refer matters to DOJ whenever the CFPB "has reason to believe that one or more creditors has engaged in a pattern or practice of discouraging or denying applications for credit in violation of Section 1691(a)" of ECOA, which states ECOA's basic prohibitions against discrimination.[23] In matters that do not involve a pattern or practice of discouragement or denial, the CFPB may refer the matter to the DOJ whenever the agency has reason to believe that one or more creditors has violated Section 1691(a).[24] Headquarters will handle referral of appropriate matters to DOJ.

Matters not within the CFPB's authority

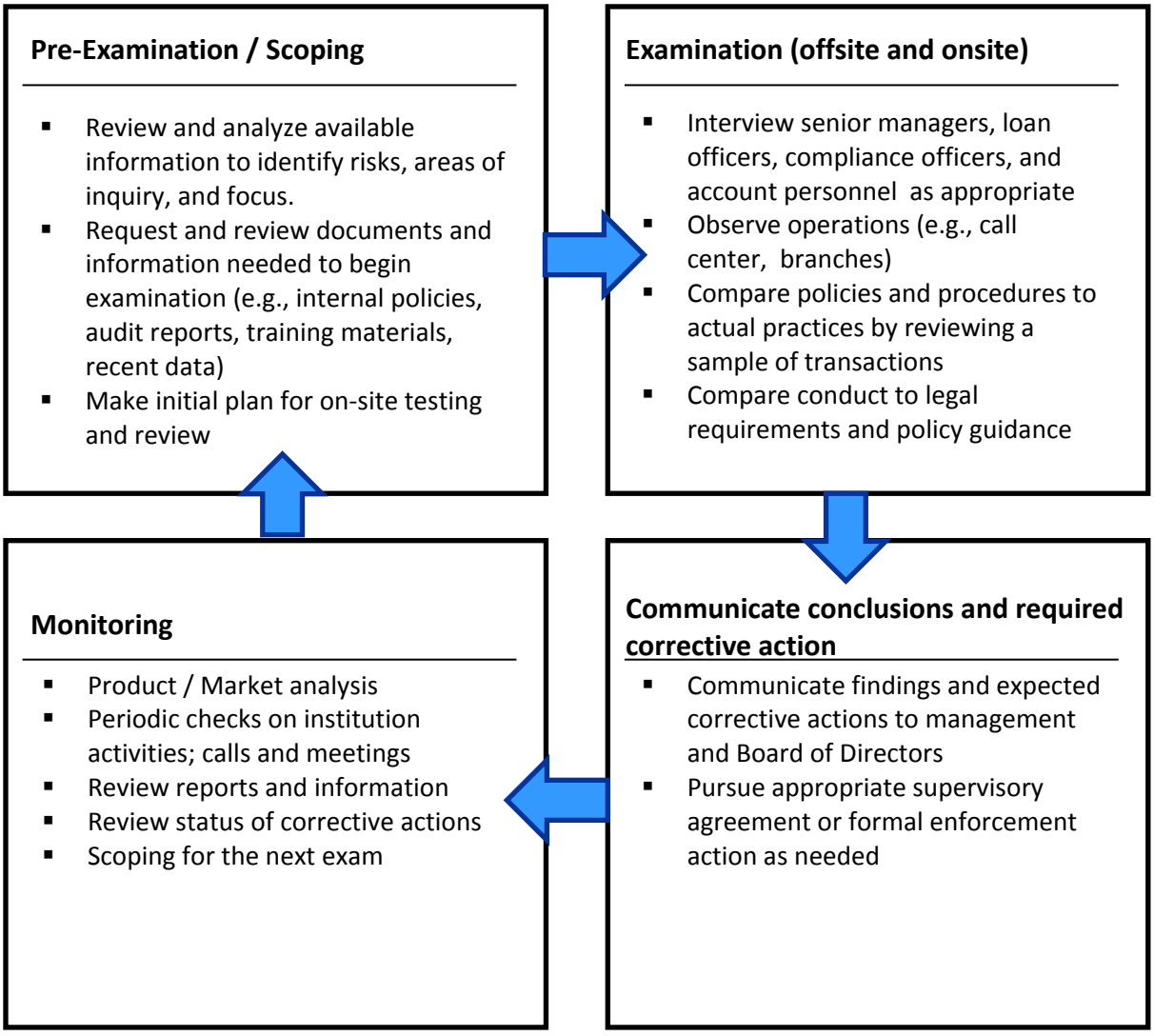
When examiners find information that may indicate violations of law that are not within the CFPB's authority, the information will be passed on to the appropriate prudential, other Federal, or state regulator. These situations will generally be handled by the Examiner in Charge, after consulting internally.

[23] 15 U.S.C. § 1691e(g).

[24] *Id.*

Supervision Examination Cycle

As shown in the graphic and described in this section, CFPB supervision operates as a continuous cycle.



Examination Prioritization: Given the large number, size, and complexity of entities falling under its supervisory authority, the CFPB uses a "prioritization" approach to examining. The CFPB's prioritization approach focuses on risks to consumers rather than risks to institutions. The prioritization approach focuses on individual product lines at an institution rather than on a comprehensive focus of all products and services offered by an institution. This approach allows the CFPB to assess the likely risk to consumers across the consumer financial marketplace in all product lines at all stages of a product's life cycle, including product development and implementation.

The prioritization process begins by analyzing an institution's products and services and breaking the institution down into its distinct product lines that are offered to consumers. For example, a large depository institution might have several product lines – auto lending, credit cards, deposit accounts, international money transfers, mortgage origination, and mortgage servicing – while a nonbank mortgage company might have just two – mortgage origination and servicing. We refer to each distinct product line at a regulated entity as an "Institution Product Line." These are the basic units of analysis for the CFPB's prioritization approach.

Once broken down into institution product lines, the product lines are compared across entities, charters, or licenses. This approach promotes an evaluation of each product line not by the provider's form of organization but by the product line activity within an organization. Each product line is evaluated on the potential consumer harm related to a particular market; the size of the product market; the regulated entity's market share; and risks inherent to the regulated entity's operations and offering of financial consumer products within that market.

The prioritization framework assesses risks to the consumer at two levels: the market level and the institution level. At the market-wide level, the CFPB assesses the risk to the consumer from the products and practices being offered in a particular market. In addition, the prioritization approach considers the relative product market size in the overall consumer finance marketplace.

At the institution level, the prioritization framework distinguishes that some institutions' business models within a market pose greater risks of harm to consumers than do others. Accordingly, prioritization efforts assess the relative risks to consumers from each institution's activity within any given market. This process takes into account a broad range of factors that bear upon the likelihood of consumer harm. The process starts with a regulated entity's market share within an individual product line, which corresponds to the number of consumers affected. Relatively large entities with a more dominant presence have a greater ability to impact more consumers, thus are prioritized over relatively small entities.

The prioritization approach augments this size consideration significantly with "field and market intelligence." Field and market intelligence includes both qualitative and quantitative factors for each institution product line, such as the strength of compliance management systems, findings from prior examinations, metrics gathered from public reports, and the number and severity of consumer complaints the CFPB receives. In addition, given the CFPB's mandate to ensure fair, equitable, and nondiscriminatory access to credit for all consumers, fair-lending-focused

information supplements general field and market intelligence in order to ensure that fair lending risks are identified and prioritized as well.

Taken together, the information about each institution product line, both at the market level and at the institutional level, allows the CFPB to focus on areas where consumers have the greatest potential to be harmed, specifically, on relatively higher risk institution product lines within relatively higher risk markets.

Central Point of Contact Duties: The CFPB may assign a staff member to perform central point of contact (CPC) duties at an institution to monitor the institution's on-going compliance efforts and to serve as the primary communication conduit between the company and the CFPB. CPC duties may be assigned to a field manager, an examiner or an analyst. CPC duties will vary from institution to institution based upon the company's risk profile and the examination schedule developed pursuant to the examination prioritization process described above.

Monitoring: The primary purpose of institution monitoring is to maintain current information about the institution's activities in order to determine whether changes in risks to consumers or markets warrant a change in the CFPB's prioritization strategy. Monitoring also allows the CFPB to assess institutional compliance with previously established corrective action and to evaluate on-going efforts by institution management to improve the company's compliance program. The frequency and scope of monitoring will vary depending on the organization's risk profile and will be established by CFPB management.

Examples of monitoring activities include:

- Reviewing supervisory and public information about the entity, such as:
  - Prudential and state regulator examination reports;
  - Community Reinvestment Act performance evaluations;
  - Current enforcement actions;
  - Call report data;
  - Complaint data;
  - Home Mortgage Disclosure Act data;
  - Home Affordable Modification Program Data;
  - SEC filings;
  - Licensing or registration information;
  - Reports from the entity to prudential or state regulators, if any;
  - CFPB research analyst reports;
  - Institution website; and
  - CFPB consumer complaints.

- Contacting the appropriate officer of the institution to discuss new products or services, events that may impact compliance management, and any questions raised by information reviewed by the CPC.
- Contacting the federal prudential regulator and relevant state regulators to discuss any recent events and any questions raised by supervisory or public information about the institution.
- Consulting internally.

Information developed through monitoring will be used to regularly assess the institution's risk profile and will be incorporated into the examination prioritization as described above.

Supervision Plan: A Supervision Plan is created and revised periodically for large depository institutions and certain nonbank institutions depending on the organization's risk profile. The Supervision Plan summarizes the plan for monitoring and examining the institution and its affiliates. It describes the priorities for CFPB supervision activities to assist in allocating and scheduling examiner resources. The Plan should be updated at least annually and may be updated at any time as a result of changes in the risk profile of the entity.

Exhibit D

- Content of the supervised entity's website

Before contacting the supervised entity to gather additional information, the EIC (or designee(s)) reviews the material gathered from these sources to help avoid duplicative requests. Of course, it may still be necessary to verify or update the information or documents with the supervised entity, but the burden of production will be reduced.

Develop a Scope Summary

Consistent with the Bureau's risk-based prioritization process, the EIC prepares the Scope Summary, which provides all members of the examination team with a central point of reference throughout the examination. The initial Scope Summary is based on internal consultation and a review of available information and documents gathered prior to sending the Information Request to the supervised entity.

The initial Scope Summary addresses the following:

- Key dates;
- Composition of the examination team;
- Contact information for the entity and any applicable prudential and state regulators;
- Communication plan;
- Activities to be undertaken to review:
  - The compliance management system (CMS);
  - Examination Procedures to be completed;
  - Areas selected for transaction testing, including estimated sampling sizes and methodology used to select the sample;
  - Areas where potential legal violations may exist, including those involving unfair, deceptive, or abusive acts or practices;
  - Fair lending compliance, if applicable.
  - Issues arising from complaints; and
  - Specific regulatory compliance issues.

At the conclusion of the examination, the EIC updates the initial Scope Summary with the following:

- Description of changes to the scope during the course of the review, and reasons for such changes; and

- Recommendations for the scope of subsequent reviews.

The initial Scope Summary, as well as any material changes to the scope during the review, should be approved in accordance with current Bureau requirements. The Scope Summary is maintained with the review records in the Supervision and Examination System.

The customizable Scope Summary template is available in the Supervision and Examination System.

Contact the Entity

For most reviews, the EIC, or designee, contacts the supervised entity's management no later than 60 days prior to the scheduled onsite date for the examination to arrange either a telephone or in-person discussion of the Information Request. The principal purpose of the discussion is to gather current information to ensure that the request is tailored to what is necessary to properly conduct the review of that particular institution.

The EIC or designee should also use the discussion to help determine whether certain information needed for the review should be sent to the examination team for review offsite or held for onsite review. The discussion should include the timing of production and the subsequent onsite review. The EIC should use the discussions to apprise management about who should be available to be interviewed during the onsite portion of the review. If not already known, the EIC should obtain information about the organization of the entity and where it maintains certain operations for the purpose of deciding which operation centers and/or branches the team will review.

