ALERTS

New CFPB UDAAP Examination Manual Announces Anti-Discrimination Agenda

March 24, 2022

The Consumer Financial Protection Bureau revised its Examination Manual to announce that the Bureau will pursue discrimination as an "unfair" practice under its authority to address unfair, deceptive or abusive acts or practices ("UDAAPs"). These revisions preserve all of the prior edition's guidance while adding the Bureau's view that discrimination qualifies as an unfair practice it has the power to correct. Although the CFPB has several nondiscrimination statutes in its toolkit, the Bureau intends to leverage its UDAAP authority to reach "situations where fair lending laws may not apply."[1] This follows the CFPB's commitment last year to exert its full statutory authority to root out "abusive" practices.[2]

The Dodd-Frank Act gave the CFPB expansive power to pursue UDAAPs in connection with consumer financial products or services.[3] An act or practice is unfair when (1) it is likely to cause substantial injury to consumers, (2) consumers cannot reasonably avoid the injury and (3) countervailing benefits to consumers or competition do not outweigh the injury.[4]

The Examination Manual illustrates how discrimination fits into this rubric and underscores along the way that the CFPB will take an expansive approach to UDAAP enforcement in all areas. Previously, injury meant economic harm that consumers had suffered or were likely to suffer if the act or practice continued. The revised Examination Manual highlights that the "emotional impacts or dignitary harms" of discrimination also qualify, as well as the "denial of access to products or services."[5] The Manual states conclusively that "Consumers cannot reasonably avoid

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discrimination."[6] The Manual does not specifically address how the Bureau will weigh countervailing benefits in discrimination cases, suggesting that there is no balancing to perform.

The Examination Manual makes clear that the CFPB will use this authority to target discrimination directly, even where no other statute would allow the CFPB to intervene. "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 [the Equal Credit Opportunity Act] ECOA does not apply."[7] Where other statutes do apply, the CFPB is likely to seek relief for each violation. As an example, the Manual advises that "a discriminatory act or practice that is unfair, deceptive, or abusive may also violate other antidiscrimination laws, such as ECOA."[8]

Starting now, CFPB exams will collect information specifically directed at uncovering discrimination in consumer financial products and services. Among other things, all exams will gather any customer demographic information the financial institution collects, including "any demographic research or analysis related to marketing or advertising" consumer financial products and services.[9] Transaction testing is more likely to follow in the exam where there are demographic differences in the offers, terms, or availability of the entity's products or services, marketing or customer service.[10] The CFPB will look for discriminatory outcomes regardless of whether there is any evidence of discriminatory intent.[11]

All exams will also gather "documentation regarding the use of models, algorithms, and decision-making processes."[12] This puts in focus algorithmic bias as a key CFPB priority. Director Chopra has asserted that "we should never assume that algorithms will be free of bias."[13] He forecasted that the Bureau would work to uncover how algorithms work in order to root out bias in automated decision-making. "When consumers and regulators do not know how decisions are made by the algorithms, consumers are unable to participate in a fair and competitive market free from bias."[14] The CFPB also recently released guidance on steps financial institutions can take to prevent algorithmic bias in home valuations.[15] In this regard, financial institutions are well served to conduct their own analysis to test for and address discriminatory

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outcomes in their products and services, including how they reach out to consumers in the first place such as digital advertising.[16]

Financial institutions should also review their written policies and procedures ahead of their next exam. Examiners will expect financial institutions to have policies and procedures in place "to prevent discrimination" in its products and services including evaluating "all policies, procedures, and processes for discrimination prior to implementation or making changes" and on an ongoing basis.[17] Examiners will also expect financial institutions to train their customer service personnel to prevent discrimination, and ensure that the institution has the ability to take calls from consumers, including consumers with limited English proficiency.[18] Financial institutions will also be expected to demonstrate they have "a process to take prompt corrective action if the decision-making processes it uses produce deficiencies or discriminatory results."[19]

This relatively modest revision of the examination manual calls for financial institutions to pay close attention to traditional UDAAP concerns and now also disparate outcomes the Bureau will pursue as discrimination. The Manual calls for financial institutions to demonstrate "established policies and procedures to review, test, and monitor any decision-making processes it uses for potential UDAAP concerns" of any nature, as well as policies to mitigate the concerns it uncovers.[20] Examinations will also evaluate financial institutions' third-party service providers, especially those who service or collect debts in ways "that lead to differential treatment or disproportionately adverse impacts on a discriminatory basis."[21] Financial institutions should review and update their policies and compliance programs to meet these new expectations. This wave of examinations may produce enforcement actions by which the CFPB will seek to stop certain industry practices under this expansive UDAAP umbrella.

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If you have any questions concerning this *Alert*, please contact your attorney at Schulte Roth & Zabel or one of the authors.

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[1] Press Release, CFPB, *CFPB Targets Unfair Discrimination in Consumer Finance* (Mar. 16, 2022).

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[2] *CFPB Policy Rescission Stakes Out Broad Enforcement Authority*, *SRZ Client Alert* (Mar. 22, 2021), *available at* https://www.srz.com/resources/cfpb-policy-rescission-stakes-out-broad-enforcement-authority.html.

[3] Dodd-Frank Act of 2010 § 1031 (codified at 12 U.S.C. § 5531).

[4] CFPB, *UDAAP Examination Manual* at 1-2 (3d ed. 2022) ("Manual"), *available at* https://files.consumerfinance.gov/f/documents/cfpb_unfair-deceptive-abusive-acts-practices-udaaps_procedures.pdf.

[5] *Id.* at 2.

[6] *Id.*

[7] *Id.* at 10.

[8] *Id.*

[9] *Id.* at 12.

[10] *Id.* at 15.

[11] *See id.* at 2 (past injury not required, only a likelihood of future injury), 7 (intent to deceive unnecessary for deception to exist).

[12] *Id.* at 12.

[13] Remarks of Director Rohit Chopra at a Joint DOJ, CFPB, and OCC Press Conference on the Trustmark National Bank Enforcement Action (Oct. 22, 2021), *available at* 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/.

[14] *Id.*

[15] CFPB, *Consumer Financial Protection Bureau Outlines Options To Prevent Algorithmic Bias In Home Valuations* (Feb. 23, 2022), *available at* https://www.consumerfinance.gov/about-us/newsroom/cfpb-outlines-options-to-prevent-algorithmic-bias-in-home-valuations/.

[16] Manual at 16.

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[17] *Id.* at 13.

[18] *Id.* at 14, 18.

[19] *Id.* at 18.

[20] *Id.* at 14.

[21] *Id.* at 18.

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