

# Consumer Finance Monitor (Season 5, Episode 15): The CFPB Takes Aim at Discrimination as “Unfair”: What Does It Mean For Your Business?

Speakers: Alan Kaplinsky, John Culhane, Ronald Vaske, Heather Klein

Alan Kaplinsky:

Welcome to Consumer Finance Monitor podcast, where we explore important new developments in the world of consumer finance. I'm Alan Kaplinsky, Senior Counsel with Ballard Spahr. I'm formally the Chair of the Consumer Financial Services Group. We are going to be doing a podcast today that is predicated and based on a webcast that we did not long ago on a very important topic. And we wanted to make sure that our podcast listeners are as aware of this issue as the listeners to our webcast. And the name of the show today is The CFPB Takes Aim at Discrimination as Unfair. What Does It Mean for Your Business?

Alan Kaplinsky:

And let me describe to you briefly what the CFPB has done. And they did it not by issuing a request for information or a request for comments, but rather by amending the supervision examination manual dealing with what is an unfair or deceptive act or practice, or a UDAAP violation. And they did something that is really unprecedented and, in my view, really constitutes pushing the envelope quite far.

Alan Kaplinsky:

So they announced that they intend to consider discriminatory conduct as an unfair act or practice. And it represents, as I said earlier, a significant expansion of the bureau's authority to address unfair, deceptive, or abusive acts or practices. The bureau has directed its examiners to treat any discriminatory conduct by a supervised entity in connection with offering or providing consumer financial products or services, whether or not covered by fair lending laws, such as the Equal Credit Opportunity Act, as possible unfair acts or practices to which the bureau's UDAAP authority applies.

Alan Kaplinsky:

And so during today's podcast, we have three presenters. We're going to discuss these topics. The CFPB's theory for treating discrimination as unfair, the types of products, services, and discrimination the bureau's theory could reach, information and issues CFPB examiners will be considering when looking for discriminatory conduct in UDAAP examinations, the implications for entities that are not supervised by the CFPB or not subject to CFPB jurisdiction, potential legal challenges to the CFPB's theory, and what companies should be doing now to prepare for the CFPB's expansion of its UDAAP authority.

Alan Kaplinsky:

And indeed, as you'll find out during the last presentation today by John Culhane, there is much that needs to be done by companies that are being supervised by the CFTB. And this is an area that companies that are subject to their supervision have never had to prepare for before. So we are involved in helping several companies get ready for this type of special UDAAP examination. And of course, we'd be happy to help any of our clients that are interested in getting our assistance to prepare for this kind of an exam.

Alan Kaplinsky:

So let me introduce our presenters today on our podcast show. First, John Culhane, who is a partner in our Consumer Financial Services Group and a member of our Fair Lending Team. Second, is Ron Vaske. He's Co-leader of our Fintech and Payments Team. And finally, Heather Klein. Heather is of counsel based out of our Philadelphia office, and she counsels

financial services clients on a wide range of consumer financial services issues. So without further ado, let me now turn our show over to Ron Vaske.

Ron Vaske:

Thanks, Alan. First, I want to talk about where did this come from? And it really, it seemed to come out of nowhere. But if we look back over the past couple of years, this maybe shouldn't be so much of a surprise. In 2020, as an FTC commissioner, Director Chopra gave a concurring opinion in a ECOA matter against Liberty Chevrolet. And in that case, he argued for how UDAAP and unfairness could be applied to achieve the same result. After that, last year, there was a white paper that was published by the Student Borrower Protection Center. It may have largely gone unnoticed, but it really basis its analysis on Chopra's theory and sites Chopra extensively and really lays out how UDAAP and unfairness can be used to apply to discrimination cases that otherwise might not be covered under typical discrimination laws.

Ron Vaske:

So how does the bureau justify it? How do they say that discrimination is unfair? Well, under the Dodd- Frank Act and under section 5(n) of the FTC Act, the statutes clearly define what is unfair. First, it has to be, it's a three-part test, it has to be something that causes a substantial injury to consumers, has to be something that is not reasonably avoidable by consumers and is not outweighed by countervailing benefits to consumers or competition. We'll talk quickly about each of those three.

