Federal Trade Commission Act, Section 5 Unfair or Deceptive Acts or Practices[1]

Introduction

Advances in banking technology and changes in lending organization structure since Gramm-Leach-Bliley have permitted banks to engage in non-banking activities and given banking organizations the ability to structure financial products in increasingly complex ways and to market such products with increasingly sophisticated methods. While most banking organizations do not engage in unfair or deceptive acts or practices, the pace and complexity of these advances heighten the potential risk for consumer harm. This potential risk, coupled with identified abusive practices, warrants increased scrutiny by the FDIC and state and federal enforcement agencies. Unfair and deceptive practices are wrong, undermine consumer confidence, and present significant credit and asset quality risk undermining the financial soundness of banking organizations.

Section 5 of the Federal Trade Commission Act (FTC Act) declares that unfair or deceptive trade practices are illegal. ***See*** 15 USC §45(a) (FTC Act Section 5). The FDIC confirmed its intent to cite state nonmember banks and their institution-affiliated parties for violations of FTC Act Section 5 and will take appropriate action pursuant to its authority under Section 8 of the Federal Deposit Insurance Act (FDI Act) when unfair or deceptive trade practices are discovered.[2] FDIC enforcement action against entities other than banks will be coordinated with the Federal Trade Commission, which also has authority to take action against nonbank parties that engage in unfair or deceptive trade practices.

On March 11, 2004, the FDIC and the Federal Reserve Board (FRB) issued additional guidance regarding unfair or deceptive acts or practices prohibited by section 5 of the FTC Act.[3] The guidance explains:

- the standards used to assess whether an act or practice is unfair or deceptive;
- the interplay between the FTC Act and other consumer protection statutes; and
- guidelines for managing risks related to unfair and deceptive practices.

Following the release of the UDAP guidance, the FDIC issued a revised consultation policy which requires examiners to consult with the Regional and Washington Offices whenever an apparent unfair or deceptive act or practice is found.

Standards for Determining What is Unfair or Deceptive

The legal standards for unfairness and deception are independent of each other. Depending on the facts, a practice may be unfair, deceptive, or both.

In order to determine whether a practice is "unfair," the FDIC will consider whether the practice "causes or is likely to cause substantial injury to consumers which is not reasonably avoided by consumers themselves and not outweighed by countervailing benefits to consumers or to competition", ***see*** 15 USC §45(n). By adhering to this tenet, the FDIC will take action to address conduct that falls well below the high standards of business practice expected of banks and the parties affiliated with them.

To correct deceptive trade practices, the FDIC will take action against representations, omissions, or practices that are likely to mislead consumers acting reasonably under the circumstances, and are likely to cause such consumers harm. The FDIC will focus on material misrepresentations, i.e., those that affect choices made by consumers because such misrepresentations are most likely to cause consumers financial harm. ***See*** FTC Policy Statement on Deception (October 14, 1983).

Unfair or deceptive acts or practices that violate the FTC Act may also violate other federal or state laws. These include the Truth-in-Lending and Truth-in-Savings Acts, the Equal Credit Opportunity and Fair Housing Acts, and the Fair Debt Collection Practices Act. On the other hand, certain practices may comply fully with consumer protection or other laws and yet still violate the FTC Act. Examiners should consider both possibilities.

Unfair Acts or Practices

Standards for assessing whether an act or practice is unfair

An act or practice is unfair where it (1) causes or is likely to cause substantial injury to consumers, (2) cannot be reasonably avoided by consumers, and (3) is not outweighed by countervailing benefits to consumers or to competition. Public policy may also be considered in the analysis of whether a particular act or practice is unfair. Each of these elements is discussed further below.

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1 This section fully incorporates the examination procedures issued under DSC RD Memo 05-021: Procedures for Determining Compliance with the Prohibition on Unfair or Deceptive Acts or Practices Found in Section 5 of the FTC Act.

2 *See* FIL 57-2002

3 *See* FIL 26-2004