Prepare and Send the Information Request

After conducting the review and discussion outlined above, the EIC or designee will use the monitoring information and any other relevant information to customize an Information Request that includes only items that are pertinent to the review of a particular entity. Not all items will be relevant to every review. In addition, the Information Request must specify the review period when it requests information or documentation such as periodic reports, ledgers, policies and procedures, and administrative changes, to avoid receiving data not relevant to the review.

The EIC or designee may provide the Information Request to entity management in either hard copy or electronic format, although electronic is preferred, indicating where the materials should be delivered and in what format. If at all possible, the requested materials should be delivered to the Bureau electronically. Examiners should consult with their field managers about what system should be used for secure requests and transmission of electronic examination files. The timing of the request and the response date must ensure that entity staff has sufficient time to assemble the requested information and the examination team has sufficient time to adequately review the materials.

Contacting the supervised entity at least 60 days prior to the onsite date, whenever feasible, and

sending the Information Request as soon as possible thereafter will generally ensure that staff of the supervised entity have sufficient time to properly gather and submit the response, and that the examination team has time to conduct its offsite review. To the extent possible and consistent with statutory requirements, examiners should coordinate the information request with the prudential and state regulator(s) and keep them abreast of monitoring efforts, correspondence with the supervised entity, and schedule planning.

The customizable Information Request templates are available in the Supervision and Examination System.

Conduct the Review

After receiving and reviewing the information and documents requested from the entity, the EIC will determine how to deploy the examination team to complete the examination procedures identified in the Scope Summary, conduct interviews, make observations, conduct transaction testing, and oversee other processes. Available examination procedures are part of this Supervision and Examination Manual. Templates should be downloaded from the Supervision and Examination System and used to create workpapers.

Upon determining the onsite start date, the EIC should arrange an entrance meeting with the appropriate member(s) of the supervised entity's management. At the meeting, the EIC can introduce the examination team, discuss generally the expected activities, clarify any questions about arrangements for being onsite at the entity (such as building security, work space, etc.), and set the tone for the examination.

Thereafter, the EIC should meet regularly with the entity point of contact to discuss interim findings and progress of the review. The EIC should also communicate regularly with his or her point of contact at the entity's prudential or state regulator(s). Throughout the examination, the EIC should follow current Bureau procedures for providing updates to regional and headquarters stakeholders

Close the Review

Closing Meeting

When all onsite activities and internal Bureau consultations are complete, the EIC should meet with the supervised entity's management to discuss the preliminary examination findings; expected Matters Requiring Attention or Supervisory Recommendations; recommended rating (if applicable); and next steps, if any. Management should be reminded that supervisory information, including ratings, is confidential and should not be shared except as allowed by Bureau regulation. Depending on the severity of the findings, other Bureau representatives may attend this meeting as well. Management should be alerted if a meeting with the board of directors or principals of the supervised entity will be required.

Entity management must be informed that examination findings, including compliance ratings, are

not final until internal Bureau reviews are conducted and, in the case of an insured depository institution or affiliate, the prudential regulator has had the opportunity to review and comment on the draft report.

Determine the Compliance Rating

When an Examination Report is issued, it will include a compliance rating that reflects the Bureau's assessment of the effectiveness of the institution's compliance management system to ensure compliance with consumer protection laws and regulations and reduce the risk of harm to consumers. The Bureau has adopted and uses the FFIEC Uniform Consumer Compliance Rating System (CC Rating System)[2] to determine compliance ratings. The system is based upon a numeric scale of "1" through "5" in increasing order of supervisory concern. Thus, "1" represents the highest rating and consequently the lowest degree of supervisory concern, while "5" represents the lowest rating and the most critically deficient level of performance, and therefore, the highest degree of supervisory concern. Ratings of "1" or "2" represent satisfactory or better performance. Ratings of "3," "4," or "5" indicate performance that is less than satisfactory.

- The highest rating of "1" is assigned to a financial institution that maintains a strong compliance management system (CMS) and takes action to prevent violations of law and consumer harm.
- A rating of "2" is assigned to a financial institution that maintains a CMS that is satisfactory at managing consumer compliance risk in the institution's products and services and at substantially limiting violations of law and consumer harm.
- A rating of "3" reflects a CMS deficient at managing consumer compliance risk in the institution's products and services and at limiting violations of law and consumer harm.
- A rating of "4" reflects a CMS seriously deficient at managing consumer compliance risk in the institution's products and services and/or at preventing violations of law and consumer harm. "Seriously deficient" indicates fundamental and persistent weaknesses in crucial CMS elements and severe inadequacies in core compliance areas necessary to operate within the scope of statutory and regulatory consumer protection requirements and to prevent consumer harm.
- A rating of "5" reflects a CMS critically deficient at managing consumer compliance risk in the institution's products and services and/or at preventing violations of law and consumer harm. "Critically deficient" indicates an absence of crucial CMS elements and a demonstrated lack of willingness or capability to take the appropriate steps

[2] This description of the rating system is adapted for Bureau purposes from the revised Uniform Interagency Consumer Compliance Rating System (CC Rating System) effective March 31, 2017. *See* ffiec.gov/press/pr110716.htm. The revisions update the original CC Rating System adopted by the FFIEC in 1980.

necessary to operate within the scope of statutory and regulatory consumer protection requirements and to prevent consumer harm.

CC Rating System Categories and Assessment Factors

CC Rating System – Categories

The CC Rating System is organized under three broad categories:

1. Board and Management Oversight,
2. Compliance Program, and
3. Violations of Law and Consumer Harm.

The Consumer Compliance Rating Definitions below list the assessment factors considered within each category, along with narrative descriptions of performance. The first two categories, Board and Management Oversight and Compliance Program, are used to assess a financial institution's CMS. As such, examiners should evaluate the assessment factors within these two categories commensurate with the institution's size, complexity, and risk profile. All institutions, regardless of size, should maintain an effective CMS. The sophistication and formality of the CMS typically will increase commensurate with the size, complexity, and risk profile of the entity.

Additionally, compliance expectations contained within the narrative descriptions of these two categories extend to third-party relationships[3] into which the financial institution has entered. There can be certain benefits to financial institutions engaging in relationships with third parties, including gaining operational efficiencies or an ability to deliver additional products and services, but such arrangements also may expose financial institutions to risks if not managed effectively.

As noted in the Consumer Compliance Rating Definitions, examiners should evaluate activities conducted through third-party relationships as though the activities were performed by the institution itself. Examiners should review a financial institution's management of third-party relationships and servicers as part of its overall compliance program.

The third category, Violations of Law and Consumer Harm, includes assessment factors that evaluate the dimensions of any identified violation or consumer harm. Examiners should weigh each of these four factors – root cause, severity, duration, and pervasiveness – in evaluating relevant violations of law and any resulting consumer harm.

[3]For the purposes of assessing compliance ratings, the FFIEC refers to these relationships as being with "third parties." Because the Bureau has adopted the FFIEC's CC Rating System, the Bureau is using that terminology in this section of the manual. However, the Bureau generally uses the term "service provider" in its supervisory documents. For more information, see Bureau Bulletin 2016-02.

Consumer Compliance Rating Definitions

Board and Management Oversight – Assessment Factors

Under Board and Management Oversight, the examiner should assess the financial institution's board of directors and management, as appropriate for their respective roles and responsibilities, based on the following assessment factors:

- Oversight of and commitment to the institution's CMS;
- Effectiveness of the institution's change management processes, including responding timely and satisfactorily to any variety of change, internal or external, to the institution;
- Comprehension, identification, and management of risks arising from the institution's products, services, or activities; and
- Self-identification of consumer compliance issues and corrective action undertaken as such issues are identified.

Compliance Program – Assessment Factors

Under Compliance Program, the examiner should assess other elements of an effective CMS, based on the following assessment factors:

- Whether the institution's policies and procedures are appropriate to the risk in the products, services, and activities of the institution;
- The degree to which compliance training is current and tailored to risk and staff responsibilities;
- The sufficiency of the monitoring and audit to encompass compliance risks throughout the institution; and
- The responsiveness and effectiveness of the consumer complaint resolution process.

Violations of Law and Consumer Harm – Assessment Factors

Under Violations of Law and Consumer Harm, the examiner should analyze the following assessment factors:

- The root cause, or causes, of any violations of law identified during the examination;
- The severity of any consumer harm resulting from violations;
- The duration of time over which the violations occurred; and
- The pervasiveness of the violations.

As a result of a violation of law, consumer harm may occur. While many instances of consumer harm can be quantified as a dollar amount associated with financial loss, such as charging higher fees for a product than was initially disclosed, consumer harm may also result from a denial of an opportunity. For example, a consumer could be harmed when a financial institution denies the consumer credit or discourages an application in violation of the Equal Credit Opportunity Act, whether or not there is resulting financial harm.

This next category of the Consumer Compliance Rating Definitions defines four factors by which examiners can assess violations of law and consumer harm.

1. **Root Cause.** The Root Cause assessment factor analyzes the degree to which weaknesses in the CMS gave rise to the violations. In many instances, the root cause of a violation is tied to a weakness in one or more elements of the CMS. Violations that result from critical deficiencies in the CMS evidence a critical absence of management oversight and are of the highest supervisory concern.

2. **Severity.** The Severity assessment factor of the Consumer Compliance Rating Definitions weighs the type of consumer harm, if any, that resulted from violations of law. More severe harm results in a higher level of supervisory concern under this factor. For example, some consumer protection violations may cause significant financial harm to a consumer, while other violations may cause negligible harm, based on the specific facts involved.

3. **Duration.** The Duration assessment factor considers the length of time over which the violations occurred. Violations that persist over an extended period of time will raise greater supervisory concerns than violations that occur for only a brief period of time. When violations are brought to the attention of an institution's management and management allows those violations to remain unaddressed, such violations are of the highest supervisory concern.

4. **Pervasiveness.** The Pervasiveness assessment factor evaluates the extent of the violation(s) and resulting consumer harm, if any. Violations that affect a large number of consumers will raise greater supervisory concern than violations that impact a limited number of consumers. If violations become so pervasive that they are considered to be widespread or present in multiple products or services, the institution's performance under this factor is of the highest supervisory concern.

Self-Identification of Violations of Law and Consumer Harm

Strong compliance programs are proactive. They promote consumer protection by preventing, self-identifying, and addressing compliance issues in a proactive manner. Accordingly, the CC Rating System provides incentives for such practices through the definitions associated with a 1 rating.

Self-identification and prompt correction of violations of law reflect strengths in an institution's

CMS. A robust CMS appropriate for the size, complexity and risk profile of an institution's business often will prevent violations or will facilitate early detection of potential violations.

This early detection can limit the size and scope of consumer harm. Moreover, self-identification and prompt correction of serious violations represents concrete evidence of an institution's commitment to responsibly address underlying risks. In addition, appropriate corrective action, including both correction of programmatic weaknesses and full redress for injured parties, limits consumer harm and prevents violations from recurring in the future. Thus, the CC Rating System recognizes institutions that consistently adopt these strategies as reflected in the Consumer Compliance Rating Definitions.

Evaluating Performance Using the Consumer Compliance Rating Definitions

The consumer compliance rating is derived through an evaluation of the financial institution's performance under each of the assessment factors described above. The consumer compliance rating reflects the effectiveness of an institution's CMS to identify and manage compliance risk in the institution's products and services and to prevent violations of law and consumer harm, as evidenced by the financial institution's performance under each of the assessment factors.

The consumer compliance rating reflects a comprehensive evaluation of the financial institution's performance under the CC Rating System by considering the categories and assessment factors in the context of the size, complexity, and risk profile of an institution. It is not based on a numeric average or any other quantitative calculation. Specific numeric ratings will not be assigned to any of the 12 assessment factors. Thus, an institution need not achieve a satisfactory assessment in all categories in order to be assigned an overall satisfactory rating.

Conversely, an institution may be assigned a less than satisfactory rating even if some of its assessments were satisfactory.

The relative importance of each category or assessment factor may differ based on the size, complexity, and risk profile of an individual institution. Accordingly, one or more category or assessment factor may be more or less relevant at one financial institution as compared to another institution. While the expectations for compliance with consumer protection laws and regulations are the same across institutions of varying sizes, the methods for accomplishing an effective CMS may differ across institutions.