Ron Vaske:

What is a substantial injury? Well, typically it means monetary harm, such as higher fees. However, with respect to discrimination, the bureau added to the exam manual a couple of examples that apply more neatly to illegal discrimination. It could also mean opportunity costs associated with the inability to obtain a financial service. If you can't get the service because of your race, for example, you will have costs that apply because you didn't get that service. In addition, the exam manual now, the addition to the exam manual talks about it in the case of discrimination that it could even be, substantial injury could be emotional impacts or dignitary harms that would contribute to a substantial injury.

Ron Vaske:

Second, not reasonably avoidable by consumers. Longstanding FTC definition that's adopted by the CFPB in the exam manual goes through what that means. And the bottom line of what it really means is that it effectively makes it difficult, or it hinders the consumer's ability to make a decision on whether to obtain or use the product or service. The exam manual updated, with respect to discrimination, talks about it in the context of there must be no practical means to avoid it and the actions the consumer is expected to take must be reasonable. And then it goes on to talk about typically consumers cannot avoid the harms of discrimination. So it fits into the second part of the three-part test in that way.

Ron Vaske:

The third part, not outweighed by countervailing benefits to consumers or competition. They didn't make any changes to the exam manual to explain this in how it applies in the context of unfair discrimination. But it's probably intuitive that if the discrimination really is based on a protected class, that there really couldn't be any benefit to consumers or competition. If it is, in effect, based on or used for a purpose that would not be discriminatory, a valid business purpose, then it would be, under this theory, still unfair if a different practice could achieve the same result that didn't have the disparate impact on a discriminatory basis.

Ron Vaske:

So what types of products and services are potentially reached by this that aren't already reached under existing law, such as the Equal Credit Opportunity Act or the Fair Housing Act? It's basically everything. It's deposits, it's funds transmission, it's debt collection, check cashing, anything you can think of that might fit into the realm of consumer financial services or the practices related to those.

Ron Vaske:

It also applies in the context of credit where the ECOA or the FHA might not completely cover the field. For example, the Equal Credit Opportunity Act is limited to discrimination against applicants and prospective applicants. And there's authority out there to suggest that the ECOA would not apply to prescreening, for example, because the subjects of the prescreen are not applicants or perspective applicants. Similarly, the ECOA only applies to discrimination by creditors. However, there are other parties that may have a substantial effect on the credit decision, such as the signees of a loan who would establish criteria for what loans they would be willing to purchase.

Ron Vaske:

In addition, the Civil Rights Act of 1964 already prohibits discrimination in contracting generally. That would apply to credit products and noncredit products. But through interpretation, that's been determined it only applies to intentional discrimination and the categories of protected classes are much fewer. In addition, the Civil Rights Act of 1964 is not something that the bureau or the agencies have authority to enforce.

Ron Vaske:

Other limitations under existing law. As I mentioned, each of these existing laws specifically applies to a scope of persons who fit into a protected class. All of them prohibit discrimination on the basis of race, national origin, religion, and sex. But FHA, Fair Housing Act, for example, prohibits on the basis of disability and familial status. But the Equal Credit Opportunity Act does not. Equal Credit Opportunity Act, on the other hand, prohibits discrimination on the basis of race or of age, receipt of public assistance, and marital status. But the Fair Housing Act does not. Under the unfairness theory, could potentially apply to all recognized protected classes. That's the argument that's made in the white paper I mentioned earlier, that it should apply to all class that's been identified in any existing law.

Ron Vaske:

Perhaps the biggest concern or the biggest change that results from this update to the exam manual is that the discrimination here would not have to be intentional discrimination. It would apply in the context of disparate impact, which is an ECOA or Fair Housing Act theory or discrimination law theory. And it means that it applies to a facially neutral policy or practice that results in disproportionately adverse effects on members of a protected class. So no intent required. It's based on how the outcome is with respect to the policy. How would this apply in the real world?

