

Consumer Financial Protection Law and Regulation

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Preface

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Since the 2008 financial crisis sparked the creation of the Consumer Financial Protection Bureau via the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, much has changed in the world of consumer finance. Prior to the Bureau's creation, the regulatory framework for consumer financial products and services was both fragmented and duplicative; at least seven Federal agencies with competing goals were charged with protecting consumers, but jurisdictional limitations and concerns with financial institutions' safety and soundness hindered these agencies' ability to detect, prevent, and enforce violations of the Federal consumer financial protection laws. All that changed on July 21, 2011, the date that Dodd-Frank transferred to the Bureau its authorities.

In the shifted regulatory landscape, whether the Bureau is exercising its rulemaking, supervisory, or enforcement authority, it regulates almost all consumer financial products and services markets. It touches an estimated 70,000 U.S. businesses. While the Bureau implements and enforces longstanding consumer credit laws, such as the Truth in Lending Act, the Fair Debt Collection Practices Act, and the Fair Credit Reporting Act, among others, the agency also has new regulatory tools at its disposal, such as the ability to identify and prohibit business practices it believes to be unfair, deceptive, or abusive. It has the on-site supervision and examination authority of the prudential banking regulators. Also, the Bureau wields powerful enforcement powers. It can issue administrative subpoenas on mere suspicion of wrongdoing. The Bureau can file federal court lawsuits on its own accord, and only a very few statutes of limitations and exceptions to Bureau authority circumscribe its activities. Free from Congressional appropriations and staffed by zealous professionals with extensive consumer protection, banking, economics, and law enforcement backgrounds, the Consumer Financial Protection Bureau has become a juggernaut in the field of consumer finance.

Consumer Financial Protection Law and Regulation serves as a guide to counsel whose clients are subject to the Bureau's sweeping jurisdiction and potent toolkit. It is designed to provide practical insight for navigating the Bureau's mandated functions and authorities, its rulemaking, examination, and enforcement processes, and the substantive laws it implements and enforces.

For generalist lawyers working in banks, non-bank lending, collections, credit reporting, payments, or the many firms that serve and support consumer finance, Part One will aid in identifying relevant agencies, laws, and considerations that affect your companies. For seasoned

banking, white-collar, and regulatory lawyers, Part Two provides the unique process and practice insights necessary to effectively advise clients in their interactions with consumer finance's new regulator, the Consumer Financial Protection Bureau. Investors, lawyers, executives, and compliance officers can use Part Three as a tool for identifying risks to business lines, which will aid in determining when to invest in compliance management systems or where new opportunities may lie.

As a former Acting Deputy Director of Enforcement at the Bureau who transferred from a prudential regulator on the Bureau's first day and as a law professor and former Trial Attorney in the Executive Office of U.S. Trustees, we draw upon our experience to highlight the inner working of government and administrative litigation. We hope to provide you a comprehensive resource for representing entities the Bureau regulates.

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I. INTRODUCTION

“Supervision” and “supervisory activity” mean the Consumer Financial Protection Bureau’s (CFPB or Bureau) exercise, or intended exercise, of supervisory authority, including by initiating or undertaking an examination, or requiring a report, of a covered person pursuant to 12 U.S.C. §5514. Supervision may involve requests for information or records, on-site or off-site examinations, or some combination of these activities. While the specifics of an examination may vary by market and by firm, the following discussion applies generally to the supervision process. Typically, Bureau officials begin an on-site examination by contacting the firm for an initial conference with management and often by requesting records and information. Based on these discussions and an initial review of the information received, examiners determine the scope of an on-site examination and then coordinate with the firm to initiate the on-site portion of the examination.

While on-site, examiners hold discussions with management about the company’s processes and procedures; review documents, records, and accounts for compliance; and evaluate the firm’s compliance management systems. The Bureau’s examinations involve issuing confidential supervisory letters, examination reports, and compliance ratings. In some cases, supervision activity can lead to Matters Requiring Attention (MRAs), corrective actions, Memorandums of Understanding (MOUs), or a Potential Action and Request for Response (PARR) letter. This chapter explains these supervisory tools. In addition, it covers how the CFPB selects subjects for supervision, the examination process and procedure, and confidential supervisory information.

II. SELECTION OF SUPERVISED ENTITIES

The Bureau has supervisory authority over banks, thrifts, and credit unions with assets over \$10 billion, as well as their affiliates (for

convenience, “banks”).¹ In addition, it has supervisory authority over nonbank mortgage originators and servicers,² payday lenders,³ and private student lenders of all sizes.⁴

The Bureau supervises the larger participants of other consumer financial markets as defined by Bureau rules. To date, this includes larger participants in the following markets: consumer reporting, consumer debt collection, student loan servicing, international money transfer, and automobile financing. The Consumer Financial Protection Act (CFPA) Section 1024 requires that the Bureau consult with the Federal Trade Commission prior to issuing larger participant rules,⁵ which is yet another method by which the CFPA mandates cooperation between federal regulators of the financial services markets.