The evaluation of an institution's performance within the Violations of Law and Consumer Harm category of the Consumer Compliance Rating Definitions considers each of the four assessment factors: Root Cause, Severity, Duration, and Pervasiveness. At the levels of "4" and "5" in this category, the distinctions in the definitions are focused on the root cause assessment factor rather than Severity, Duration, and Pervasiveness. This approach is consistent with the other categories where the difference between a "4" and a "5" is driven by the institution's capacity and willingness to maintain a sound consumer compliance system.

In arriving at the final rating, the examiner must balance potentially differing conclusions about the effectiveness of the financial institution's CMS over the individual products, services, and activities of the organization. Depending on the relative materiality of a product line to the institution, an observed weakness in the management of that product line may or may not impact the conclusion about the institution's overall performance in the associated assessment factor(s). For example, serious weaknesses in the policies and procedures or audit program of the mortgage department at a mortgage lender would be of greater supervisory concern than those same gaps at an institution that makes very few mortgage loans and strictly as an accommodation. Greater weight should apply to the financial institution's management of material products with significant potential consumer compliance risk.

An institution may receive a less than satisfactory rating even when no violations were identified, based on deficiencies or weaknesses identified in the institution's CMS. For example, examiners may identify weaknesses in elements of the CMS in a new loan product. Because the presence of those weaknesses left unaddressed could result in future violations of law and consumer harm, the CMS deficiencies could impact the overall consumer compliance rating, even if no violations were identified.

Similarly, an institution may receive a "1" or "2" rating even when violations were present, if the CMS is commensurate with the risk profile and complexity of the institution. For example, when violations involve limited impact on consumers, were self-identified, and resolved promptly, the evaluation may result in a "1" or "2" rating. After evaluating the institution's performance in the two CMS categories, Board and Management Oversight and Compliance Program, and the dimensions of the violations in the third category, the examiner may conclude that the overall strength of the CMS and the nature of observed violations viewed together do not present significant supervisory concerns.

Consumer Compliance Rating Definitions

ASSESSMENT FACTORS TO BE CONSIDERED	1	2	3	4	5
Board and Management Oversight Board and management oversight factors should be evaluated commensurate with the institution's size, complexity, and risk profile. Compliance expectations below extend to third-party relationships.					
Oversight and Commitment	Board and management demonstrate strong commitment and oversight to the financial institution's compliance management system. Substantial compliance resources are provided, including systems, capital, and human resources commensurate with the institution's size, complexity, and risk profile. Staff is knowledgeable, empowered and held accountable for compliance with consumer laws and regulations. Management conducts comprehensive and ongoing due diligence and oversight of third parties consistent with agency expectations to ensure that the financial institution complies with consumer protection laws, and exercises strong oversight of third parties' policies, procedures, internal controls, and training to ensure consistent oversight of compliance responsibilities.	Board and management provide satisfactory oversight of the financial institution's compliance management system. Compliance resources are adequate and staff is generally able to ensure the financial institution is in compliance with consumer laws and regulations. Management conducts adequate and ongoing due diligence and oversight of third parties to ensure that the financial institution complies with consumer protection laws, and adequately oversees third parties' policies, procedures, internal controls, and training to ensure appropriate oversight of compliance responsibilities.	Board and management oversight of the financial institution's compliance management system is deficient. Compliance resources and staff are inadequate to ensure the financial institution is in compliance with consumer laws and regulations. Management does not adequately conduct due diligence and oversight of third parties to ensure that the financial institution complies with consumer protection laws, nor does it adequately oversee third parties' policies, procedures, internal controls, and training to ensure appropriate oversight of compliance responsibilities.	Board and management oversight, resources, and attention to the compliance management system are seriously deficient. Compliance resources and staff are seriously deficient and are ineffective at ensuring the financial institution's compliance with consumer laws and regulations. Management oversight and due diligence over third-party performance, as well as management's ability to adequately identify, measure, monitor, or manage compliance risks, is seriously deficient.	Board and management oversight, resources, and attention to the compliance management system are critically deficient. Compliance resources are critically deficient in supporting the financial institution's compliance with consumer laws and regulations, and management and staff are unwilling or incapable of operating within the scope of consumer protection laws and regulations. Management oversight and due diligence of third-party performance is critically deficient.

ASSESSMENT FACTORS TO BE CONSIDERED	1	2	3	4	5
Change Management	Management anticipates and responds promptly to changes in applicable laws and regulations, market conditions and products and services offered by evaluating the change and implementing responses across impacted lines of business. Management conducts due diligence in advance of product changes, considers the entire life cycle of a product or service in implementing change, and reviews the change after implementation to determine that actions taken have achieved planned results.	Management responds timely and adequately to changes in applicable laws and regulations, market conditions, products and services offered by evaluating the change and implementing responses across impacted lines of business. Management evaluates product changes before and after implementing the change.	Management does not respond adequately and/or timely in adjusting to changes in applicable laws and regulations, market conditions, and products and services offered.	Management's response to changes in applicable laws and regulations, market conditions, or products and services offered is seriously deficient.	Management fails to monitor and respond to changes in applicable laws and regulations, market conditions, or products and services offered.
Comprehension, Identification and Management of Risk	Management has a solid comprehension of and effectively identifies compliance risks, including emerging risks, in the financial institution's products, services, and other activities. Management actively engages in managing those risks, including through comprehensive self-assessments.	Management comprehends and adequately identifies compliance risks, including emerging risks, in the financial institution's products, services, and other activities. Management adequately manages those risks, including through self-assessments.	Management has an inadequate comprehension of and ability to identify compliance risks, including emerging risks, in the financial institution's products, services, and other activities.	Management exhibits a seriously deficient comprehension of and ability to identify compliance risks, including emerging risks, in the financial institution.	Management does not comprehend nor identify compliance risks, including emerging risks, in the financial institution.
Corrective Action and Self-Identification	Management proactively identifies issues and promptly responds to compliance risk management deficiencies and any violations of laws or regulations, including remediation.	Management adequately responds to and corrects deficiencies and/or violations, including adequate remediation, in the normal course of business.	Management does not adequately respond to compliance deficiencies and violations including those related to remediation.	Management response to deficiencies, violations and examination findings is seriously deficient.	Management is incapable, unwilling and/or fails to respond to deficiencies, violations or examination findings.

ASSESSMENT FACTORS TO BE CONSIDERED	1	2	3	4	5
Compliance Program Compliance Program factors should be evaluated commensurate with the institution's size, complexity, and risk profile. Compliance expectations below extend to third-party relationships.					
Policies and Procedures	Compliance policies and procedures and third-party relationship management programs are strong, comprehensive and provide standards to effectively manage compliance risk in the products, services and activities of the financial institution.	Compliance policies and procedures and third-party relationship management programs are adequate to manage the compliance risk in the products, services and activities of the financial institution.	Compliance policies and procedures and third-party relationship management programs are inadequate at managing the compliance risk in the products, services and activities of the financial institution.	Compliance policies and procedures and third-party relationship management programs are seriously deficient at managing compliance risk in the products, services and activities of the financial institution.	Compliance policies and procedures and third-party relationship management programs are critically absent.
Training	Compliance training is comprehensive, timely, and specifically tailored to the particular responsibilities of the staff receiving it, including those responsible for product development, marketing and customer service. The compliance training program is updated proactively in advance of the introduction of new products or new consumer protection laws and regulations to ensure that all staff are aware of compliance responsibilities before rolled out.	Compliance training outlining staff responsibilities is adequate and provided timely to appropriate staff. The compliance training program is updated to encompass new products and to comply with changes to consumer protection laws and regulations.	Compliance training is not adequately comprehensive, timely, updated, or appropriately tailored to the particular responsibilities of the staff.	Compliance training is seriously deficient in its comprehensiveness, timeliness, or relevance to staff with compliance responsibilities, or has numerous major inaccuracies.	Compliance training is critically absent.

ASSESSMENT FACTORS TO BE CONSIDERED	1	2	3	4	5
Monitoring and/or Audit	Compliance monitoring practices, management information systems, reporting, compliance audit, and internal control systems are comprehensive, timely, and successful at identifying and measuring material compliance risk management throughout the financial institution. Programs are monitored proactively to identify procedural or training weaknesses to preclude regulatory violations. Program modifications are made expeditiously to minimize compliance risk.	Compliance monitoring practices, management information systems, reporting, compliance audit, and internal control systems adequately address compliance risks throughout the financial institution.	Compliance monitoring practices, management information systems, reporting, compliance audit, and internal control systems do not adequately address risks involving products, services or other activities including timing and scope.	Compliance monitoring practices, management information systems, reporting, compliance audit, and internal controls are seriously deficient in addressing risks involving products, services or other activities.	Compliance monitoring practices, management information systems, reporting, compliance audit, or internal controls are critically absent.
Consumer Complaint Response	Processes and procedures for addressing consumer complaints are strong. Consumer complaint investigations and responses are prompt and thorough. Management monitors consumer complaints to identify risks of potential consumer harm, program deficiencies, and customer service issues and takes appropriate action.	Processes and procedures for addressing consumer complaints are adequate. Consumer complaint investigations and responses are generally prompt and thorough. Management adequately monitors consumer complaints and responds to issues identified.	Processes and procedures for addressing consumer complaints are inadequate. Consumer complaint investigations and responses are not thorough or timely. Management does not adequately monitor consumer complaints.	Processes and procedures for addressing consumer complaints and consumer complaint investigations are seriously deficient. Management monitoring of consumer complaints is seriously deficient.	Processes and procedures for addressing consumer complaints are critically absent. Meaningful investigations and responses are absent. Management exhibits a disregard for complaints or preventing consumer harm.
Violations of Law and Consumer Harm					
Root Cause	The violations are the result of minor weaknesses, if any, in the compliance risk management system.	Violations are the result of modest weaknesses in the compliance risk management system.	Violations are the result of material weaknesses in the compliance risk management system.	Violations are the result of serious deficiencies in the compliance risk management system.	Violations are the result of critical deficiencies in the compliance risk management system.
Severity	The type of consumer harm, if any, resulting from the violations would have a minimal impact on consumers.	The type of consumer harm resulting from the violations would have a limited impact on consumers.	The type of consumer harm resulting from the violations would have a considerable impact on consumers.	The type of consumer harm resulting from the violations would have a serious impact on consumers.	

ASSESSMENT FACTORS TO BE CONSIDERED	1	2	3	4	5
Duration	The violations and resulting consumer harm, if any, occurred over a brief period of time.	The violations and resulting consumer harm, if any, occurred over a limited period of time.	The violations and resulting consumer harm, if any, occurred over an extended period of time.	The violations and resulting consumer harm, if any, have been long standing or repeated.	
Pervasiveness	The violations and resulting consumer harm, if any, are isolated in number.	The violations and resulting consumer harm, if any, are limited in number.	The violations and resulting consumer harm, if any, are numerous.	The violations and resulting consumer harm, if any, are widespread or in multiple products or services.	

Draft the Examination Report or Supervisory Letter

Examinations that result in the assignment of a consumer compliance rating will be communicated to the entity through an Examination Report. Targeted reviews that do not result in a rating will be communicated through a Supervisory Letter. Examination Report and Supervisory Letter templates are provided in Part III.

The primary purpose of these reports and letters is to communicate findings to the board of directors or principals and senior executives of a supervised entity. The narratives should be concise, constructive, and direct. In general, the commentaries for stable entities with low consumer or compliance risk should be brief, while the commentaries for those with elevated or increasing risk should successively provide more support and detail.

Comments should clearly cite statutory or regulatory violations and describe the basis for the findings. This will ensure that the supervised entity understands the basis for the conclusions and so that enforcement actions, if required, are well supported.

For each specific area reviewed, the narrative sections of the report have two parts:

1. **Conclusion:** The Conclusion contains an overall conclusion followed by a concise summary of findings. The conclusion should match the tone and language of the rating definition. This section should include summary details or facts supporting the conclusion, including a summary of material deficiencies. Avoid an overly detailed conclusion section. Include details supporting the conclusion in the Comments and Supporting Analysis section. Do not include cross-references within the Conclusion section.