Ron Vaske:

Well, the white paper gives a couple examples. Talks about reverse redlining, and that would be a practice where an unfair product was targeted at a protected class, or it has a disproportionately adverse effect on the protected class. Another example they cited was account opening policies that have disproportionately adverse effect on a protected class. The policy may apply universally to everyone, but members of a protected class may be differently affected or there's statistical evidence to suggest that the result that is achieved by application to the protected class is more adverse.

Ron Vaske:

Finally, another example that they cite are dispute policies. In particular, in the white paper, they talk about it in the context of credit reporting. But it could apply to any kind of dispute that you might have that might have a disproportionately adverse effect on a protected class. Again, policy could be neutral and apply to all customers, but it may have a more adverse effect on members of the protected class.

Ron Vaske:

I'll turn it over to Heather and she will continue with talking about examination procedures and what you should do to prepare.

Heather Klein:

Hello, everybody. Nice to be with you today. So let's chat about the additional headache that this is causing for you if you are an in-house fair lending lawyer or a compliance officer or anybody else who now has a responsibility with getting your organization ready to base off in a UDAAP exam that now is supplemented by these additional discrimination aspects.

Heather Klein:

So what I'm hoping to do in the next five or 10 minutes is walk through the updates to the exam manual, the updates to the UDAAP exam procedures specifically, and give you some examples based on the fair lending exams that we've participated in, examples about what this could look like outside of the fair lending context and in a broader context because we expect that the CFPB's playbook is going to come largely from its fair lending exams that it has done, because the additions to the UDAAP exam procedures read like a fair lending exam but outside of a specific fair lending context and in a broader discrimination context.

Heather Klein:

So just to start off, at a high level, how does the CFPB describe its updates to the procedure? So if you go on their website and click on their little summary, they highlight three areas that they focused on in the update. One being the practices themselves. So the examiners are directed to evaluate discriminatory practices as potential unfair practices. Secondly, they're not only interested in the practices but on the decision-making processes that get an entity to the practices or to the various customer outcomes. And then thirdly, the examiners are going to be looking at the safeguards to prevent discrimination, so monitoring, auditing, what kind of corrective actions are being taken. So we'll get into these in more detail.

Heather Klein:

So the first kind of discreet category that was amended in this new release of the UDAAP exam procedures was what are examiners going to be requesting when they start off an exam, and what are they looking at? And so there were two main additions here. One being documents regarding the use of models, algorithms, and decision-making processes used in connection with consumer financial products and services. So this is interesting, right? Because you usually see models and algorithms in relation to a fair lending exam, but now they are porting this over into an unfairness review and really looking more broadly at models and algorithms outside of the pure fair lending context.

Heather Klein:

They're also going to be requesting more information on customer demographic information that an entity collects, retains, or uses. And that could include how products and services are used by different demographics, what the fee revenue is, the different revenue sources, what the costs are to the extent that an organization is classifying those based on customer demographics, or even if the system does it without people at the organization really being aware that the system is doing it, the CFPB is going to be asking for that information. They will also be asking for demographic research or analysis related to marketing or advertising, which, of course, organizations conduct in the course of evaluating the efficacy of where their dollars are going for marketing and advertising campaigns, and so all of these are going to be brought into this updated UDAAP exam.

Heather Klein:

So for example, in some of the fair lending exams that we've been a part of, the requests have included does your organization maintain information on an account level or a product level about characteristics of customers, including all the protected characteristics, so race, ethnicity, sex, marital status, religion, national origin, whether the customer receives income from public assistance programs, what the customer's age and date of birth is? So to the extent that your organization's system is capturing any of those categories, that will be part of a data set that the CFPB would be asking for.

Heather Klein:

In addition, does the organization collect any visual information about a customer, like a driver's license or a photo ID? Where is that stored on the system, and how is that used? Additionally, like on the marketing context, for instance, does the entity target market to particular populations that would directly or indirectly be protected classes, and what's the reason for the organization targeting in that fashion providing sample of ads?