A. Very Large Banks and Thrifts

The CFPA Section 1025 coined the statutory term “very large banks.” It established an arbitrary threshold of \$10 billion of assets to identify the financial institutions that fall under CFPB supervision.⁶ Notably, the statute does not limit the CFPB’s authority to depository institutions that have a federal charter. State banks, thrifts, and credit unions that operate under a state charter and have Federal Deposit Insurance qualify for supervision under Section 1025.⁷

The \$10 billion asset threshold does not specify the portion of assets that derive from consumer finance activities. Nor does the threshold differentiate between consolidated assets and domestic assets. As a result, several private banks for wealth management, principally commercial banks, and predominately foreign banks fall under CFPB supervision.

The prudential regulators retain authority for examining Very Large institutions for compliance with certain other laws related to consumer financial protection, including the Community Reinvestment Act, the Fair Housing Act, and Section 5 of the Federal Trade Commission Act. Table 1 below identifies the federal consumer financial laws the Dodd-Frank Act

¹ 12 U.S.C. §5515(a). For purposes of this chapter, depository institutions like banks, savings associations (i.e., “thrifts”), and credit unions may be referred to as “banks” where doing so will not cause inaccuracies. Non-depository institutions are generally referred to as “nonbanks,” both in this publication and within CFPB materials and parlance.

² *Id.* §5514(a)(1)(A).

³ *Id.* §5514(a)(1)(E).

⁴ *Id.* §5514(a)(1)(D).

⁵ *Id.* §5514(a)(2).

⁶ 12 U.S.C. §5515(a).

⁷ *Id.* §5515(a).

transferred to the CFPB, for which the agency has examination responsibility, and laws for which the prudential regulators retain examination responsibility.

The CFPA reserves to prudential regulators supervising and enforcement authority over banks that do not meet the \$10 billion threshold.⁸ The CFPA Section 1026 explicitly provides, with respect to those “Other” banks that are not “Very Large,” that the bank’s prudential regulator has “the exclusive authority (relative to the Bureau) to enforce [the consumer financial protection] laws.”⁹ As a result, the Bureau may not conduct enforcement actions against Other banks. The Bureau has slightly more access to small, medium, and large banks through its supervision powers. Section 1026 provides that the Bureau may include CFPB examiners on a sample of prudential regulator Other bank examinations to assess compliance with the requirements of federal consumer financial law.¹⁰ When a sample exam like this occurs, the Bureau examiner is entitled to copies of all examination materials and to be involved in the entire examination process. The prudential regulator must consider the Bureau examiner’s input concerning the scope and conduct of the examination, as well as the contents of the exam report, matters requiring attention, and examination ratings.¹¹ This manner of inter-agency coordination is consistent with the vision of the Bureau as an expert agency in consumer finance and creating regulatory consistency.

The asset information that informs the Bureau’s identification of supervised banks appears on publicly available bank or thrift “call reports.” The Federal Financial Institutions Examination Council (FFIEC) administers the call report process by which insured depository institutions report quarterly their critical financial health information, including asset information. The FFIEC publishes the reports in unredacted form.¹² The public can find call reports for individual institutions or download the reports in bulk. Because bank assets fluctuate over time, depository institutions may move on or off the CFPB’s list of supervised institutions.

Because Other banks are exempt from CFPB authority, the potential for a second consecutive quarterly call report that reports less than \$10

⁸ *Id.* §5516(c-d). The prudential regulators are the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the National Credit Union Administration.

⁹ *Id.* §5516(d).

¹⁰ *Id.* §5516(c).

¹¹ 12 U.S.C. §5516(c)(2).

¹² The Federal Financial Institutions Examination Council posts quarterly call reports and Uniform Performance Reports, which compare depositories to their similarly-sized peers on its website; records are posted for several years. *See* <https://cdr.ffiec.gov/public/>.

billion in assets can cause a Bureau enforcement matter to accelerate. In the case of Flagstar Bank, F.S.B.,¹³ the prospect of the Bureau losing authority over the bank compressed an investigation and settlement negotiation period considerably. Flagstar consented in a CFPB order to provide redress of \$27.5 million to approximately 6,500 consumers whose loans were being serviced by Flagstar and who were subject to its allegedly unlawful practices.¹⁴ The CFPB filed the administrative order one day before Flagstar's quarter ended. For the quarter ended September 30, 2014, Flagstar reported its total assets (line RCON217012) as having dropped from \$9.8 billion the previous quarter to \$9.5 billion. Having spent two consecutive quarters below the \$10 billion asset threshold thus moved the entity beyond the Bureau's enforcement authority a day after the consent order issued.