2. **Comments and Supporting Analysis**: Comments discuss major strengths and/or weaknesses to support the conclusions. Supporting Analysis is information that demonstrates conclusions.

Examination reports and Supervisory Letters may include two types of communication to convey supervisory expectations related to violations of Federal consumer financial law, consumer harm, or compliance management weaknesses:

1. **Matters Requiring Attention (MRAs)**: MRAs are used by the Bureau to communicate to an institution's Board of Directors, senior management, or both, specific goals to be accomplished in order to correct violations of Federal consumer financial law, remediate harmed consumers, and address related weaknesses in the CMS that the examiners found are directly related to violations of Federal consumer financial law. MRAs include timeframes for periodic reporting of efforts taken to address these matters, as well as expected timeframes for implementation.

2. **Supervisory Recommendations (SRs)**: SRs are used by the Bureau to recommend actions for management to consider taking if it chooses to address the Bureau's supervisory concerns related to CMS. SRs are used when the Bureau has not identified a violation of Federal consumer financial law, but has observed weaknesses in CMS. SRs do not include provisions for periodic reporting or expected timelines for implementation. However, the Bureau will review through monitoring the steps institutions have taken to address SRs, including any information that institutions may provide regarding actions taken.

Neither MRAs nor SRs are legally enforceable. The Bureau will, however, consider an institution's response in addressing identified violations of Federal consumer financial law, weaknesses in CMS, or other noted concerns when assessing an institution's Compliance rating, or otherwise considering the risks that an institution poses to consumers and to markets. These risk considerations may be used by the Bureau when prioritizing future supervisory work or assessing the need for potential enforcement action.

Submit Examination Report or Supervisory Letter for Review

After the Examination Report or Supervisory Letter draft is complete, the Region will obtain any reviews required by internal Bureau policy.

If an Examination Report concerns an insured depository institution, the draft must be shared with the institution's prudential regulator.[4] The regulator must be given a reasonable opportunity to review and comment (not less than 30 days after the date of receipt of the report by the prudential regulator). The Bureau must take into consideration any concerns raised by the prudential regulator prior to issuing a final Examination Report or taking supervisory action. The interagency comment process will be managed by the Bureau's regional offices, with input from Bureau headquarters as appropriate. If a conflict arises between the Bureau and the prudential regulator regarding a proposed supervisory determination, regional and headquarters management will seek to resolve the issue as expeditiously as possible, with due regard for each agency's supervisory responsibilities. If the Bureau's review of an insured depository institution results in a Supervisory Letter, the final Supervisory Letter will be shared with the institution's

[4] Dodd-Frank Act, section 1025(e)(1)(C)

prudential regulator prior to issuance to the institution.

If the Examination Report concerns other types of regulated entities, opportunities for comment by state regulators will depend on whether Bureau is conducting joint or coordinated examinations with the relevant state regulators. The comment process will also be handled by the regional offices.

Board of Directors or Principal(s) Meeting

The purpose of a meeting with a supervised entity's board of directors or principal(s) is to convey the findings of a review directly to those individuals ultimately responsible for the policies and procedures of the institution. Board meetings should be conducted after the closing meeting with management, and should be attended by at least a quorum of directors or by the entity principal(s). The EIC and appropriate Bureau management should attend. The board or principals should be reminded that the Examination Report/Supervisory Letter and rating are confidential and should not be disclosed except as permitted by Bureau regulation.[5]

A board or principal(s) meeting is required when one or more of the following circumstances are present:

- The proposed compliance rating is "3," "4," or "5";
- A supervisory agreement or enforcement action is recommended; or
- The supervised entity's management, board, or principal(s) requests such a meeting.

The meeting should be used to discuss examination findings, supervisory actions, and expected corrective actions; advise the board or principal(s) of the recommended compliance rating; and discuss any recommended enforcement actions.

The timing of a board or principal(s) meeting will depend on the specific situation, and the EIC should work this out with his or her Field Manager, who will ensure the necessary internal coordination. Meetings should be coordinated with prudential and state examiners, and planned for regularly scheduled meetings whenever possible.

Send the Examination Report or Supervisory Letter

The EIC signs the final Examination Report or Supervisory Letter. Regional office administrative staff will handle transmission to the supervised entity.

Upload Final Examination Documents

At the conclusion of the examination, the EIC must finalize the Scope Summary, ensure all workpapers are complete, and be certain that all required documents and information are uploaded or entered into the Supervision and Examination System.

Workpapers

During a review, examiners collect and review information from the supervised entity to reach conclusions about its practices, its compliance management system, and its compliance with Federal consumer financial law. The records documenting the review are called workpapers.

Workpapers should contain sufficient information and supporting documents to explain to a knowledgeable reviewer the basis for the review's conclusions.

Purposes of Workpapers

Examiners develop and maintain workpapers for three principal purposes:

- To provide a record of the work performed during the review that supports findings and conclusions;
- To maintain the evidence necessary to support supervisory agreements or enforcement actions; and
- To facilitate internal quality control reviews.

All information collected and all records created during the review that are used to support findings and conclusions could potentially be included in the workpapers. For example, if an examiner interviews a Real Estate Lending Officer, the write-up of the interview notes becomes a workpaper if the information provided by the lending officer was used to support a particular finding or conclusion. If the examiner also scans pages of the supervised entity's RESPA procedures manual to help illustrate deviations from policy, the scanned pages should be included in the workpapers. Other examples of workpapers include, but are not limited to:

- Scope Summary document
- Completed Bureau Examination Procedures (downloadable templates that allow the examiner to enter narrative findings as they follow the procedures);
- Completed Bureau Checklists;
- Other documents created during the examination to record work, such as spreadsheets or completed job aids;
- Documentation of staff and management interviews;
- Meeting agendas, attendance lists, and notes or minutes;
- Documentation of compliance research performed, including consultations with Bureau stakeholders (e.g., legal opinions, regulation sections reviewed, regulatory alerts); and

- Scanned copies of material obtained from the supervised entity, such as policies, procedures, rate sheets, internal memos and reports, external audit reports, and complaint letters, that are necessary to support a finding or conclusion.

Generally, workpapers should document or support the:

- Proposed scope of the review and any changes to the scope during the course of the review;
- Work performed during the review (what you did);
- Sampling process and methodology used (how you did it);
- Findings and violations noted during the review (what you found);
- Matters Requiring Attention issued;
- Decision to address issues through supervisory or enforcement action;
- Communications with management regarding findings;
- Management's response (oral and written) to findings and violations;
- Commitments made by management regarding corrective action, remediation, and financial relief;
- Changes to the Risk Assessment;
- Consumer Compliance Rating; and
- Changes to the Supervision Plan (where applicable).

The amount of supporting documentation from the entity's records that is necessary to maintain in the workpapers will depend on the particular situation.

Review and Signoff

The EIC is responsible for the adequacy of the workpapers created during the review. Since large team examinations require the EIC to delegate numerous specific areas of review to other examiners, the EIC must track the:

- Workpapers developed;
- Responsible examination team member; and
- EIC's review and approval of the workpapers.

Workpapers that require additional analysis or support should be discussed with and returned to the responsible examiner for further development. The Workpaper Checklist, found in the Supervision and Examination System, must be used to record the EIC's review and sign off on all workpapers developed during the review.

After the EIC reviews and signs off on the workpapers, the Field Manager or Senior Examination Manager assigned to the review should also review and sign off on their adequacy.

Electronic Format and Encryption

All workpapers and related documentation for the review should be maintained in electronic form. If the supervised entity is only able to provide a document in hard copy form, the examiner should scan the document and return the original. Workpapers should be uploaded to the Supervision and Examination System with the completed examination to be preserved as part of the examination record and made available for future reference.

All electronic documents received from the supervised entity should be transmitted and maintained on encrypted media. Examiners should be mindful at all times of the need to protect personally identifiable information (e.g., names, social security numbers, account numbers) and confidential supervisory information. Hard copies should not be left anywhere unattended (even onsite at the entity), should not be removed from the examination site, and if printed while working offsite, should be kept in a locked cabinet when not being used.

Consult Bureau's Privacy and FOIA regulations and guidance for further information.[5]

Quality Control Reviews

Workpapers will also be reviewed through an internal quality control process to ensure they meet the Bureau's standards related to their documentation and proper storage.

[5] *See* Disclosure of Records and Information, 12 CFR Part 1070 (76 Fed. Reg. 45372 (July 28, 2011)), and any subsequent related guidance that may be issued.

Exhibit E

Unfair, Deceptive, or Abusive Acts or Practices

Unfair, deceptive, or abusive acts and practices (UDAAPs) can cause significant financial injury to consumers, erode consumer confidence, and undermine the financial marketplace. Under the Dodd-Frank Act, it is unlawful for any provider of consumer financial products or services or a service provider to engage in any unfair, deceptive or abusive act or practice.[1] The Act also provides CFPB with rule-making authority and, with respect to entities within its jurisdiction, enforcement authority to prevent unfair, deceptive, or abusive acts or practices in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service.[2] In addition, CFPB has supervisory authority for detecting and assessing risks to consumers and to markets for consumer financial products and services.[3]

As examiners review products or services, such as deposit products or lending activities, they generally should identify the risks of harm to consumers that are particular to those activities. Examiners also should review products that combine features and terms in a manner that can increase the difficulty of consumer understanding of the overall costs or risks of the product and the potential harm to the consumer associated with the product.

These examination procedures provide general guidance on:

- The principles of unfairness, deception, and abuse in the context of offering and providing consumer financial products and services;
- Assessing the risk that an institution's practices may be unfair, deceptive, or abusive;
- Identifying unfair, deceptive or abusive acts or practices (including by providing examples of potentially unfair or deceptive acts and practices); and
- Understanding the interplay between unfair, deceptive, or abusive acts or practices and other consumer protection statutes.

Unfair Acts or Practices

The standard for unfairness in the Dodd-Frank Act is that an act or practice is unfair when:

(1) It causes or is likely to cause substantial injury to consumers;

(2) The injury is not reasonably avoidable by consumers; and

[1] Dodd-Frank Act, Title X, Subtitle C, Sec. 1036; PL 111-203 (July 21, 2010).

[2] Sec. 1031 of the Dodd-Frank Act. The principles of "unfair" and "deceptive" practices in the Act are similar to those under Sec. 5 of the Federal Trade Commission Act (FTC Act). The Federal Trade Commission (FTC) and federal banking regulators have applied these standards through case law, official policy statements, guidance, examination procedures, and enforcement actions that may inform CFPB.

[3] Dodd-Frank Act, Secs. 1024; 1025(b)(1); 1026(b) of the Act.

(3) The injury is not outweighed by countervailing benefits to consumers or to competition.[4]

- ***The act or practice must cause or be likely to cause substantial injury to consumers.***
  Substantial injury usually involves monetary harm. Monetary harm includes, for example, costs or fees paid by consumers as a result of an unfair practice.[5] An act or practice that causes a small amount of harm to a large number of people may be deemed to cause substantial injury.

  Actual injury is not required in every case. A significant risk of concrete harm is also sufficient. However, trivial or merely speculative harms are typically insufficient for a finding of substantial injury. Emotional impact and other more subjective types of harm also will not ordinarily amount to substantial injury. Nevertheless, in certain circumstances, such as unreasonable debt collection harassment, emotional impacts may amount to or contribute to substantial injury.

- ***Consumers must not be reasonably able to avoid the injury.***
  An act or practice is not considered unfair if consumers may reasonably avoid injury. Consumers cannot reasonably avoid injury if the act or practice interferes with their ability to effectively make decisions or to take action to avoid injury. Normally the marketplace is self-correcting; it is governed by consumer choice and the ability of individual consumers to make their own private decisions without regulatory intervention. If material information about a product, such as pricing, is modified after, or withheld until after, the consumer has committed to purchasing the product; however, the consumer cannot reasonably avoid the injury. Moreover, consumers cannot avoid injury if they are coerced into purchasing unwanted products or services or if a transaction occurs without their knowledge or consent.