Heather Klein:

So those are all going to be considered as part of whether there is discrimination and whether it meets the unfairness test.

Heather Klein:

The second key piece of the update to the exam manual comes in the section of what examiners are going to be reviewing in policies and procedures and customer complaints, in statistical and management reports and internal/external audit reports, and in their conversations with management. And so some of the highlights of the updates include not only are policies, procedures, and processes whether they are evaluated for discrimination prior to being rolled out, but also is that evaluation done again before they're modified? And are policies, procedures, and processes monitored for discrimination specifically? And then beyond that, targeting the substance of the organization's products, do they target or exclude consumers or offer different terms and conditions in a discriminatory manner?

Heather Klein:

So for example, the CFPB might ask the organization to provide summaries, memoranda, reports, analyses, et cetera, et cetera of reviews conducted by the entity into various policies, procedures, processes. Furthermore, they'll have the entity describe or provide policies, procedures, practices that differ based on a protected class, or something that would be correlated perhaps with a protected class, geography, race, religion, national origin, sex, marital status, age, receipt of public assistance income, et cetera.

Heather Klein:

And then not only looking at do the policies, procedures, and processes differ based on those protected classes, but are there any policies or procedures that contain facially neutral criteria that could have a negative impact on a protected basis? So you're seeing here both the two theories of under fair lending. And we think that would be likewise ported over into this kind of an exam. So for instance, in the marketing context, do outreach policies vary by geography?

Heather Klein:

And then talking more about the internal controls aspect of this, which is going to be a focus of these kinds of exams, the CFPB will be asking to see controls that review, test, and monitor decision-making processes for UDAAP concerns, including discrimination and whether the organization upon getting the results of these tests and audits, whether it takes corrective action or otherwise acts to mitigate a risk. So to the extent that your organization is not currently auditing all of its processes, procedures, and processes with this discrimination lens in mind, that would be a thing to look at across your organization and to see if there are ways to supplement your existing controls with the CFPB's new guidance in mind.

Heather Klein:

So for instance, in fair lending exams that we've been a part of, the CFPB has asked for the entity to identify software or databases that are used to monitor, for instance, servicers, and then just asking the entity to describe how it relies on the software to monitor for discrimination compliance among servicers. So that would be an example. Another example would be the CFPB would ask an entity to list and describe corrective measures relating to discrimination that were taken as a result of the entity's audits, monitoring, et cetera. So they're going to be digging deep there.

Heather Klein:

And then the last thing I want to talk about in this respect focuses on the customer service personnel who are the frontline interacting with your customers and what training they receive to prevent discrimination. You know, this is common among our larger clients, that they are training up their customer service personnel on non-discrimination laws. Hopefully, there has also been an effort over the past few years to supplement that training to educate customer service personnel and how they handle interactions with customers who have limited English proficiency. Because as you might recall, two Januarys ago, January 2021, the bureau released guidance on LAP customers. So really crucial to make sure that the training in place is effective there.

Heather Klein:

And not only the training itself, but I would add that the CFPB would be asking for completion records, the schedule of training, the percentage of customer service personnel who completed the training, what their scores were. So it's not only the training itself, but the processes around training, which hopefully should not surprise you because these are kind of core elements of what CFPB looks at when they look at training.

Heather Klein:

Okay. So before I pass this off to John Culhane is to talk through a bit more about what examiners will be looked at when they are scrutinizing the customer files and the data. And I want to give you a few examples here. They will look at whether an entity varies its product offerings by customer demographics. So a low-hanging fruit here would be are different products or services or different terms offered to a customer if they are located in, for instance, the U.S. Virgin islands, Puerto Rico, or another U.S. territory, or similarly, are there different terms offered based on a geography that's within the continental United States?

Heather Klein:

Additionally, taking a look at exceptions that are offered to customers and, for instance, if you're waiving a fee or if you're providing a premium customer service to individuals who have certain level of product from you, is that going to be disadvantaging in a discriminatory way customers who are not receiving that same assistance or not receiving the same ability to obtain exceptions, such as fee waivers or the like?