The CFPA does not require prudential regulators to act in instances where the Bureau identifies law violations. When the Bureau has reason to believe that banks with assets below the \$10 billion threshold have engaged in a material violation of a federal consumer financial law, the Bureau must "notify the prudential regulator in writing and recommend appropriate action to respond."¹⁵ In return, the CFPA requires prudential regulators, such as the Comptroller of the Currency, to respond in writing to a Bureau notification under Section 1026 within 60 days.¹⁶

In early 2015, the Offices of Inspector General (OIGs) for the prudential regulators conducted a joint review of the coordination between the Consumer Financial Protection Bureau and the prudential regulators with respect to performing supervisory activities and avoiding duplication of regulatory oversight responsibilities on matters related to federal consumer financial laws and regulations.¹⁷ The OIGs concluded that the CFPB and the prudential regulators were generally coordinating their regulatory oversight activities for federal consumer financial laws in a manner consistent with the provisions of a memorandum of understanding governing coordination activities and with the Dodd-Frank Wall Street Reform and Consumer Protection Act. The OIGs, however, were unable to

¹³ Consent Order, *In re* Flagstar Bank, F.S.B., 2014-CFPB-0014 (2014).

¹⁴ *Id.*

¹⁵ 12 U.S.C. §5516(d)(2)(A).

¹⁶ *Id.* §5516(d)(2)(B).

¹⁷ Offices of Inspector General for the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System and the Consumer Financial Protection Bureau, the Office of the Comptroller of the Currency, and the National Credit Union Administration, *Coordination of Responsibilities Among the Consumer Financial Protection Bureau and the Prudential Regulators—Limited Scope Review*, Board-CFPB OIG Report No. 2015-SR-X-009 (June 1, 2015).

verify that the CFPB had been consistently complying with the requirements of Section 1026(d) of the Dodd-Frank Act.¹⁸ After the OIG’s findings, the Bureau adopted the Civil Referrals Incoming and Outgoing policy. The policy outlines an escalation and approval process that precedes a written notification and a tracking process for written notifications and recommendations.¹⁹

B. Supervisory Authority over Nonbanks

Under 12 U.S.C. 5514, Congress mandated that the Bureau have supervisory authority over nonbank covered persons of any size offering or providing three enumerated types of consumer financial products or services: (1) origination, brokerage, or servicing of residential mortgage loans secured by real estate;²⁰ (2) offering or providing to a consumer any private education loan;²¹ or (3) offering or providing to a consumer a payday loan.²² This section also provides that the Bureau, through notice and comment rulemaking, can extend supervision authority over entities that the rule identifies as a larger participant of a market for consumer financial products or services.²³

The final method by which the Bureau can exercise supervisory authority over a covered person is by order. Section 5514(a)(1)(C) provides that the Bureau can place an entity under supervision by order after notice to the covered person and a reasonable opportunity to respond.²⁴ The statute sets forth a process that is based on complaints collected under the CFPA Section 5493(b)(3), or information from other sources, that “such covered person is engaging, or has engaged, in conduct that poses risks to consumers with regard to the offering or provision of consumer financial products or services.”²⁵ The Bureau has yet to issue an order that appears to derive exclusively from this statutory process; however, the Bureau typically requires in its enforcement action consent orders with non-supervised entities that the entity fall under the CFPB’s supervision authority for a

¹⁸ *Id.*

¹⁹ Office of the Inspector General for the Board of Governors of the Federal Reserve System and the Consumer Financial Protection Bureau, Letter re OIG Report No. 2015-SR-C-010: The CFPB Can Enhance Its Process for Notifying Prudential Regulators of Potential Material Violations 3 (June 29, 2015).

²⁰ 12 U.S.C. §5514(a)(1)(A).

²¹ *Id.* §5514(a)(1)(D).

²² *Id.* §5514(a)(1)(E).

²³ *Id.* §5514(a)(1)(B).

²⁴ *Id.* §5514(a)(1)(C).

²⁵ *Id.*

proscribed time. The provision appears as follows in numerous consent orders:

Defendants agree to be subject to the Bureau’s supervisory authority under 12 U.S.C. §5514 for 3 years from the effective date. Consistent with 2 C.F.R. §1091.111, Defendants shall not petition for termination of supervision under 12 C.F.R. §1091.113.”²⁶

The CFPB does not have a process to terminate an enforcement investigation in favor of the investigation subject consenting to supervisory authority.

III. NONDEPOSITORY LARGER PARTICIPANTS

The CFPA authorizes the Bureau to supervise larger participants of markets for consumer financial products or services, as defined by rule.²⁷ Congress required the Bureau to issue an initial “larger participant” rule by July 21, 2012.²⁸ The Bureau has issued five larger participant rules thus far.²⁹ In general, the rules set thresholds based on a company’s gross revenue to determine which market participants are large enough to fall within the CFPB’s supervision.³⁰ To date, the CFPB has issued larger participant rules, available at 12 CFR Part 1090, with respect to the following nonbank markets:

²⁶ *E.g.*, CFPB v. Nat’l Corrective Grp., Case 1:15-cv-00899-RDB, Doc. No. 6, at 13 (D. Md. Mar. 30, 2015).