  A key question is <u>not</u> whether a consumer could have made a better choice. Rather, the question is whether an act or practice hinders a consumer's decision-making. For example, not having access to important information could prevent consumers from comparing available alternatives, choosing those that are most desirable to them, and avoiding those that are inadequate or unsatisfactory. In addition, if almost all market participants engage in a practice, a consumer's incentive to search elsewhere for better terms is reduced, and the practice may not be reasonably avoidable.[6]

  The actions that a consumer is expected to take to avoid injury must be reasonable. While a consumer might avoid harm by hiring independent experts to test products in advance or by bringing legal claims for damages in every case of harm, these actions generally

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[4] The standard for unfairness in the Dodd-Frank Act has the same three-part test as the FTC Act. This standard was first stated in the FTC Policy Statement on Unfairness (Dec. 17, 1980), *available at*: http://www ftc.gov/bcp/policystmt/ad-unfair htm. Congress later amended the FTC Act to include this specific standard in the Act itself. 15 U.S.C. § 45(n).

[5] FTC Policy Statement on Unfairness, at p. 3.

[6] *See* Credit Practices Rule, 49 Fed. Reg. 7740, 7746 (1984).

would be too expensive to be practical for individual consumers and, therefore, are not reasonable.

- ***The injury must not be outweighed by countervailing benefits to consumers or competition.***

  To be unfair, the act or practice must be injurious in its net effects — that is, the injury must not be outweighed by any offsetting consumer or competitive benefits that also are produced by the act or practice. Offsetting consumer or competitive benefits of an act or practice may include lower prices to the consumer or a wider availability of products and services resulting from competition.

  Costs that would be incurred for measures to prevent the injury also are taken into account in determining whether an act or practice is unfair. These costs may include the costs to the institution in taking preventive measures and the costs to society as a whole of any increased burden and similar matters.

Public policy, as established by statute, regulation, judicial decision, or agency determination, may be considered with all other evidence to determine whether an act or practice is unfair. However, public policy considerations by themselves may not serve as the primary basis for determining that an act or practice is unfair.

Examples

The examples described below stem from federal enforcement actions. They provide insight into practices that have been alleged to be unfair by other regulators and may inform CFPB's determinations. However, the particular facts in a case are crucial to a determination of unfairness. It is important to bear in mind that a change in facts could change the appropriate determination. Moreover, the brief summaries below do not present all of the material facts relevant to the determinations in each case. The examples show how the unfairness standard may be applied.

Refusing to release lien after consumer makes final payment on a mortgage.[7] The FTC brought an enforcement action against a mortgage company based on allegations, described below, that repeatedly failed to release liens after consumers fully paid the amount due on their mortgages.

- Substantial injury. Consumer's sustained economic injury when the mortgage servicer did not release the liens on their properties after the consumers had repaid the total amount due on the mortgages.

- Not outweighed by benefits. Countervailing benefits to competition or consumers did not result from the servicer's alleged failure to appropriately service the mortgage loan and release the lien promptly.

[7] *FTC v. Capital City Mortgage Corp*., Civil No. 98 CV-237 (D.D.C. Feb. 2005), *available at* http://www ftc.gov/opa/2005/02/capitalcity.shtm.

- Not reasonably avoidable. Consumers had no way to know in advance of obtaining the loan that the mortgage servicer would not release the lien after full payment. Moreover, consumers generally cannot avoid the harm caused by an improper practice of a mortgage servicer because the servicer is chosen by the owner of the loan, not the borrower. Thus, consumers cannot choose their loan servicer and cannot change loan servicers when they are dissatisfied with the quality of the loan servicing.

Dishonoring credit card convenience checks without notice.[8] The OTS and FDIC brought enforcement actions against a credit card issuer that sent convenience checks with stated credit limits and expiration dates to customers. For a significant percentage of consumers, the issuer reduced credit lines after the checks were presented, and then the issuer dishonored the consumers' checks.

- Substantial injury. Customers paid returned-check fees and may have experienced a negative impact on credit history.

- Not outweighed by benefits. The card issuer later reduced credit limits based on credit reviews. Based on the particular facts involved in the case, the harm to consumers from the dishonored convenience checks outweighed any benefit of using new credit reviews.

- Not reasonably avoidable. Consumers reasonably relied on their existing credit limits and expiration dates on the checks when deciding to use them for a payment. Consumers had received no notice that the checks they used were being dishonored until they learned from the payees. Thus, consumers could not reasonably have avoided the injury.

Processing payments for companies engaged in fraudulent activities.[9] The OCC brought an enforcement action in a case involving a bank that maintained deposit account relations with telemarketers and payment processors, based on the following allegations. The telemarketers regularly deposited large numbers of remotely created checks drawn against consumers' accounts. A large percentage of the checks were not authorized by consumers. The bank failed to establish appropriate policies and procedures to prevent, detect, or remedy such activities.

- Substantial injury. Consumers lost money from fraudulent checks created remotely and drawn against their accounts.

- Not outweighed by benefits. The cost to the bank of establishing a minimum level of due diligence, monitoring, and response procedures sufficient to remedy the problem would have been far less than the amount of injury to consumers that resulted from the bank's avoiding those costs.

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[8] *In re American Express Bank, FSB* (Cease and Desist Order WN-09-016, and Order of Assessment of a Civil Money Penalty for $250,000, WN-09-017, June 29, 2009) OTS Docket No. 15648; *In re American Express Centurion Bank*, (Cease and Desist Order, June 30, 2009) Docket FDIC-09-251b, available at http://www fdic.gov/news.

[9] *In re Wachovia Bank, National Association*, available at http://www.occ.treas.gov

- Not reasonably avoidable. Consumers could not avoid the harm because the harm resulted principally from transactions to which the consumers had not consented.

Deceptive Acts or Practices

A representation, omission, actor practice is deceptive when

(1) The representation, omission, act, or practice misleads or is likely to mislead the consumer;

(2) The consumer's interpretation of the representation, omission, act, or practice is reasonable under the circumstances; and

(3) The misleading representation, omission, act, or practice is material.[10]

- ***There must be a representation, omission, act, or practice that misleads or is likely to mislead the consumer.***

  Deception is not limited to situations in which a consumer has already been misled. Instead, an act or practice may be deceptive if it is *likely to mislead* consumers.

  It is necessary to evaluate an individual statement, representation, or omission not in isolation, but rather in the context of the entire advertisement, transaction, or course of dealing, to determine whether the overall net impression is misleading or deceptive. A representation may be an express or implied claim or promise, and it may be written or oral. If material information is necessary to prevent a consumer from being misled, it may be deceptive to omit that information.

  Written disclosures may be insufficient to correct a misleading statement or representation, particularly where the consumer is directed away from qualifying limitations in the text or is counseled that reading the disclosures is unnecessary. Likewise, oral or fine print disclosures or contract disclosures may be insufficient to cure a misleading headline or a prominent written representation. Similarly, a deceptive act or practice may not be cured by subsequent truthful disclosures.

  Acts or practices that may be deceptive include: making misleading cost or price claims; offering to provide a product or service that is not in fact available; using bait-and-switch techniques; omitting material limitations or conditions from an offer; or failing to provide the promised services.

  The FTC's "four Ps" test can assist in the evaluation of whether a representation, omission, act, or practice is likely to mislead:

  - Is the statement prominent enough for the consumer to notice?

[10] *See* FTC Policy Statement on Deception, available at http://www.ftc.gov/bcp/policystmt/ad-decept.htm. Examiners should be informed by the FTC's standard for deception.

- Is the information presented in an easy-to-understand format that does not contradict other information in the package and at a time when the consumer's attention is not distracted elsewhere?
- Is the placement of the information in a location where consumers can be expected to look or hear?
- Finally, is the information in close proximity to the claim it qualifies?[11]

- ***The representation, omission, act, or practice must be considered from the perspective of the reasonable consumer.***

  In determining whether an act or practice is misleading, one also must consider whether the consumer's interpretation of or reaction to the representation, omission, act, or practice is reasonable under the circumstances. In other words, whether an act or practice is deceptive depends on how a reasonable member of the target audience would interpret the representation. When representations or marketing practices target a specific audience, such as older Americans, young people, or financially distressed consumers, the communication must be reviewed from the point of view of a reasonable member of that group.

  Moreover, a representation may be deceptive if the majority of consumers in the target class do not share the consumer's interpretation, so long as a significant minority of such consumers is misled. When a seller's representation conveys more than one meaning to reasonable consumers, one of which is false, the seller is liable for the misleading interpretation.

  Exaggerated claims or "puffery," however, are not deceptive if the claims would not be taken seriously by a reasonable consumer.

- ***The representation, omission, or practice must be material.***

  A representation, omission, act, or practice is material if it is likely to affect a consumer's choice of, or conduct regarding, the product or service. Information that is important to consumers is material.

  Certain categories of information are presumed to be material. In general, information about the central characteristics of a product or service – such as costs, benefits, or restrictions on the use or availability – is presumed to be material. Express claims made with respect to a financial product or service are presumed material. Implied claims are presumed to be material when evidence shows that the institution intended to make the claim (even though intent to deceive is not necessary for deception to exist).

[11] FTC, *Dot Com Disclosures, Information about On-Line Advertising*, available at: http://business ftc.gov/documents/bus41-dot-com-disclosures-information-about-online-advertising.pdf.

> Claims made with knowledge that they are false are presumed to be material. Omissions will be presumed to be material when the financial institution knew or should have known that the consumer needed the omitted information to evaluate the product or service.

If a representation or claim is not presumed to be material, it still would be considered material if there is evidence that it is likely to be considered important by consumers.

Examples

The examples described below stem from federal enforcement actions. They provide insight into practices that have been alleged to be deceptive by other regulators and may inform CFPB's determinations. However, as with unfairness, the particular facts in a case are crucial to a determination of deception. It is important to bear in mind that a change in facts could change the appropriate determination. Moreover, the brief summaries below do not present all of the material facts relevant to the determinations in each case. The examples show how the deception standard may be applied.

Inadequate disclosure of material lease terms in television advertising.[12] The FTC brought actions against vehicle leasing companies alleging that their television advertisements represented that consumers could lease vehicles for "$0 down" when advertising a monthly lease payment. However, the FTC alleged that the "blur" of "unreadable fine print" that flashed on the screen at the end of the advertisement disclosed costs of at least $1,000. The settlements prohibited the vehicle leasing companies from misrepresenting the amount consumers must pay when signing the lease.

In addition, the FTC required that if the companies make any representation about the amounts due at lease signing, or that there is "no down payment," the companies must make an equally prominent (readable and audible) disclosure of the total amount of all fees due when consumers sign the lease.

- Representation or omission likely to mislead. The television advertisements featured prominent statements of "no money down" or "$0 down" at lease signing. The advertisement also contained, at the bottom of the screen, a "blur" of small print in which disclosures of various costs required by Regulation M (the Consumer Leasing Act) were made. The FTC alleged that the disclosures were inadequate because they were not clear, prominent, or audible to consumers.

- Reasonable consumer perspective. A reasonable consumer would believe that he did not have to put any money down and that all he owed was the regular monthly payment.

- Material representation. The stated "no money down" or "$0 down" plus the low monthly lease payment were material representations to consumers. The fact that the additional,

[12] *In the matters of Mazda Motor of America, Inc.; Mitsubishi Motor Sales of America, Inc.; American Honda Motor Company, Inc.; General Motors Corporation; American Isuzu Motors, Inc.*, available at http://www.ftc.gov/opa/1997/02/petapp09.shtm.

material costs were disclosed at signing of the lease did not cure the deceptive failure to disclose in the television advertising, the FTC claimed.

Misrepresentation about loan terms.[13] In 2004, the FTC sued a mortgage broker advertising mortgage refinance loans at "3.5% fixed payment 30-year loan" or "3.5% fixed payment for 30 years," implying that the offer was for a 30-year loan with a 3.5% fixed interest rate. Instead, the FTC claimed that the broker offered adjustable rate mortgages (ARMs) with an option to pay various amounts, including a minimum monthly payment that represented only a portion of the required interest. As a result, unpaid interest was added to the principal of the loan, resulting in negative amortization.[14]

- Practice likely to mislead. The FTC claimed that the advertisements were misleading because they compared payments on a mortgage that fully amortized to payments on a non-amortizing loan with payments that increased after the first year. In addition, the FTC claimed that after application, the broker provided Truth in Lending Act (TILA) disclosures that misstated the annual percentage rate (APR) and that failed to state that the loan was a variable rate loan.

