San Francisco Region Bankers’ Forum: Consumer Protection Hot Topics

June 25, 2012
Agenda

• Opening Comments
  • Regional Director Stan Ivie

• Fair Lending
  • Fair Lending Examination Specialist Lorrie Wang

• Unfair or Deceptive Acts or Practices (UDAP)
  • UDAP Examination Specialist Heather Smedra

• Overdraft Payment Programs
  • Compliance Examiner Karen Kopczak

• Question and Answers
Fair Lending

Lorrie Wang
Fair Lending Exam Specialist
What is fair lending?

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<th>Equal Credit Opportunity Act (Regulation B): Prohibits discrimination in any aspect of a credit transaction.</th>
<th>Fair Housing Act (HUD’s 24 CFR Part 100): Prohibits discrimination in all aspects of &quot;residential real-estate related transactions.&quot;</th>
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| • Race  
• Color  
• National origin  
• Religion  
• Sex  
• Marital status  
• Age (provided the applicant has the capacity to contract)  
• The applicant’s receipt of income derived from any public assistance program  
• The applicant’s exercise, in good faith, of any right under the Consumer Credit Protection Act | • Race  
• Color  
• National origin  
• Religion  
• Sex  
• Marital status  
• Handicap  
• Familial status (defined as children under the age of 18 living with a parent or legal custodian, pregnant women, and people securing custody of children under 18)  
• Handicap |

Law

Prohibited Bases
Trends in Examination Findings

• Disparate impact in pricing:
  • Mortgage (national origin, race)
  • Unsecured consumer lending (national origin)

• To limit pricing risk:
  • Establish clear pricing guidance
    • Rate sheets, exception policy, etc.
  • Monitor for exceptions and areas with discretion
  • Consider testing transactions to detect any differences in treatment
Trends in Examination Findings

• Disparate treatment in underwriting
  • Credit scoring models (age, gender)
  • Credit card lending (age)
  • Spousal signatures (marital status)

• To limit disparate treatment risk:
  • Consider fair lending risk during product development and when changing procedures
  • Establish underwriting guidelines
  • Provide training on guidelines
  • Monitor for adherence and areas with discretion
Trends in Examination Findings

• Discouragement in marketing
  • Credit card lending (age)
  • Advertising practices that target specific segments of the community (race, gender)

• To limit marketing risk:
  • Review marketing/advertising campaigns for compliance with applicable consumer protection laws and regulations
  • Consider the fair lending implications of the bank’s marketing program
What’s Next

• Underwriting
• Loss mitigation
• Redlining
• Steering
Redlining

• Unequal access to credit or unequal terms of credit based on prohibited basis characteristic(s) of the residents of the area in which:
  • the credit seeker resides, or
  • the residential property to be mortgaged is located

• To limit redlining risk:
  • Ensure marketing, branching, and lending activities support equal access to credit
    • Consider “gaps” that may result from branching, merger, and/or acquisition activity
  • Analyze areas with no lending activity to identify any prohibited basis characteristic(s) and potential lending opportunities
Steering

- Lending channel and product placement based on:
  - Prohibited basis (national origin, race, religion, gender, etc.) → steering
  - Placement based on applicant’s needs or other legitimate factors → okay

- Not necessary to demonstrate financial harm

- To limit steering risk:
  - Ensure all options are communicated to eligible applicants
  - Adopt guidelines for product placement based on legitimate credit factors
  - Document referral decisions
  - Ensure loan officer compensation is not tied to lending channel or product placement
What can you do?

• Understand your credit operations
  • Relationships with third parties
    • Brokers
    • Dealers
    • Servicers
    • Collectors
    • Others

• Perform periodic risk assessments
  • Proactively identify and mitigate fair lending risk
  • Frequency should be based on institution needs
What can you do?

- FFIEC Fair Lending Examination Procedures
  - List of discrimination risk indicators
  - Types of analyses that may be performed
  - Compliance Management Checklist
What can you do?

Incorporate fair lending into your compliance management system

- **Program**
  - Formalize policies, procedures, and written guidelines where possible
  - Fully investigate consumer complaints alleging discrimination

- **Audit**
  - Consider whether your institution would benefit from a fair lending review

- **Oversight**
Unfair or Deceptive Acts or Practices

Heather Smedra
UDAP Exam Specialist
What is UDAP?

- Unfair or Deceptive Acts or Practices (Section 5 of the FTC Act)

- Two separate tests:
  1. Unfair
  2. Deceptive
Unfair Acts or Practices

- The act or practice must cause or be likely to cause substantial injury to consumers.

- Consumers must not be reasonably able to avoid the injury.

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

*Note: Public policy may also be considered under the unfairness test.
Deceptive Acts or Practices

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

• The act or practice must be considered from the perspective of the reasonable consumer.