²⁷ 12 U.S.C. §§5514(a)(1)(B), (a)(2).

²⁸ *Id.* §5514(a)(2) (“The Bureau shall consult with the Federal Trade Commission prior to issuing a rule, in accordance with paragraph (1)(B), to define covered persons subject to [Section 1024–supervision of nondepository covered persons]. The Bureau shall issue its final rule not later than 1 year after the designated transfer date [July 21, 2011].” *See also* 12 U.S.C. §§5514, 5512(b)(1), which, among other things, authorize the Bureau to prescribe rules to facilitate the supervision of covered persons and grant the Bureau the authority to prescribe rules as may be necessary and appropriate to enable the Bureau to administer and carry out the purposes and objectives of federal consumer financial law and to prevent evasions of such law.

²⁹ *See* 12 C.F.R. Pt. 1090.

³⁰ Gross receipts for purposes of the larger participant rules are calculated by fiscal year. The term “completed fiscal year” means a tax year, including any fiscal year, calendar year, or short tax year. 12 C.F.R. §1090.101.

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- debt collection,³¹
- consumer reporting,³²
- student loan servicing,³³
- international money transfers,³⁴ and
- automobile financing.³⁵

A difficult aspect of the rules relates to the computation of activity levels for purposes of the CFPA Section 1024.³⁶ The CFPA provides that the activities of affiliated companies (other than insured depository institutions or insured credit unions) shall be aggregated.³⁷ But the CFPA does not define the term “affiliated company;” it only defines “affiliate.”³⁸ To eliminate confusion, the CFPB defined the term “affiliated company” through rulemaking. Thus, the term “affiliated company” of a person means any company³⁹ (other than an insured depository institution or insured credit union) that controls, is controlled by, or is under common control with the person.⁴⁰

Prior to undertaking supervisory activity of a market participant, the Bureau notifies the company in writing.⁴¹ Entities that disagree with the

³¹ Defining Larger Participants of the Consumer Debt Collection Market, 77 Fed. Reg. 65775 (Oct. 31, 2012); 12 C.F.R. §1090.105.

³² Defining Larger Participants of the Consumer Reporting Market, 77 Fed. Reg. 42873 (July 20, 2012); 12 C.F.R. §1090.104.

³³ Defining Larger Participants of the Student Loan Servicing Market, 78 Fed. Reg. 73383 (Dec. 6, 2013); 12 C.F.R. §1090.106.

³⁴ Defining Larger Participants of the International Money Transfer Market, 79 Fed. Reg. 56631 (Sept. 23, 2014); 12 C.F.R. §1090.107.

³⁵ Defining Larger Participants of the Automobile Financing Market and Defining Certain Automobile Leasing Activity as a Financial Product or Service, 80 Fed. Reg. 37495 (June 30, 2015); 12 C.F.R. §1090.108.

³⁶ 12 U.S.C. §5514(a)(1).

³⁷ *Id.* §5514(a)(3)(B).

³⁸ *Id.* §5481(1).

³⁹ For purposes of the definition of “affiliated company,” the Rule defines the term “company” to mean any corporation, limited liability company, business trust, general or limited partnership, proprietorship, cooperative, association, or similar organization. The definition, which encompasses “similar organization[s]” to those expressly enumerated, covers professional corporations and professional limited liability companies, as well as other forms of organization comparable to those on the enumerated list that exist or may arise. Defining Larger Participants of the Consumer Reporting Market, 77 Fed. Reg. 42873, 42877 (July 20, 2012).

⁴⁰ *Id.*

⁴¹ *Id.* at 42878.

Bureau’s assessment that their activities or gross receipts meet the Bureau’s test for falling under supervision can challenge their status as a larger participant under Rule 1090.103.⁴² Grounds for challenging the determination include: (1) the entity’s annual receipts should not be aggregated with those of certain other companies because they are not under common control with the entity doing business in the regulated market, (2) the Bureau incorrectly calculated annual receipts, or (3) the company does not participate in the market subject to the larger participant rule.⁴³

A person qualifying as a larger participant remains a larger participant until two years from the first day of the tax year in which the person last met the applicable threshold to be defined as a larger participant.⁴⁴ The Bureau wrote this two-year tail to have sufficient time to undertake and complete supervisory activities, including any necessary follow-up examinations relating to a larger participant. According to the Bureau, less than two years would not be adequate to achieve this goal.⁴⁵ The two-year tail also recognizes that the demarcation of which (or when) market participants are “larger” is imprecise.⁴⁶

The Bureau uses various data sources, including public data, to identify which nonbank covered persons appear to qualify as larger participants. Such data includes SEC filings, public shareholder information, industry surveys, or data obtained through proprietary sources. In some instances, if sufficient information is not available to the Bureau to assess a person’s larger-participant status, the Bureau may, as discussed below, request information to facilitate such an assessment.