- Reasonable consumer perspective. It was reasonable for consumers to believe that they would obtain fixed-rate mortgages, based on the representations.

- Material representation. The representations were material because consumers relied on them when making the decision to refinance their fully amortizing 30-year fixed loans. As a result, the consumers ended up with adjustable rate mortgages that would negatively amortize if they made payments at the stated 3.5% payment rate.

[13] FTC v. Chase Financial Funding, Inc., No. SACV04-549 (C.D.Cal. 2004), Stipulated Preliminary Injunction, available at http://www ftc.gov/os/caselist/0223287/0223287.shtm.

[14] In 2008, amendments to the Truth in Lending Act's Regulation Z were adopted to prohibit certain advertising practices, such as misleading advertising of fixed rates and payments, for credit secured by a dwelling. Similar practices could be identified as deceptive in other product lines. See 73 Fed. Reg. 44522 (July 30, 2008) (promulgating 12 CFR 226.24), which has since been recodified as 12 CFR 1026.24.

Abusive Acts or Practices

The Dodd-Frank Act makes it unlawful for any covered person or service provider to engage in an "abusive act or practice."[15] An abusive act or practice:

- Materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service or
- Takes unreasonable advantage of:
  - A lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service;
  - The inability of the consumer to protect its interests in selecting or using a consumer financial product or service; or
  - The reasonable reliance by the consumer on a covered person to act in the interests of the consumer.

Although abusive acts also may be unfair or deceptive, examiners should be aware that the legal standards for abusive, unfair, and deceptive each are separate.

The Role of Consumer Complaints in Identifying Unfair, Deceptive, or Abusive Acts or Practices

Consumer complaints play a key role in the detection of unfair, deceptive, or abusive practices. Consumer complaints have been an essential source of information for examinations, enforcement, and rule-making for regulators. As a general matter, consumer complaints can indicate weaknesses in elements of the institution's compliance management system, such as training, internal controls, or monitoring.

While the absence of complaints does not ensure that unfair, deceptive, or abusive practices are not occurring, complaints may be one indication of UDAAPs. For example, the presence of complaints alleging that consumers did not understand the terms of a product or service may be a red flag indicating that examiners should conduct a detailed review of the relevant practice. This is especially true when numerous consumers make similar complaints about the same product or service. Because the perspective of a reasonable consumer is one of the tests for evaluating whether a representation, omission, act, or practice is potentially deceptive, consumer complaints alleging misrepresentations or misunderstanding may provide a window into the perspective of the reasonable consumer.

When reviewing complaints against an institution, examiners should consider complaints lodged against subsidiaries, affiliates, and third parties regarding the products and services offered through the institution or using the institution's name. In particular, examiners should determine

[15] Dodd-Frank Act, Sec. 1036(a)(1)(B), 12 U.S.C. § 5536(a)(1)(B).

whether an institution itself receives, monitors, and responds to complaints filed against subsidiaries, affiliates, and third parties. Consumers can file complaints at a number of entities: the institution itself, the Better Business Bureau, State Attorneys General, the FTC's Consumer Sentinel, the CFPB Consumer Response Center, other Federal and State agencies, or on-line consumer complaint boards such as www.ripoffreport.com or www.complaints.com.

Analyzing Complaints

Analysis of consumer complaints may assist in the identification of potential unfair, deceptive, or abusive practices. Examiners should consider the context and reliability of complaints; every complaint does not indicate violation of law. When consumers repeatedly complain about an institution's product or service, however, examiners should flag the issue for possible further review. Moreover, even a single substantive complaint may raise serious concerns that would warrant further review. Complaints that allege, for example, misleading or false statements, or missing disclosure information, may indicate possible unfair, deceptive, or abusive acts or practices needing review.

Another area that could indicate potential unfair, deceptive, or abusive acts or practices is a high volume of charge-backs or refunds for a product or service. While this information is relevant to the consumer complaint analysis, it may not appear in the institution's complaint records.

Relationship to Other Laws

An unfair, deceptive, or abusive act or practice may also violate other federal or state laws. For example, pursuant to the TILA, creditors must "clearly and conspicuously" disclose the costs and terms of credit. An act or practice that does not comply with these provisions of TILA may also be unfair, deceptive, or abusive.

Conversely, a transaction that is in technical compliance with other federal or state laws may nevertheless violate the prohibition against UDAAPs. For example, an advertisement may comply with TILA's requirements, but contain additional statements that are untrue or misleading, and compliance with TILA's disclosure requirements does not insulate the rest of the advertisement from the possibility of being deceptive.

Unfair, Deceptive, or Abuse Acts and Practices

Exam Date:	[Click&type]
Prepared By:	[Click&type]
Reviewer:	[Click&type]
Docket #:	[Click&type]
Entity Name:	[Click&type]

Examination Objectives

- To assess the quality of the regulated entity's compliance risk management systems, including internal controls and policies and procedures, for avoiding unfair, deceptive, or abusive acts or practices (UDAAP).
- To identify acts or practices that materially increase the risk of consumers being treated in an unfair, deceptive, or abusive manner.
- To gather facts that help determine whether a regulated entity engages in acts or practices when offering or providing consumer financial products or services that are likely to be unfair, deceptive, or abusive.
- To determine, in consultation with Headquarters, whether an unfair, deceptive or abusive act or practice has occurred and whether further supervisory or enforcement actions are appropriate.

General Guidance

Based on the results of the risk assessment of the entity, examiners should review for potential unfair, deceptive, or abusive acts or practices, taking into account an entity's marketing programs, product and service mix, customer base, and other factors, as appropriate. Even if the risk assessment has not identified potential unfair, deceptive, or abusive acts or practices, examiners should be alert throughout an examination for situations that warrant review.

1. **Document Review**
   a. To initially identify potential areas of UDAAP concerns, obtain and review copies of the following to the extent relevant to the examination:

   b. Training materials.

   c. Lists of products and services, including descriptions, fee structure, disclosures, notices, agreements, and periodic and account statements.

   d. Procedure manuals and written policies, including those for servicing and collections.

   e. Minutes of the meetings of the Board of Directors and of management committees, including those related to compliance.

   f. Internal control monitoring and auditing materials.

   g. Compensation arrangements, including incentive programs for employees and third parties.

h. Documentation related to new product development, including relevant meeting minutes of Board of Directors, and of compliance and new product committees.

i. Marketing programs, advertisements, and other promotional material in all forms of media (including print, radio, television, telephone, Internet, or social media advertising).

j. Scripts and recorded calls for telemarketing and collections.

k. Organizational charts, including those related to affiliate relationships and work processes.

l. Agreements with affiliates and third parties that interact with consumers on behalf of the entity.

m. Consumer complaint files.

n. Documentation related to software development and testing, as applicable.

Management and Policy-Related Examination Procedures

1. Identify potential UDAAP concerns by reviewing all relevant written policies and procedures, customer complaints received by the entity or by the CFPB, internal and external audit reports, statistical and management reports, and examination reports. Determine whether:

a. The scope of the entity's compliance audit includes a review of potential unfair, deceptive, or abusive acts or practices.

b. The compliance audit work is performed consistent with the audit plan and scope.

c. The frequency and depth of audit review is appropriate to the nature of the activities and size of the entity.

d. Management and the Board of Directors are made aware of and review significant deficiencies and their causes.

e. Management has taken corrective actions to followup on any identified deficiencies.

f. The entity's compliance programs ensure that policies are being followed through its sampling of relevant product types and decision centers, including sales, processing, and underwriting.

g. The entity has a process to respond to consumer complaints in a timely manner and determine whether consumer complaints raise potential UDAAP concerns.

h. The entity has been subject to any enforcement actions or has been investigated by a regulatory or law enforcement agency for violations of consumer protection laws or regulations that may indicate potential UDAAP concerns.

[Click&type]

2. Through discussions with management and a review of available information, determine whether the entity's internal controls are adequate to prevent unfair, deceptive or abusive acts or practices. Consider whether:

a. The compliance management program includes measures aimed at avoiding unfair, deceptive, or abusive practices, including:

- Organization charts and process flowcharts;
- Policies and procedures; and
- Monitoring and audit procedures.

b. The entity conducts prior UDAAP reviews of advertising and promotional materials, including promotional materials and marketing scripts for new products.

c. The entity evaluates initial and subsequent disclosures, including customer agreements and changes in terms, for potential UDAAP concerns.

d. The entity reviews new products and changes in the terms and conditions of existing products for potential UDAAP concerns.

e. The entity has a thorough process for receiving and responding to consumer complaints and has a process to receive complaints made to third parties, such as the Better Business Bureau or the CFPB.

f. The entity evaluates servicing and collections for UDAAP concerns.

g. The entity has established policies and controls relating to employee and third-party conduct, including:

- Initial and ongoing training;
- Performance reviews or audits;
- Discipline policies and records of disciplinary actions;
- Third-party agreements and contractual performance standards;
- Compensation programs; and
- Monitoring.

h. The entity's internal control processes are documented.

i. Computer programs are tested and documented to ensure accurate and timely disclosures to consumers.

[Click&type]

3. Potential Areas for Transaction Testing

Through a high-level assessment of the entity's products, services, and customer base, identify areas for potential transaction testing. This process should determine whether:

a. The entity does not underwrite a given credit product on the basis of ability to repay.

b. A product's profitability depends significantly on penalty fees or "back-end" rather than upfront fees.

c. A product has high rates of repricing or other changes in terms.

d. A product combines features and terms in a manner that can increase the difficulty of consumer understanding of the overall costs or risks of the product and the potential harm.

e. Penalties are imposed on a customer when he terminates his relationship with the entity.

f. Fees or other costs are imposed on a consumer to obtain information about his account.

g. A product is targeted to particular populations, without appropriate tailoring of marketing, disclosures, and other materials designed to ensure understanding by the consumers.

[Click&type]

Transaction-Related Examination Procedures

If upon conclusion of the management and policy-related examination procedures, procedural weaknesses, or other UDAAP risks require further investigation, conduct transaction testing, as necessary, using the following examination procedures. Use judgment in deciding to what extent to sample individual products, services, or marketing programs. Increase the sample size to achieve confidence that all aspects of the entity's products and services are reviewed sufficiently. Consult with Headquarters to obtain assistance with the sampling process.

1. Marketing and Disclosures

Through a review of marketing materials, customer agreements, and other disclosures, determine whether, before the consumer chooses to obtain the product or service:

a. All representations are factually based.

b. All materials describe clearly, prominently, and accurately:

- costs, benefits, and other material terms of the products or services being offered;
- related products or services being offered either as an option or required to obtained certain terms; and
- material limitations or conditions on the terms or availability of products and services, such as time limitations for favorable rates, promotional features, expiration dates, prerequisites for obtaining particular products or services, or conditions for canceling services.

c. The customer's attention is drawn to key terms, including limitations and conditions, that are important to enable the consumer to make an informed decision.

d. All materials clearly and prominently disclose the fees, penalties, and other charges that may be imposed and the reason for the imposition.

e. Contracts clearly inform customers of contract provisions that permit changes in terms and conditions of the product or service.

f. All materials clearly communicate the costs, benefits, availability, and other terms in language that can be understood when products are targeted to particular populations, such as reverse mortgage loans for the elderly.

g. Materials do not misrepresent costs, conditions, limitations, or other terms either affirmatively or by omission.

h. The entity avoids advertising terms that are generally not available to the typical targeted consumer.

[Click&type]

2. Availability of Terms or Services as Advertised

Evaluate whether product(s) and service(s) that consumers are receiving are consistent with the disclosures and policies. For each product and service being reviewed, select a sample that:

a. Is sufficient in size to reach a supportable conclusion about such consistency;

b. Includes, as appropriate, transactions from different origination and underwriting channels — for example, different geographical areas or different sectors of the entity's organization structure; and

c. Includes approved and/or denied accounts.