• The representation, omission, or practice must be material.
The New Abusive Standard

Under the Dodd-Frank Act, the CFPB has the power to declare an act or practice abusive if it:
(1) materially interferes with the ability of the consumer to understand a term or condition of a consumer financial product or service, or
(2) takes unreasonable advantage 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 his or her interests in selecting or using the financial product or service; or the reasonable reliance by the consumer on a covered person to act in the interests of the consumer.
UDAP Risks with Prepaid Cards

• Three areas to pay close attention to:
  1. Fees
  2. Features
  3. Marketing
Regulation E UDAP Risks

• Overdraft Payment Practices
  • Aggressive Marketing Campaigns
  • Steering

• Error Resolution Procedures
  • Requiring consumers to complete additional steps before investigating errors
Advertising UDAP Risks

- Misleading/Inaccurate Statements

- Incomplete or Omitted Information

- Consider the 4 P’s
  - Prominence
  - Presentation
  - Placement
  - Proximity
Third Party Oversight and UDAP

• A bank’s responsibility for third-party activity is the SAME as an activity handled directly by the bank.

• Effective third-party management programs incorporate:
  1. Risk Assessment
  2. Due Diligence
  3. Contract Structuring and Review
  4. Oversight
What Can You Do?

• Oversee the products and services offered by the institution
• Provide training to applicable personnel
• Conduct periodic monitoring
• Include higher risk products in scope of internal or external audits
• Review consumer complaints and questions
Overdraft Payment Programs

Karen Kopczak
Compliance Examiner
What is an Overdraft?

- Customer initiates withdrawal activity that is not covered by their available funds on deposits in that account
  - Check or other negotiable instrument
  - ACH – recurring or one-time
  - ATM
  - Debit card – recurring or one-time POS transaction
What is an Overdraft Program?

• Types of programs:
  • Automatic transfer of customer funds from another deposit account
  • Automatic transfer from a customer line of credit
  • Bank covers overdraft from the bank’s own funds.
    • Ad hoc manual decisions made by bank staff, or
    • Automated credit decision systems (often provided by a third-party vendor)
Coverage of Rules and Guidance

• Distinction between program types is critical

• Guidance & Rules that apply to all three scenarios:
  • 2005 Joint Guidance (FIL-11-2005)
  • Regulation DD requirements (Section 230.11(c))

• Rules that apply only to ad hoc and automated programs:
  • Regulation E overdraft requirements
    • Only for ATM or one-time POS transactions
  • Regulation DD requirements (Section 230.11(a))

• Guidance focused on automated programs:
  • FDIC’s Overdraft Payment Program Guidance (FIL-81-2010)
Joint Agency Guidance
Overdraft Protection Programs

• FIL-11-2005, dated 2/18/2005
• Coverage – all overdraft programs
• Discusses:
  • Potential concerns of regulatory agencies
  • Risk management considerations
  • Compliance with all federal and state laws
  • Best practices
Final FDIC Overdraft Supervisory Guidance

• FIL-81-2010, dated 11/24/2010
• Reaffirms existing guidance
• Focuses on risks posed by *automated* overdraft payment and excessive use
Highlights of Supervisory Guidance

- Monitor Accounts
- Meaningful and Effective Follow-Up
- Fee Limits
- Neutral Transaction Processing Order
- Opt-In Requirement
  - Opt-out recommended for transactions not covered by Regulation E
Applicable Laws and Regulations

- Truth in Savings & Regulation DD
- Truth in Lending & Regulation Z
- Electronic Fund Transfer Act & Regulation E
- Section 5 of the FTC Act (UDAP) & Regulation AA
- Equal Credit Opportunity Act & Regulation B
- Community Reinvestment Act
- Privacy
Question and Answers

Press *1

or email

SFConsumerProtection@fdic.gov
Fair Lending References

• Fair Lending Examination Procedures
  

• Policy Statement on Discrimination in Lending
  

• DOJ Fair Lending Cases
  
  http://www.justice.gov/crt/about/hce/caselist.php#lending

• FDIC Teleconference on Conducting a Fair Lending Risk Assessment
  
UDAP References

• UDAP Financial Institution Letters

• FDIC’s UDAP Examination Procedures

• FTC Websites
  http://www.ftc.gov/
  http://www.ftc.gov/bcp/policystmt/ad-unfair.htm
  http://www.ftc.gov/bcp/policystmt/ad-decept.htm
UDAP References (cont.)

• FTC’s Dot Com Disclosures: Information About Online Advertising

• FDIC Supervisory Insight Articles

  Chasing the Asterisk: A Field Guide to Caveats, Exceptions, Material Misrepresentations, and Other Unfair or Deceptive Acts or Practices (Winter 2006)
  http://www.fdic.gov/regulations/examinations/supervisory/insights/siwin06/article02_chasing.html
Overdraft Program References

• Financial Institution Letters
- Overdraft Protection Programs Joint Agency Guidance (FIL-11-2005)
- Overdraft Payment Programs and Consumer Protection: Final Overdraft Payment Supervisory Guidance (FIL-81-2010)

• FDIC Overdraft Payment Program Supervisory Guidance FAQs

• FDIC’s Overdraft Payment Programs Exam Procedures
## Contact Information

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