A. Challenging Assessments as a Larger Participant

When a firm receives notice from the Bureau that it is deemed a larger market participant and that the Bureau intends to initiate a supervisory examination, the company has 45 days to dispute its larger participant status.⁴⁷ The larger participant rules set forth a procedure for challenging the designation as a larger participant. The firm may begin the challenge by providing to the Bureau an affidavit setting forth an explanation of the basis for the person’s assertion that it does not meet the

⁴² 12 C.F.R. §1090.103.

⁴³ *See*, 1090.104.

⁴⁴ *Id.* §1090.103.

⁴⁵ 77 Fed. Reg. at 42877.

⁴⁶ *Id.* at 42881 (“For example, a firm with annual receipts falling below the threshold for the consumer reporting market may still be a relatively large participant of the market, especially if its annual receipts, calculated using the procedures specified in the final rule, were above the threshold within the previous two years.”)

⁴⁷ 12 C.F.R. §1090.103(a).

definition of larger participant. The response should include copies of any records, documents, or other information that supports the assertion. Failing to submit necessary records waives the right to rely on that information when prosecuting the dispute.⁴⁸ The Assistant Director may, however, require that a person provide to the Bureau such records, documents, and information as he or she may deem appropriate for assisting assessments of the entity's status as a larger participant.⁴⁹

The appeal is informal and conducted via email. This is appropriate under the Administrative Procedure Act (APA) and principles of due process because supervision does not impose any penalty on an entity, does not deprive it of any property, and does not restrict its ability to engage in a viable business. Thus, a decision to initiate supervision does not implicate an interest protected by the Fifth Amendment. The appeal procedures here are comparable to those offered by the Federal Deposit Insurance Corporation and other agencies.⁵⁰ Due process does not necessitate a hearing in every instance, and the evidence involved in assessing a larger participant's annual receipts from consumer reporting is not of the kind that requires oral presentation.⁵¹

B. Markets Selected to Supervise

The Bureau has wide discretion in choosing markets for which to define larger participants. The CFPA does not mandate particular tests or thresholds prior to defining larger participants in a given market.⁵² For example, the Bureau chose to first define larger participants in consumer reporting, noting:

[c]hoosing consumer reporting as the subject of this rule is reasonable because consumer reporting, as defined in the rule, is an important activity that affects hundreds of millions of consumers and because supervision of larger participants of this market will be beneficial to consumers and markets and will further the Bureau's mission to ensure consumers' access to fair, transparent, and competitive markets for consumer financial products and services.⁵³

⁴⁸ *Id.* §1090.103(b).

⁴⁹ *Id.* §1090.103(d). The Bureau would assert that it has this authority under 12 U.S.C. §5514 even absent a regulation.

⁵⁰ *See, e.g., Karpova v. Snow*, 497 F.3d 262 (2d Cir. 2007); *FDIC v. Coushatta*, 930 F.2d 1122 (5th Cir. 1991).

⁵¹ *See Mathews v. Eldridge*, 424 U.S. 319, 344–45 (1976).

⁵² *Cf.* 12 U.S.C. §5514(b)(1) (authorizing discretion without specific requirements).

⁵³ *Defining Larger Participants of the Consumer Reporting Market*, 77 Fed. Reg. 42873, 42877 (July 20, 2012).

The definitions in federal statutes and prior implementing regulations do not necessarily equate to the definitions in the CFPB’s larger participant rules. In particular, the definition of “consumer reporting” in the larger participant rule does not mirror the scope of the Fair Credit Reporting Act’s (FCRA) definitions of “consumer report” and “consumer reporting agency.”⁵⁴ First, the credit reporting larger participant rule excludes information to be used solely in a decision for employment, government licensing, or residential leasing or tenancy.⁵⁵ In other respects, the definition has broader coverage than in the FCRA. For example, “consumer report information or other account information” in the CFPB rule could include information beyond what would be considered a “consumer report” under the FCRA, which is limited to consumer information that bears on a consumer’s credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living and is used or collected for credit or other permissible purposes.⁵⁶ Similarly, certain entities that are not “consumer reporting agencies” within the meaning of the FCRA—such as certain analyzers of consumer report information—may be larger participants of the consumer reporting market delineated by the final rule.⁵⁷

C. Risk-Based Supervisory Authority

The Bureau can also assert supervisory authority under the CFPA Section 1024 based on a risk determination.⁵⁸ The Bureau can supervise any nonbank covered person that the Bureau “has reasonable cause to determine, by order, after notice . . . and a reasonable opportunity . . . to respond . . . is engaging, or has engaged, in conduct that poses risks to consumers with regard to the offering or provision of consumer financial products or services.”⁵⁹

The Bureau must use consumer complaints as a basis for its reasonable cause determinations,⁶⁰ or it may rely on information collected from other sources. This provision allows the agency to supervise entities that have attempted to evade larger participant determinations that could potentially occur by a market participant’s structuring business activities through separate entities.⁶¹ Under the final rule, a notice of reasonable

⁵⁴ 15 U.S.C. §1681a(f).