Determine whether:

a. Consumers are reasonably able to obtain the products and services, including interest rates or rewards, as represented by the entity.

b. Consumers receive the specific product or service that they request.

c. Counter-offers clearly, prominently, and accurately explain the difference between the original product or services requested and the one being offered.

d. Actual practices are consistent with stated policies, procedures, or account disclosures.

[Click&type]

3. Availability of Actual Credit to the Consumer

Evaluate whether the entity represents the amount of useable credit that the consumer will receive in a truthful way. Consider whether:

a. The available credit is sufficient to allow the consumer to use the product as advertised and disclosed to the consumer.

b. The fees and charges, typically imposed on the average targeted customer, both initially and throughout the term of the loan, remain in a range that does not prevent the availability of credit.

c. The entity honors convenience checks when used by the customer in a manner consistent with introductory or promotional materials and disclosures.

[Click&type]

4. Employees and Third Parties Interacting with Consumers

Evaluate how the entity monitors the activities of employees and third-party contractors, marketing sales personnel, vendors, and service providers to ensure they do not engage in unfair, deceptive, or abusive acts or practices with respect to consumer interactions. Interview employees and third parties, as appropriate. Specifically, consider whether:

a. The entity ensures that employees and third parties who market or promote products or services are adequately trained so that they do not engage in unfair, deceptive, or abusive acts or practices.

b. The entity conducts periodic evaluations or audits to check whether employees or third parties follow the entity's training and procedures and has a disciplinary policy in place to deal withany deficiencies.

c. The entity reviews compensation arrangements for employees, third-party contractors, and service providers to ensure that they do not create unintended incentives to engage in unfair, deceptive, or abusive acts or practices, particularly with respect to product sales, loan originations, and collections.

d. Performance evaluation criteria do not create unintended incentives to engage in unfair, deceptive, or abusive acts or practices, including criteria for sales personnel based on sales volume, size, terms of sale, or account performance.

e. The entity implements and maintains effective risk and supervisory controls to select and manage third-party contractors and service providers.

[Click&type]

5. Servicing and Collections

Evaluate whether servicing and collections practices raise potential UDAAP concerns, by considering whether**:**

a. The entity has policies detailing servicing and collections practices and has monitoring systems to prevent unfair, deceptive or abusive acts or practices.

b. Call centers, either operated by the entity itself or by third parties, effectively respond to consumers' calls.

c. The entity ensures that employees and third party contractors:

- represent fees or charges on periodic statements in a manner that is not misleading;
- post and credit consumer payments in a timely manner;
- apply payments in a manner that does not unnecessarily increase customer payments, without clear justification;
- only charge customers for products and services, such as insurance or credit protection programs, that are specifically agreed to;
- mail periodic statements in time to provide the consumer ample opportunity to avoid late payments; and
- do not represent to consumers that they may pay less than the minimum amount without clearly and prominently disclosing any fees for paying the reduced amount.

d. The entity has policies to ensure compliance with the standards under the Fair Debt Collections Practices Act to prevent abusive, deceptive, or unfair debt collection practices.

e. Employees and third party contractors clearly indicate to consumers that they are calling about the collection of a debt.

f. Employees and third party contractors do not disclose the existence of a consumer's debt to the public without the consent of the consumer, except as permitted by law.

g. The entity avoids repeated telephone calls to consumers that annoy, abuse, or harass any person at the number called.

[Click&type]

6. Interviews with Consumers

If potential UDAAP issues are identified that would necessitate interviews with consumers, consult with regional management who will confer with Headquarters.

[Click&type]

Examiner's Summary, Recommendations, and Comments

[Click&type]

Exhibit F

Consumer Financial Protection Bureau (cfpb.gov/)

CFPB Targets Unfair Discrimination in Consumer Finance

Discrimination or improper exclusion can trigger liability under ban on unfair acts and practices

MAR 16, 2022

WASHINGTON, D.C. – Today the Consumer Financial Protection Bureau (CFPB) announced changes to its supervisory operations to better protect families and communities from illegal discrimination, including in situations where fair lending laws may not apply. In the course of examining banks' and other companies' compliance with consumer protection rules, the CFPB will scrutinize discriminatory conduct that violates the federal prohibition against unfair practices. The CFPB will closely examine financial institutions' decision-making in advertising, pricing, and other areas to ensure that companies are appropriately testing for and eliminating illegal discrimination.

"When a person is denied access to a bank account because of their religion or race, this is unambiguously unfair," said CFPB Director Rohit Chopra. "We will be expanding our anti-discrimination efforts to combat discriminatory practices across the board in consumer finance."

The CFPB enforces several laws that can target discriminatory practices. Government regulators and private plaintiffs have commonly relied on the Equal Credit Opportunity Act (ECOA), a fair lending law which covers extensions of credit. However, certain discriminatory practices may also trigger liability under the Consumer Financial Protection Act (CFPA), which prohibits unfair, deceptive and abusive acts and practices (UDAAPs).

The CFPB published an updated exam manual today for evaluating UDAAPs, which notes that discrimination may meet the criteria for "unfairness" by causing substantial harm to consumers that they cannot reasonably avoid, where that harm is not outweighed by countervailing benefits to consumers or competition. Consumers can be harmed by discrimination regardless of whether it is intentional. Discrimination can be unfair in cases where the conduct may also be covered by ECOA, as well as in instances where ECOA does not apply. For example, denying access to a checking account because the individual is of a particular race could be an unfair practice even in those instances where ECOA may not apply.

The CFPB will examine for discrimination in all consumer finance markets, including credit, servicing, collections, consumer reporting, payments, remittances, and deposits. CFPB examiners will require supervised companies to show their processes for assessing risks and discriminatory outcomes, including documentation of customer demographics and the impact of products and fees on different demographic groups. The CFPB will look at how companies test and monitor their decision-making processes for unfair discrimination, as well as discrimination under ECOA.

Read the updated exam manual on Unfair, Deceptive or Abusive Acts or Practices (https://files.consumerfinance.gov/f/documents/cfpb_unfair-deceptive-abusive-acts-practices-udaaps_procedures.pdf)

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Exhibit G

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From Crypto To Apps, CFPB's Chopra Has Payments In Focus

By **Jon Hill**

Law360 (July 27, 2022, 12:02 AM EDT) -- Consumer Financial Protection Bureau Director Rohit Chopra is pushing forward on a busy agenda that includes keeping tabs on the downstream consumer impacts of higher interest rates, preparing for the age of real-time payments and taking a tough line with so-called repeat offender companies. "Stay tuned," he told Law360.

Rohit Chopra

In a wide-ranging interview, Chopra discussed how the CFPB could seek to help mortgage borrowers strained by the Federal Reserve's battle against inflation and how the agency is looking at cryptocurrency, which the rest of Washington, D.C., is scrambling to regulate.

Chopra cast crypto as part of a wave of innovations that are making faster payments a reality for many consumers. But these innovations, which include mobile payment apps and other technologies, raise new consumer protection questions that Chopra said the CFPB is studying, like whether additional fraud-related guidance is needed amid a bevy of complaints from peer-to-peer payments users.

Chopra also downplayed prospects for new rulemaking on payday loans, defended recent examination policy changes aimed at extending the CFPB's anti-discrimination scrutiny to consumer financial markets not covered by traditional fair lending laws, and highlighted efforts to strengthen enforcement for companies that repeatedly break the law.

This interview has been edited for length and clarity.

Let's start with the macro perspective. We're on the verge of the Fed's fourth interest rate hike in five months, and more are expected. Consumers haven't seen a tightening cycle like this in decades. So where do you see potential pitfalls for them? And how is the bureau responding to those?

In terms of the rate environment, we're looking at how it is affecting each of the big consumer verticals. In order, that would be mortgages, student loans, auto [loans] and then credit cards.

For student [loans], because of the federal piece of it, it's a little bit de-linked from the overall rate environment.

Mortgages, we obviously are seeing quite a bit of a tick-up, although it's relaxed recently. A key place that we're thinking through there is the extent to which the macro-environment changes and there is depreciation, or a reduction of the amount of home equity in the system, that could spell some challenges in terms of mortgage servicing.

Also, with those elevated rates for people who are getting mortgages now, I am interested in figuring out ways we could do any targeted changes to the [qualified mortgage] rule so that we can have more streamlined refinances or streamlined loan modifications to benefit people when rates go down or to benefit people who need loan modifications.

Auto is big. I think with the issues in the global automotive supply chain — we continue to see forecasts of where inventories are going to be, and I think we're expecting for new and used car [prices] to remain elevated above historical levels for the next year or so — we project that the $1.4 trillion auto loan market is going to get a little bigger as loan sizes increase.

We're really watching in terms of credit tiers, on how performance is moving. I personally think some of the accelerations in delinquency that you see in auto and credit card debt may be a bit more of a story about normalization. However, I don't know if that's going to sustain. It really depends on the labor market, and it depends on really what's going to happen with inflation overall.

On credit card debt, we are seeing that people are noticing some higher rates, and the same is true with auto and mortgage debt. I think that increases the stakes on how do we make sure there's good competition and refinancing later, not just when rates go down, but also when people's income increases or their credit score is increasing. Are they able to take advantage of that?

And then of course there's deposit accounts. You're seeing a lot of banks actually try and shrink the amount of assets that they have on their balance sheets. We see that cash deposits still tend to be a little higher than they were in 2019, though it has come down a little bit. We'll see how that plays through in terms of credit performance on consumer financial instruments, but that's how I see the macro picture. It's going to be very dependent on where the labor market is.

The Fed's tightening is credited with contributing to recent turmoil in the crypto market, where a lot of consumers have been burned by falling coin prices and freezes on withdrawals. There's a debate about who should regulate these assets, but how closely is the bureau monitoring this turbulence? Are you seeing any worrying practices from a consumer protection standpoint?

I would say our primary focus is really on the effect of real-time consumer payments, which need not use blockchain-based technologies. We know FedNow [a real-time payment network **being built by the Fed**] is turning on next year, there's broad adoption of apps and other ways to transfer money in real time. There's a lot of attendant consumer protection issues that every developed country experiences when those technologies gain broader adoption.

But right now, cryptocurrency, including stablecoins, are not primarily used in consumer payments. They're really used for speculative trading purposes.

We're obviously monitoring it along with the other regulators. There are a couple of things that come to mind.

One, we have published some guidance about misrepresentations about deposit insurance, and the [Federal Deposit Insurance Corp.] has also **finalized a rulemaking** related to those misrepresentations. I think there are questions that some individuals have had about is their money in a dollar-denominated stablecoin, or is it in a true cash deposit that's insured? Many people may not know the difference. We think people should be upfront about that.

We're also confronting the question of will a stablecoin or other type of digital currency one day ride the rails of the Big Tech payment platforms? Then adoption for consumer payments could really surge.

So we have really looked at this primarily through payments. I'm not saying there aren't some other consumer financial product issues — we have started to hear about how the intersections of crypto and credit cards, ATMs, mortgages and other loan products are working. But I would say the primary focus, at least from the CFPB perspective, is around preparing for real-time payments.

Is this a potential use case for the bureau's **risk-based nonbank supervision** authority?

To be clear, our Section 1024(a)(1)(C) authority doesn't create any new jurisdiction for the CFPB. It allows us to supervise entities based on indicia of risk, but those entities would already be covered under the enforcement jurisdiction.

I think there are certain payments issues that could be applicable there. I think more broadly, there are a lot of firms involved in data — collection and monetization of financial data. There are also a host of other nonbanks that are growing very, very rapidly, where we may be seeing consumer complaints or other issues.

It's not an authority that I think will be bread and butter, but it's an important vehicle for us to supervise certain nonbank firms in addition to the existing enforcement jurisdiction.

Speaking of payments, another fintech-related issue is fraud in peer-to-peer payments on platforms like **Zelle** and **Venmo**. From where you sit now, do you think banks and other platform operators are doing a good enough job of helping consumers who get scammed on these services?