Heather Klein:

Discriminatory targeted advertising or marketing has been an issue that's been percolating for a few years, especially in digital marketing with different algorithms that Facebook or Google or other digital platforms have used, and so those platforms have been evaluating their own targeted marketing. And it's certainly been an issue among fair lending teams at depository institutions as well as, hopefully, some of the larger non-depository institutions. So this is going to become, I think, an even greater issue now that the bureau is expanding its, purporting to expand its authority in the enforcement and supervision of discrimination issues.

Heather Klein:

In addition, decision-making processes, ineligibility determinations, underwriting, pricing, servicing, or collections, that might result in discrimination. Going back even four or five years, the CFPB was starting to push on this, and perhaps even before this. But four or five years ago, one of our clients received an exam request in which the CFPB was trying to get at fair lending issues with servicing and collections in terms how, and the CFPB was asking questions such as how are repayment options offered to borrowers? What are the criteria the borrower, excuse me, the white paper by Rome and Colfax gave as an example, whether different settlement offers are going to be made available based on where a customer lives on a theory that a borrower who lives in a certain Census tract with a certain, or, borrower who has a certain income level will be likely or unlikely to be negotiating to settle their debt.

Heather Klein:

In addition, we're aware that at least one state regulator, I believe, is looking at collections, and I'm blanking a little bit on the terminology here, but the collections, the methodology and the algorithms for how often a customer is called and the like, different collection strategies. So the CFPB is giving itself additional authority, additional tools to be asking those questions of the servicing and collections operations.

Heather Klein:

We talked a few minutes ago about corrective action and risk mitigation. So that's going to be a focus as the CFPB looks at customer data. If they're seeing trends, they're going to be asking, okay, so if your audit saw a trend here, when you looked at this data, what kind of corrective action did you as the organization take?

Heather Klein:

So this is, depending on how you look at it, a huge headache or a lot of fun, depending on your level of enthusiasm. Certainly, a huge opportunity for in-house legal and compliance departments to train up their colleagues and to perhaps advocate for additional resources for their departments because this is certainly an expansion of the bureau's authority. And it's really going to take, I think, a lot of effort if you're an in-house compliance officer or lawyer. It's going to necessitate a higher level of diligence perhaps, depending on your existing level of diligence, but perhaps a higher level of diligence and communication with your business counterparts to make sure that everybody is rowing in the same direction here.

Heather Klein:

I will stop there and we'll hand you over to John Culhane.

John Culhane:

Thanks, Heather. I'm going to editorialize a little bit, and then I'm going to talk about the implications for entities that operate outside of the supervision of the CFPB or maybe outside of the reach of the CFPB. I'll talk about what seem to be the likely bases for legal challenges to this action. And then I'll conclude by talking about what to do, and a lot of what I'll say about what to do will echo what Heather has just said, probably in more detail than I'll have time to cover.

John Culhane:

But I want to start with a little bit of history here. Unfairness has a bit of a sorted past in the legal community. And Rohit seems to be determined to resurrect that sorted past. In that sorted past, which is housed at the FTC, the FTC basically focused tremendously on whether a practice offended its notion or the commissioner's notions of public policy and only later did that evolve to the standards that we see today.

John Culhane:

But remember, that the FTC Act has had unfairness in it since 1938. And you would think if unfairness really was as broad as it's being purported to be now, there wouldn't have been any need to enact the Fair Housing Act in 1968. There might not have been any need to enact the Equal Credit Opportunity Act in 1974. We could just rely on assertions of unfairness. And in fact, as I mentioned, the FTC had a history here of really asserting broadly that unfairness reached into all segments of the economy. Some of you who are my age or maybe a little younger may recall that at one time the FTC asserted that it could rely on its unfairness authority to ban all advertising to children. Likewise, Chairman Michael Pertschuk asserted that the FTC could rely on that authority to go after the employment of illegal aliens. Probably today, that wouldn't be the case, but it was certainly a broad stretch.