⁵⁵ 12 C.F.R. §1090.104(a)(4)(v).

⁵⁶ 15 U.S.C. §1681a(d)(1).

⁵⁷ 77 Fed. Reg. at 42883–84.

⁵⁸ 12 U.S.C. §5514(a)(1)(C).

⁵⁹ *Id.*

⁶⁰ The Bureau must collect consumer complaints under 12 U.S.C. §5493(b)(3).

⁶¹ *See* 12 U.S.C. §5481(1) (definition of “affiliate”).

cause does not constitute a notice of charges for any alleged violation of federal consumer financial law or other law.⁶² The proceedings under the final rule are informal and do not constitute an adjudication proceeding with a hearing on the record under the APA.⁶³

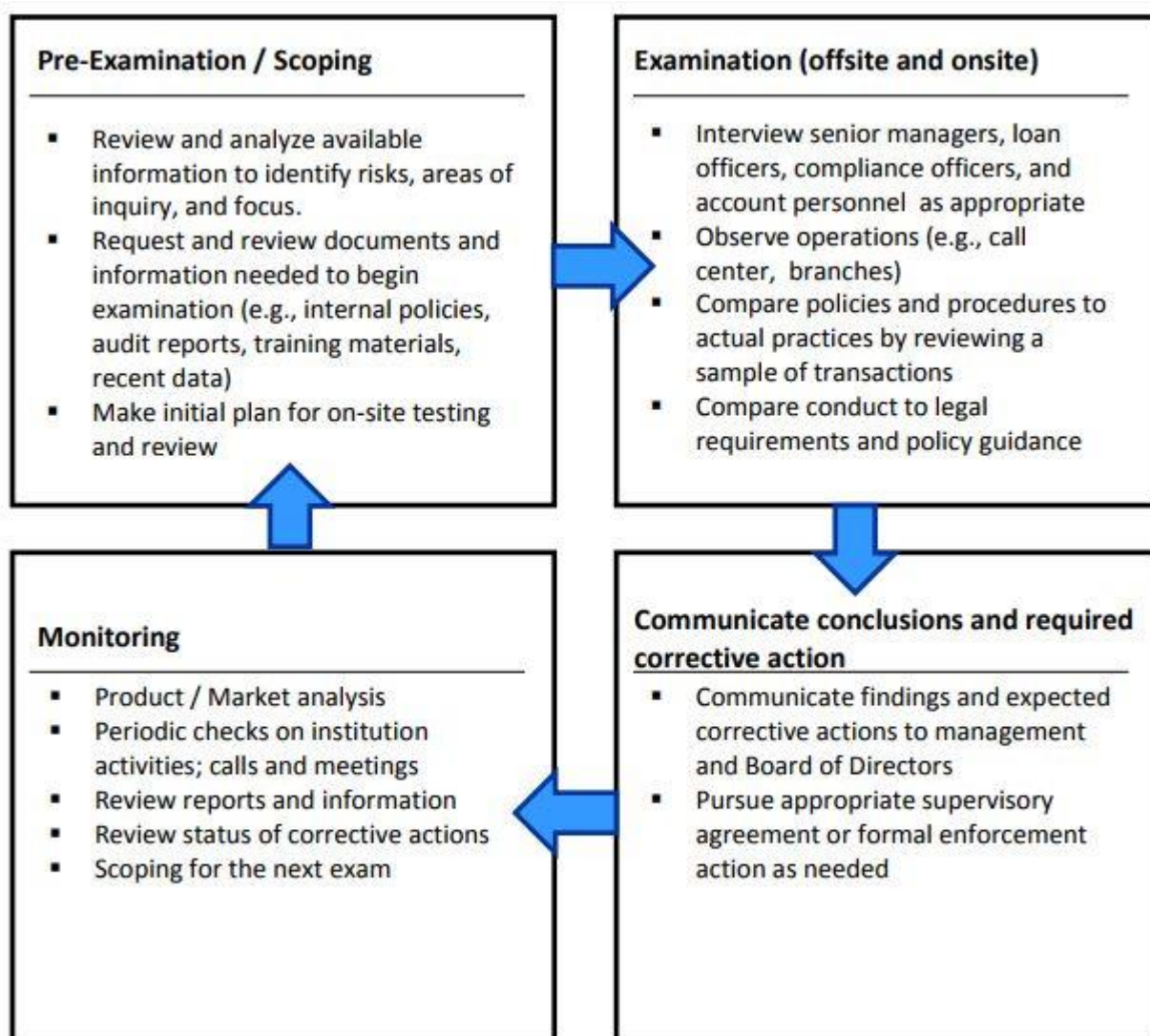
IV. SUPERVISION PROCESS AND PROCEDURE

The CFPB's Offices of Supervision Examinations and Supervision Policy are housed within the Division of Supervision, Enforcement, and Fair Lending (SEFL). These two offices develop and administer the CFPB's nationwide supervisory program for depository and non-depository financial institutions. In conducting its supervisory activities, the CFPB focuses on maintaining consistency across markets, industries, charters, and regions, as well as on ensuring efficient and effective examinations and supervisory work. The CFPB follows a risk-based approach to examinations by prioritizing consumer products and markets that pose significant risks to consumers.

