

CFPB Expands UDAAP Examinations to Target Unfair Discrimination

Supervision manual updates apply ECOA-like antidiscrimination reviews to all consumer financial products and services

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Changes to Exam Manual for Evaluating UDAAPs

- CFPB press release states that discrimination may be “unfair” under UDAAP legal standard
- Dodd-Frank Act prohibits unfair, deceptive and abusive acts and practices (UDAAPs)
- Legal standard for unfairness = an act or practice that
 - (1) causes or is likely to cause substantial injury to consumers,
 - (2) the injury is not reasonably avoidable by consumers, and
 - (3) the injury is not outweighed by countervailing benefits to consumers or to competition

Consumer Finance Markets CFPB Will Examine for Discrimination

- Credit
- Servicing
- Collections
- Consumer reporting
- Payments
- Remittances
- Deposits

Examples of Unfair Practices

- The revised manual offers only a couple of examples of discriminatory conduct that may constitute unfair practices:
 - Not allowing African-American consumers to open deposit accounts
 - Subjecting African-American consumers to different requirements to open deposit accounts
- The revised manual appears to cover both disparate treatment and disparate impact.

Review Elements

- Documentation
 - Use of models, algorithms and decision-making processes
 - Information collected, retained or used regarding customer demographics –
 - breakdowns for product uses, fees, revenue sources and costs
 - impacts of products and services on specific demographics
 - Demographic research or analysis used for marketing

Review Elements

- Policies
 - Antidiscrimination controls and monitoring
 - Established process for periodic analysis and monitoring of all decision-making processes, including a corrective action process
 - P&P to review, test and monitor for potential UDAAP concerns, including discrimination
 - P&P to mitigate potential UDAAP concerns, including discrimination
 - P&P themselves do not target, exclude or offer different terms or conditions in a discriminatory manner
 - Antidiscrimination training for customer service personnel

Transaction Testing

- Areas for transaction testing – comparing one customer demographic to other customer demographics for:
 - Inferior terms
 - Offering or providing more products or services
 - Customer service quality/exceptions provided
 - Targeted advertising or marketing
 - Decision-making processes in eligibility determinations, underwriting, pricing, servicing or collections that result in discrimination
 - Failure to evaluate and make necessary adjustments and corrections to prevent discrimination

Transaction Testing

- Transaction testing may include:
 - Marketing – institution should not improperly target or exclude consumers on a discriminatory basis
 - Terms consistent with disclosures and policies – examiners may review the institution’s decision-making processes and inputs used
 - Third-party oversight – entity should ensure employees and third parties who promote products or services are adequately trained in antidiscrimination, and should have a corrective action process
 - Servicing and collections –
 - Call centers should effectively respond to calls from consumers with limited English proficiency
 - Should ensure employees and third party contractors refrain from practices that lead to **differential treatment** or **disproportionately adverse impacts** on a discriminatory basis

Compliance Challenges

- Breadth of changes
 - Appears to cover all aspects of all consumer financial products and services
- Testing
 - What to test and how to test
 - What is the appropriate testing framework and methodology for non-credit?
 - What is a legally sufficient business justification in the non-credit context?
- Financial and other costs (e.g., internal resources)

Legal Questions

- Dodd-Frank Act expressly authorizes CFPB to “prescribe rules ... identifying as unlawful unfair, deceptive, or abusive acts or practices”
 - Notice-and-comment rulemaking
 - Is exam manual “final agency action” under APA
- Congress has chosen to outlaw discrimination in certain contexts (e.g., ECOA, FHA)
- Scope of “prohibition”
 - Prohibited bases vs. “customer demographics”

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