John Culhane:

Punish tax cheats. That was another action that Commissioner Pertschuk asserted the FTC could undertake. And in the early days of environmentalism, Commissioner Pertschuk asserted that unfairness would allow the FTC to go after polluters.

Basically, almost unfettered, unlimited authority which resulted in congressional action reining in the FCT, both limiting its funding, which unfortunately can't happen with the CFPB, but also then amending the FTC Act and changing the standards of unfairness to what we see today.

John Culhane:

Now, what is this presage outside of the CFPB realm? Ron talked a little bit about the FTC. I'm going to talk a little bit about it as well and a little bit more about what's been going on there. And obviously, the question here is how much traction is this notion going to get outside of the CFPB? What's going to happen for non-depositories and other entities subject to the jurisdiction of the Federal Trade Commission?

John Culhane:

Ron mentioned the concurring statement of Commissioner Chopra in the FTC's Liberty Chevrolet case, where he went out of his way to basically start staking out the turf for this position. That was followed in somewhat short order by an FTC business blog post by a member of the FTC's Bureau of Consumer Protection about algorithmic decision-making, and this is really where a lot of the action has been, a lot of the concerns have been expressed, asserting that the FTC could use its unfairness authority to go after decisions made by artificial intelligence models that had a discriminatory effect. And Commissioner Chopra referred to that as well.

John Culhane:

The examples that seem to be trotted out pretty regularly have to do with ridesharing models that had the effect of discriminating against women, other algorithms, including ones in the health industry and ones involving the allocation of resources for COVID-19 that were later determined to have a racial bent and not operate fairly.

John Culhane:

But the FTC hasn't really jumped into the pool here. Unlike the CFPB, it's just stuck its toe in the water. At the end of the year, the FTC issued a notice in its fall 2021 regulatory agenda about possible action under section 18 of the FTC Act. That's the section that allows the FTC to regulate unfair practices comparable to a provision in Dodd-Frank. So they're going very slowly. They have not signaled that they will be taking actions anywhere nearly as broad as those that are now going to be undertaken by the CFPB, instead a much more measured, much more modest approach.

John Culhane:

What does this mean for financial institutions that are supervised by the bank regulatory agencies and maybe fall outside of the jurisdiction of the CFPB? Well, obviously, this is all pretty new. So there haven't been any public pronouncements to date. None of the bank regulatory agencies, the FDIC, the OCC, and the Federal Reserve, have reached out and embraced this notion that unfairness is equivalent to discrimination.

John Culhane:

What we do have is the interagency guidance from 2014 when the Credit Practices Rule disappeared in which the agency said that their unfairness authority derives both from section five of the FTC Act and from sections 1031 and 1036 of Dodd-Frank. Up to this point, virtually all of the statements about unfairness made by the bank regulatory agencies had simply focused on section five of the FTC Act, in part because that's all there was. But none of the agencies have proposed to revise their examination manuals, their compliance guides, to take anywhere near this kind of action.

John Culhane:

In fact, they remain where they were prior to the CFPB announcement, distinguishing pretty clearly between unfair, deceptive, and abusive acts and practices and discrimination. Will they follow the FTC, or will they follow the CFPB? Obviously, it's too early to tell, but my thinking at this point is they're probably going to proceed slowly and they'll be more likely to follow the



cautious approach of the FTC. Now, that may depend in part on what the CFPB does, but I think they'll be considerably behind the CFPB.

John Culhane:

What about entities that are outside of the reach of the CFPB and are only subject to state mini FTC Acts? Those are acts that are similar to the Federal Trade Commission Act that as a matter of state law prohibit unfair or deceptive acts or practices and in some cases abusive practices. Again, we're sort of in the same position here that we are for depository institutions not subject to the jurisdiction of the CFPB. There's not been any great rush to embrace the position taken by the CFPB, although, obviously, all of this is pretty recent. What we do know are that many of these statutes in their text and many courts interpreting these statutes have been influenced but not necessarily bound by the FTC's interpretation of the FTC Act. So there's at least some possibility that the FTC's cautious approach may be reflected here as well rather than the more aggressive approach that the CFPB has put forth.