As shown in the graphic below, CFPB supervision operates as a continuous cycle.

⁶² Procedural Rule To Establish Supervisory Authority Over Certain Nonbank Covered Persons, 78 Fed. Reg. 40351, 40353 (July 3, 2013).

⁶³ See 5 U.S.C. §§554, 556, 557 (setting forth APA procedures for adjudications determined on the record after opportunity for an agency hearing).



CFPB, SUPERVISION AND EXAMINATION MANUAL 10 (Mar. 2017).

A. Supervision and Examination Manuals

The Bureau has published several versions of its general examination manual, plus many subject-matter updates, describing the Bureau's supervisory approach and processes, as well as substantive legal areas subject to examination. The most recent version of the full Supervision and Examination Manual issued in August 2017. This manual is available on the Bureau's website.⁶⁴ The examination manual outlines

⁶⁴ CFPB, SUPERVISION AND EXAMINATION MANUAL 907 (Mar. 2017), <https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201708>

legal requirements under the various laws applicable to the relevant products and services and guides examiners on information they should evaluate regarding compliance with those laws. The Bureau regularly supplements its manuals to include procedures specifically addressed to certain markets or new regulations.

B. Chart of Supervision and Examination Manual Topics

The Supervision and Examination Manual is 1551 digital pages and covers examination processes, substantive regulatory requirements, and specific procedures and forms for examination. It functions first as a guide to the agency’s examiners and helps the Bureau fulfill its statutory mandate to consistently enforce federal consumer financial law. The Supervision and Examination Manual is made available to supervised entities so those entities can self-identify issues and possess some transparency into the examination process.

Each chapter begins at the number 1. The table below provides a comprehensive table of contents for the Supervision and Examination Manual.

Table 5.1: CFPB’s Supervision and Examination Manual topics

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The Bureau asserts that once an entity is subject to supervision, all of its activities are open to examination. The Dodd-Frank Act authorizes the Bureau to supervise “covered person[s]” described in the CFPB Section 1002.⁶⁵ By granting the Bureau supervisory authority over such “covered persons,” as opposed to particular activities in which they engage, the Bureau’s supervisory authority extends to the covered person’s other activities that involve other consumer financial products or services or are

⁶⁵ 12 U.S.C. §5514(a)(1)(A)–(E).

subject to federal consumer financial law.⁶⁶ Specifically, the CFPB directs the Bureau to require reports and conduct examinations on covered persons to (1) assess compliance with the requirements of federal consumer financial law, (2) obtain information about the activities and compliance systems or procedures of such persons, and (3) detect and assess risks to consumers and markets for consumer financial products and services.⁶⁷ Accordingly, if an entity is subject to the Bureau’s supervisory authority, the Bureau may examine the entire entity and not just the activities that initially rendered the entity subject to Bureau supervision.

To date, no Bureau enforcement action or supervisory reprimand (as reported in Supervisory Highlights) has touched upon market conduct outside the CFPB’s purview. The Bureau’s approach appears to facilitate the practical purpose of preventing entities from withholding or redacting information about non-covered products or services. It is unlikely that the Bureau would make use of the ancillary information for purposes other than required to assess violations under its authority; rather, this approach avoids unnecessary delay and expense on the part of supervised entities for document review and redaction exercises.

C. Selection of Supervised Entities

Nonbank markets add well over 15,000 unique institutions to the CFPB’s portfolio of about 110 very large depository institutions that are subject to supervision.⁶⁸ When considering whether and how to supervise particular nonbanks, the Bureau considers several factors, including the institution’s volume of business, types of products or services, and the extent of state or federal oversight.

⁶⁶ Defining Larger Participants of the Consumer Reporting Market, 77 Fed. Reg. 42873, 42880 (July 20, 2012) (“By granting the Bureau supervisory authority over such ‘covered persons,’ as opposed to over particular activities in which they engage, the Dodd-Frank Act establishes that the Bureau’s supervisory authority is not limited to the products or services that qualified a person for supervision, but also includes other activities of such a person that involve other consumer financial products or services or are subject to Federal consumer financial law.”) (citing 12 U.S.C. §5514(b)(1) (“The Bureau shall require reports and conduct examinations on a periodic basis of ‘persons’ described in subsection (a)(1). . . .”)) (emphasis added); 12 U.S.C. §5514(a)(1) (“[T]his section shall apply to any covered ‘person’ who. . . .”) (emphasis added).