I actually got a real front-row view of this in a few different areas in the past decade. One was in student debt relief at my first stint at the bureau and while I was at the Department of Education. At the [Federal Trade Commission], I devoted quite a bit of time looking into romance scams, which often disproportionately target the elderly, and identity theft issues writ large. The more and more data there is about us, the easier it seems to be for people to steal our identities. So I don't want to make any overall assessment of where the industry is or is not living up to its expectations.

I do think that, on one hand, there has been the experience across the developed world that, when real-time payments turns on and gets broadly adopted, the amount of fraud and errors and scams surges. I would like the United States to take a different path.

We're looking at this broadly. It's part of what we are asking about in our Big Tech payments orders that we issued about six months ago. I don't want to comment specifically on Zelle or Venmo, but we obviously look very closely at how those apps are operating. And we will continue to look at some of those issues and figuring out ways forward.

I want to acknowledge that there are a number of players in this space that have started to make changes to their user interface and user experience to address some of those customer issues, including asking someone what the last four digits of the recipient's phone number are or going through a couple more steps to make sure that the sender-recipient transaction is a legitimate one.

So is this a problem where you see the solution as more based in improving disclosure and education? Or is this actually going to come down to maybe trying to redraw the lines of liability?

I think there's a whole host of issues. One is about consumer expectations. When you use your debit card or your credit card, there are certain embedded protections about it. You're asking about what would be considered the consumer's mistake versus what would be considered a bank error, what's fraud and what not. Right now, I've asked the staff to take a look at really the voluminous number of complaints we've been receiving and surface whether there's things we need to communicate, whether we need to pursue any other regulatory initiatives on it.

I don't have an answer for you now, and I'm being hesitant because you mentioned two company names, and I don't really want to comment on those two companies. But we're looking holistically at real-time payments and the attendant issues.

Let's pivot to another fintech issue. Deputy Director Zixta Martinez said last month that the CFPB is "taking a close look" at "rent-a-bank" lending partnerships, and that the bureau shares concerns consumer advocates have raised about these arrangements. Can you elaborate on the bureau's concerns and how it's scrutinizing these partnerships?

One, we're very interested in making sure we're adequately enforcing the Military Lending Act. The Military Lending Act, starting in 2013, is part of our enforcement jurisdiction. There had been issues where some entities that have partnered with banks have been violating some of those provisions.

More big-picture, I think we're very interested in the issue of relationship banking. We often hear, and it's true, that there is a different model for small institutions that operate in the community. They're mostly funding loans through deposits, they're dealing with a lot of repeat customers, and it's slanted more toward small business and consumer lending.

But at the same time, when small institutions are mostly just a vehicle for a rent-a-bank arrangement, that makes it harder for us to make sure that everything is above board. We do not have supervisory authority over those small, small banks, generally speaking, though many of the nonbanks that partner with them are subject to our supervisory authority.

Look, it's an ongoing issue. We hear concerns from a lot of states about how entities are evading certain state consumer protection laws. Federal law sets up a framework for how preemption should work and not work, and there is a concern from some that this is a vehicle to evade that framework.

The bureau has used its Unfair, Deceptive or Abusive Acts or Practices authority in the context of tribal lending to go after alleged instances of sham partnerships facilitating high-cost loans. State attorneys general have also brought cases against fintechs that are in these partnerships. Is there scope for the bureau to use its UDAAP authority to challenge partnerships between banks and nonbank lenders?

I wouldn't frame it the way you're framing it. I think the jurisprudence on unfairness, if you look at both CFPB and FTC precedent, uses the unfairness prongs not as a matter of looking at the nature of the partnership, but as a matter of analyzing the conduct. To be liable, it has to meet the prongs of injury not being reasonably avoidable, and not having countervailing benefits that outweigh it.

For example, the FTC has done a series of cases, and the CFPB has as well, on payment processors and the extent to which they had adequate safeguards in place to police certain types of conduct.

In some of those lending partnership cases, there's been an allegation of deception — that it's deceptive to enforce a loan that you as the nonbank "true lender" couldn't have validly made in the first place.

Yeah, that's true. And in fact, you might want to take a look at our recent ACE Cash Express **complaint**, and as well as our report that we published on state extended repayment plans. I think it touches on some of what you're saying, including with respect to deception theory.

Repayment plans were also brought up by the deputy director in comments on payday lending, which the bureau tried to regulate with ability-to-repay requirements that were promulgated in a 2017 rule. Those requirements were challenged and eventually repealed, and there's an ongoing challenge to other payment-related parts of the 2017 rule.

That's still going through the process. But we are continuing to work with states and others on supervision of payday firms. We will continue like we did with ACE Cash, with enforcement.

We're still looking closely at that market. I will say, though, that there are differences from many years ago, including that there have been a number of states that have **implemented rate caps**. Those rate cap laws have changed a lot of those state-based marketplaces, so we're going to continue to look at the data and see where it takes us.

I didn't hear rulemaking in that. Is this an area that you might consider revisiting with rulemaking?

I think it's too early to tell. As we've shared publicly, our focus on rulemaking is really the rulemakings that have not been implemented yet.

We have a number of very significant ones. One of them is somewhat more narrow, about algorithmic appraisals, but two are very significant — one, the required rule on **small business data collection**, and the other one, the Section 1033 rule on personal financial data rights.

And we have other rulemakings. We finalized a **Libor transition rule**, and we're starting our work on **credit card late fees**. So we have a lot of rules going on, and we'll make more determinations as the weeks and months go on.

You just mentioned credit card late fees, but you've also talked a lot about overdraft fees as part of your efforts to curb excessive fees charged to consumers. Are you seeing results from these efforts?

Yes, particularly when it comes to overdraft and nonsufficient funds fees, we're seeing a real set of changes in the market. I think a lot of banks are starting to rationalize their full set of fees that they charge, and we're asking that our examiners **focus more attention** on the institutions that have an aberrant level of their deposit account fee revenue coming from those sources. We've also worked on **pay-to-pay fees** in the debt collection context, and we received an overwhelming 80,000 submissions to our request for information on fees charged in financial services.

I think a lot of financial institutions realize they don't want to scare their customers away with junk fees. They want to keep them with good service. I think the institutions that really treat it as a service are going to do well. But there are some that program their systems in ways to trigger more fees, and you've seen the CFPB enforcement actions on some of these. Not everyone treats it like a service.

You've made some changes to the way the bureau examines for discriminatory conduct, expanding that to include this concept of unfair discrimination that relies on the bureau's UDAAP authority. How do you respond to concerns from industry about whether this means the CFPB will start pursuing disparate impact-style claims using its UDAAP authority?

Disparate impact is a different doctrine that is aligned with the Equal Credit Opportunity Act, Fair Housing Act and others. It is different than unfairness doctrine, and I think I have not heard of a robust rebuttal that discrimination may not meet the criteria under the unfairness standard. This

issue has been a subject of previous examination manuals by the banking regulators.

One of the pieces of feedback I've heard over the years was that industry wants to know more about how the CFPB might exercise its supervisory authority and enforcement authority. We've tried to respond to that about what sometimes is described as regulation by enforcement — most law enforcement agencies, they bring enforcement cases and they use the U.S. common law system to develop the law. We've tried to dramatically increase the number of guidance documents that share how we might exercise that authority on a broad range of laws. And we publish our examination manuals, which is essentially guidance to our examiners about what they might look at when they decide in the scope of an exam to dig into a specific set of complaints or issues.

So it is our attempt to try to really share with entities, what does the test look like if they get complaints of discrimination on noncredit products?

When you put out some of this guidance, there has been procedural criticism that it's not being put out for notice and comment, that it should go through a formal rulemaking process. And there have been a number of policies issued in some sort of final form, and then you might accept comment on them after.

So let me pin you down on that. What have those been? Because I keep hearing this, but no one will give me specifics. So I hear you on the UDAAP, but what else?

Another example would be the administrative adjudication procedural rules that were changed.

Well, on administrative adjudication procedural rules, I believe that the standard is those are procedural rules. We have not even used them. Every single one of our enforcement actions and litigations we brought through federal court. We're certainly taking feedback and comments on those rules, which we are assessing. But I think the premise of your question was that there was some sort of change in the obligations of financial firms, so that's why I was probing a little.

I mean, that is the argument that some critics in the industry make. For example, with the UDAAP exam manual, they say it does impose new requirements.

But how, though? How does it impose a new burden? That's what I would have you ask them. The truth is, there are supervisory highlights that include citations of noncompliant conduct on a range of laws, including the prohibition on unfair, deceptive and abusive practices. So to me, the better, more responsible way is to share when we do have some sort of analytical approach.

We're trying to be responsive to many who say, "Please do share it, because it actually helps us evaluate the complaints we're getting, evaluate our systems."

The fair lending laws list specific protected classes that they prohibit discrimination against, but the new UDAAP exam manual doesn't list specific classes like that. Is that something the bureau plans to shade in through additional updates?

We have heard those questions. We're looking at that to see what we can share more, but remember that this is unfairness. There are different standards, the standards being injury, reasonable avoidability and countervailing benefits.

And by the way, that's not a new standard. That standard has been in place since 1980, when the [FTC's] unfairness policy statement was put into place. And of course, the [FTC Act] prohibition on unfairness has been there since the early 1930s. There is quite a bit of doctrine and legal precedent that has interpreted that, for which that might be instructive.

You've made a big point of wanting to take on corporate recidivists and repeat offenders. When might we see this translate into enforcement action settlement terms, like including

some admission of wrongdoing? Is that something you're considering as part of your enforcement approach?

I've emphasized in the past the importance of findings of liability, sometimes admissions, and I think you should expect that we are focusing quite a bit on **large market actors** engaged in repeat offenses.

I have asked the staff to take a broad look at updating our approach to remedies. I think we want to be more focused on making sure that we look at the underlying business incentives, the individuals that called the shots, and I think maybe perhaps a little bit less of an emphasis on the kind of paperwork provisions, although the documentation can be important. So stay tuned.

Certainly, we did **finalize an action** that essentially was a repeat offender and that ultimately led to a prohibition on continuing to do lending.

And we have established some more focus and units within the agency on compliance order monitoring. Overall, we believe that the approach to compliance order monitoring across the board is increasing, but we will scrutinize carefully when court orders and agency orders are being violated.

You've created additional units focused on compliance order monitoring?

That's not to say that there weren't groups doing it before. But we have sharpened our focus on it and increased attention and, often, resources to it.

You should look at the body of work to date, and if you look at the CFPA civil penalty factors, the issue of whether there was intentional and willful misconduct has a major part in the remedial approach. And as I've previously shared, the CFPB can — in terms of its full set of remedies — not just get redress and disgorgement and civil penalties, but also order limitations on the activities of the firm that has violated the law.

Also, you're going to see, and I think you've probably already seen, some more joint actions with state agencies. We also recently **finalized one** with the [Office of the Comptroller of the Currency]. Those other entities may have additional remedial tools at their disposal, as well.

So you're taking a very broad approach, and we will see the bureau pursue a broader range of remedies under your leadership.

Yeah, and remember, it's different when it's a case before a federal court or a settlement. We would have to argue in federal court that a remedy was authorized by law and is appropriate, and even in settlements, most enforcement matters take years to develop. It's not something that happens overnight.

I have also taken the view that it's highly inappropriate to only think about individual liability with small firms. We should be focused on the facts, and if the fact pattern is the same, with individual liability, there's not an exemption because you work at a larger firm. And in **one of our repeat offender actions**, we did charge a longtime former executive with certain counts.

Just one more thing before you have to go — you've taken a lot of flak from Republicans and industry groups since you came in as director. What do you take away from these criticisms? Is it at all changing how you approach your job?

Well, we try and listen carefully to everyone. I don't really see this as a partisan issue, but across the board, Big Tech companies are certainly pushing back against the government for coming under scrutiny — I've seen this firsthand. We have to deal with the fact that these large tech firms are entering financial services, and they have to play by the same rules. We will go through the process of gathering evidence to make determinations, and that's how we have to proceed.

--Editing by Marygrace Anderson and Emily Kokoll.

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