John Culhane:

Now, there is at least some prior history of cases upholding assertions that these state acts reach marketing, targeting protected or particularly vulnerable groups. There's not a lot of case law in this area, but that's really focused on disparate treatment, which on fairness, I think, aligns somewhat better to than disparate impact. And in that regard, there's a case in Illinois, Fairman versus Schaumburg Toyota, sort of a classic dealer upcharge case with lots of truth and lending issues that were prevalent at the time because it goes back to 1996. But in that case, there was an assertion that the discriminatory targeting of African Americans and Hispanic Americans constituted an unfair or deceptive practice under the Illinois Consumer Fraud Act. And the court denied a motion to dismiss and allowed that claim to go forward. That's probably the lead case out there. It's certainly the one that we see cited a lot. But there's not much more at this point. And certainly, no panoply of cases embracing disparate impact as part of unfairness.

John Culhane:

So what does this mean? What's the likelihood of legal challenges to the CFPB, and how might those challenges be based? My guess is not withstanding the really expansive language that we see in the exam manual and the really broad statements made by Director Chopra, we're probably going to see fairly careful and fairly measured engagement with this issue. And we're probably going to see it in the kinds of products that have already been singled out. We're not going to see, at this point, the CFPB creating new broad classes of protected groups. We're not going to see the CFPB unwind special purpose credit programs. We're not going to see the CFPB assert that everybody is entitled to the rate relief provided under the Service Members Civil Relief Act.

John Culhane:

I think we're going to see a much more measured approach. We'll see entities written up in exam reports so that that can be cited in the next supervisory highlights. Maybe if there's an egregious case involving one of the areas where the CFPB is more focused and an institution that the CFPB assesses is not going to take it on, we'll see a consent order or consent orders.

John Culhane:

But that doesn't mean that the CFPB really is acting within its authority here. Our view is that this is just a gross misinterpretation of the Dodd-Frank Act. In fact, the plain text of the Dodd-Frank Act makes clear that these terms aren't synonymous. The bureau's directive about how to proceed in section 1021 is pretty clear on that point. It's directed to act to ensure that consumers are protected from two separate categories of conduct, unfair, deceptive, or abusive acts and practices, and discrimination. Those are not equated. They're very different.

John Culhane:

And if you look at the most recent Supreme Court pronouncement about how we determine whether a statute encompasses disparate impact claims, the Inclusive Communities case, there's just no basis for comparison. The Dodd-Frank Act is not an anti-discrimination act, not an anti-discrimination statute like the Fair Housing Act. It doesn't use disparate impact language. It has no protected classes or prohibited bases. There's no legislative history suggesting that the CFPB was stood up to use its unfairness authority to stamp out discrimination in noncredit areas. There's no body of federal appellate court decisions upholding that kind of an aggressive interpretation. There's just simply nothing comparable to what we saw in the Inclusive Communities case analyzing the Fair Housing Act.

John Culhane:

I don't think that's the limit here. I think there's ample grounds for challenging what the CFPB has done as illegitimate, improper legislative rulemaking. Now, obviously, the CFPB has been very careful here. They haven't issued a policy statement or bulletin. They haven't gone that route. What they've done is they've seeded the exam manual with statements about how to look for unfair practices that would be discriminatory practices. I don't think that's enough. It is the case that this is an area where drawing lines, finding the distinctions between things that are more interpretive in nature and things that are legislative or substantive in nature and subject to notice-and-comment rulemaking is in an off-quoted phrase enshrouded in considerable fog.

John Culhane:

But there's a lot of things that the CFPB has done here that signal legislative rulemaking. The directions in the exam manual seem to be clearly amending Dodd-Frank, particularly given the press release. The provisions of the exam manual don't seem to be affording significant discretion to examiners with regard to whether practices that are unfair are discriminatory or practices that are discriminatory are unfair. The provisions of the exam manual are really drafted to lay out the bases for supervisory and/or enforcement action. And kind of the reservation to make fact-based individualized determinations when it appears in the exam manual, it seems somewhat superficial to me and more of a facade given the press release and the aggressive remarks of Director Chopra.