⁶⁷ 12 U.S.C. §5514(a)(1).

⁶⁸ Steven Antonakes, Prepared Remarks to the Consumer Bankers Association (Mar. 25, 2015) (At the time of his presentation, Antonakes was CFPB Deputy Director and Associate Director for Supervision, Enforcement, and Fair Lending).

Visiting all the banks and nonbanks under Bureau jurisdiction on a regular schedule, as other federal agencies have in the past, would be impractical given their number, size, and complexity as well as the relatively small size of the examination force. More importantly, adopting a fixed-schedule approach would fail consumers by focusing precious resources on potentially less severe problems, when larger, more pressing, consumer protection issues awaited attention.

The Bureau has devised a system of risk-based prioritization. This prioritization includes an assessment of potential consumer risk along with factors such as product market size; the entity's market share; the potential for consumer harm; and field and market intelligence that includes other factors such as management quality, prior regulatory history, and consumer complaints.⁶⁹ Practically, under the CFPB's prioritization approach, institutions with strong compliance management systems are less likely to be selected for supervision. The below graphic depicts the four considerations in the risk-based prioritization. Note that risk evaluations focus on risks to consumers rather than risks to institutions.⁷⁰



The Bureau conducts examinations by product line rather than by an institution-centric approach. Even for the few massive institutions that have continuous supervision, the schedule upon which examiners base their examination scopes focuses on institutional product lines. For example, a large bank might have several product lines—auto lending, credit cards, deposit accounts, international money transfers, mortgage origination, and mortgage servicing—while a nonbank mortgage company might have just two—mortgage origination and servicing. The Bureau refers to each distinct product line at an institution as an Institutional Product Line (IPL).⁷¹

⁶⁹ Richard Cordray, Written Testimony of CFPB Director Richard Cordray Before the Senate Committee on Banking, Housing and Urban Affairs (Sept. 9, 2014).

⁷⁰ Antonakes presentation.

⁷¹ *Id.*

The Bureau compares IPLs across institutions, charters, or licenses to evaluate each product line based on the potential for consumer harm related to a market, the size of the product market, the supervised entity's market share, and risks inherent to the supervised entity's operations and offerings of financial consumer products within that market.⁷² Thus, the first part of the prioritization assesses risks to the consumer at two levels: the market level and then the institution level.

At the market-wide level, the Bureau assesses the risk to the consumer from the products and practices being followed in a market. Some markets have stronger incentives to serve consumers than others do. The Bureau has identified higher-risk markets to include:

- Mortgage servicing;
- Third-party debt collection;
- Credit reporting; and
- Payment processing.

The CFPB's present view is that these market structures are higher-risk because consumers cannot choose their provider of financial products or services or the market's central focus reflects a financial relationship between two businesses. Consumer interests may lose a company's focus in the face of the economics that drive these markets.⁷³

In addition to identifying structural risks, the Bureau conducts financial trend analysis to identify emerging risks.⁷⁴ For example, the Bureau analyzed the subprime auto loan market. The average term of a subprime auto loan for a new vehicle has increased every year since 2008. At the same time, credit losses for recent loan vintages over the last two years have risen from historically low levels, and some preliminary analysis suggests high levels of early delinquencies. Combined, these trends point to concern that subprime borrowers are being extended credit that they are unable to pay back. Given the potential for harm to consumers in servicing and collections, the Bureau placed subprime auto lending on its priority list in 2015.⁷⁵

The Bureau also considers the relative product market size in the overall consumer finance marketplace.⁷⁶

The second part of the prioritization framework focuses on the institution. This effort assesses the relative risks to the consumer from each institution's activity. Market share is an obvious consideration because the institution's market share within an individual product line likely corresponds to the number of consumers affected by the firm's policies and

⁷² *Id.*

⁷³ *See generally* Steven Antonakes, Prepared Remarks to the Exchequer Club (Feb. 18, 2015).

⁷⁴ *Id.*

⁷⁵ *Id.*

⁷⁶ *Id.*

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practices. The Bureau prioritizes relatively larger players with a more dominant presence due to their ability to impact more consumers than relatively small players.

The Bureau augments this size consideration with field and market intelligence that includes both qualitative and quantitative factors for each institutional product line. The Bureau considers prior experience with the institution's compliance management systems or the existence of other regulatory actions, findings from prior exams, metrics gathered from public reports, and the number and severity of consumer complaints it receives. In addition, given the Bureau's mandate to ensure fair, equitable, and nondiscriminatory access to credit for all consumers, prioritization exercises supplement general field and market intelligence with information that identifies and prioritizes fair lending risks as well.

Taken together, the information that the Bureau gathers about each IPL at the market and institutional levels focuses limited resources on where the Bureau assesses that consumers have the greatest potential to be harmed. Relatively higher risk IPLs within relatively higher risk markets are its highest priority.

[end excerpt]