John Culhane:

Now, it's always a crapshoot when you sue asserting that an agency should have engaged in legislative rulemaking. But I do think there's a basis for that here. Certainly, in another context, if we were in a slightly different era, there's enough action here that this would be a rule for purposes of the Congressional Review Act. And there would be the possibility of overturning it on that basis as happened with the CFPB's approach to disparate impact in auto dealer finance. But that's not the world we're living in. That's not the situation now. That's just not going to happen.

John Culhane:

So what should you do to prepare besides wishing that you had gotten into another line of business other than consumer financial services? Well, Heather went through this in quite a bit of detail as did Ron. The activities or products that are likely to draw attention right off the bat, right out of the shoot are the marketing of non-mortgage credit products, targeted marketing, as Heather indicated and as Ron mentioned. If you're engaging in targeted marketing, you want to look at your practices there.

John Culhane:

The SBPC report devoted a lot of time and effort to attacking what is sometimes referred to as credit adjacent products, income share agreements, noncredit products offered to students. If you're involved in those kinds of products, I think you have to expect they will be the subject of fairly intense scrutiny. And the terms and conditions of noncredit products and services. Obviously, one thing that the CFPB is going to be looking at, because it's one thing they pulled out for attention, is the offering of checking accounts. Rohit Chopra seems to have convinced himself that financial institutions around the country are denying checking accounts to individuals based on their race or based on their religion.

John Culhane:

So another obvious thing to do here just at the start is to look for signs that might already be signaling discrimination to the CFPB. So overt treatment, I think that's possibly the checking account situation, saying to certain groups or certain people that you're not going to get a checking account. Actions that might be challenged as evidencing disparate treatment, look at those. Allegations of disparate impact.

John Culhane:

Now, I've referenced here looking at both protected classes and other groupings. I do not think that, at this point, the CFPB is going to be creating new classes of protected groups. I think they're going to be sticking with their traditional classes, although they will pull from the standard non-discrimination statutes. So they will pull not just from the Equal Credit Opportunity Act, they'll pull from the Fair Housing Act, they'll pull from the Americans with Disabilities Act. But you are not going to see a CFPB action claiming that a financial institution has engaged in unfair practice because it has refused to open its lobby and make checking account services available to consumers who've refused to wear masks, for example.

John Culhane:

What else should you be doing at this point? Well, Heather discussed this in detail. You've really got to drill down on your procedures for assessing risk, identifying discriminatory outcomes, and documenting those procedures. Heather mentioned, and it's clear, that you're going to have a lot of information about customer demographics, more than you probably expect. And you're going to need to look at that information. You're going to need to assess the impact of products and product terms on different demographic groups.

John Culhane:

You're going to have to start thinking about the business justification for practices outside of the credit context. And we had a couple of questions about this. Should you be engaging in testing using the BISG method? I think you have to look at your situation. But yes, I think that's coming. And I think we're going to see that as a prudent approach for institutions to consider here.

John Culhane:

I think we're right at the limit of our time. So let me stop here and let me turn it back to Alan.

Alan Kaplinsky:

Well, that just about wraps up our show for today. I want to thank our three presenters. First of all, Ron Vaske, then Heather Klein, and then John Culhane.

Alan Kaplinsky:

And I want to remind all of you what I said during my intro. And that is this is unlike some other things that the CFPB has been doing lately, this has already been done. This is a conclusion that the bureau reached and that it's memorialized in its supervision manual. And so you as a company, if you are one or if you have a client that is one that is subject to CFPB's supervision and examination, you need to prepare right now for an examination of the issues that our presenters talked about today. And we are involved in counseling many of our clients on what you need to do in the way of preparation. So if you need any help, feel free to contact any of our presenters today, or feel free to contact me.

Alan Kaplinsky:

Thank you very much for listening to our podcast today. And I hope you enjoy the rest of your day.

