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# Washington Update

## Politics, Lawsuits and Regulators

August 24, 2023



# Overview

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2. Prudential Bank Regulator Update
3. Key Take Aways



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# CFPB Update

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# General Observations on CFPB

- Fifth and Second Circuits created a circuit split on constitutionality of CFPB's funding; Bureau has not retreated from enforcement efforts
- Enforcement activity generally centering on large institutions and claims, resulting in fewer (but larger) enforcement actions
- CFPB still engages in regulation by enforcement but is using other tools to send messages to the industry and lay down markers for the courts to consider in litigation:
  - Proposed rulemaking or rulemaking agenda
  - Circulars, Advisory Opinions, Supervisory Highlights, Blogs
- CFPB's Enforcement Division
  - More engaged in examinations and RFIs than under prior leadership
  - More aggressive monetary and non-monetary settlement demands in enforcement matters

# Exam Procedures on Unfair Discrimination

- In 2022, the CFPB announced that it had revised its UDAAP exam procedures to include the concept of “unfair discrimination.” The CFPB stated that supervised institutions should ensure that their CMS includes monitoring for discrimination in banking products other than those covered by ECOA (e.g., deposit products) and for groups of consumers other than those protected under ECOA.
- This announcement prompted a lawsuit by numerous trade associations.
- While the CFPB has not issued any enforcement actions specifically calling out this concept of consumer protection, many banks are expanding preventive and detective controls to have something to show their examiners.

# CFPB's Condemnation of "Junk Fees"

- CFPB issued white paper on December 1, 2021, condemning banks for their "fee reliance" and referring to deposit account fees as "junk fees"
  - "Rather than competing on quality service and attractive interest rates, many banks have become hooked on overdraft fees to feed their profit model," said CFPB Director Rohit Chopra. "We will be taking action to restore meaningful competition to this market."
  - Heavy condemnation of OD/NSF fee reliance by JPMorgan Chase, Wells Fargo and Bank of America
- CBA separately issued a report on December 1, 2021, summarizing the results of an overdraft study conducted by Curinos
  - Overdraft fee revenue dropped 57% from 2009 to 2019
  - Consumers understand and want overdraft protection services
  - Average size of transaction causing overdraft increased from \$50 to \$200

# CFPB's Condemnation of "Junk Fees" (cont.)

- CFPB issued Circular 2022-06 "Unanticipated overdraft fee assessment practices" in October 2022 after announcing Regions Bank settlement on APSN
  - "[O]verdraft fees assessed by financial institutions on transactions that a consumer would not reasonably anticipate are likely unfair. These unanticipated overdraft fees are likely to impose substantial injury on consumers that they cannot reasonably avoid and that is not outweighed by countervailing benefits to consumers or competition."
  - Declaring APSN both unfair and deceptive
- Supervisory Highlights, Junk Fees Special Edition issued March 8, 2023
  - Addressed junk fees in deposit accounts, payday and title lending and servicing of mortgage loans, auto loans, student loans
- Proposed rule to lower immunity provision dollar amount for credit card late fees to \$8 and cap late fee at 25% of required minimum payment

# Focal Points of Deposit Exams, Enforcement Actions and Litigation

- Overdraft fees for Authorize Positive Settle Negative (APSN)
- NSF fees for re-presented items
- Assessment of fees for which no service is delivered or the fee is not commensurate with the service
- Transfer fees for accounts linked to checking account
- Records demonstrating a customer's decision to opt-in
- Discrepancies in customer agreement and practices
- Opt-in practices
- Customer communications regarding cost of overdraft protection



# Current State of Play with APSN and NSF Fees

- Large and midsize banks have publicly announced reduction or elimination of fees charged when an account is overdrawn; other banks discretely changing fees and account agreements
- CFPB has conducted multiple rounds of Requests for Information on NSF and OD fees
- CFPB conducting deposit exams – concluding that APSN-based OD fees and NSF fees for represented items are unfair
  - Banks refusing to refund fees voluntarily being issued PARR letters
- Many banks being threatened with litigation or mass arbitration for same practices scrutinized by CFPB and other regulators

# Fair Lending and Fair Servicing

- Small Business Data Collection and Reporting
  - Final rule issued – staggered effective dates
  - Litigation in Texas has called into question effective date for some banks (members of TBA and ABA, plus named plaintiff bank)
  - Even without 1071, ECOA still makes it unlawful to discriminate in small business or commercial lending
- Redlining remains major focal point in fair lending exams
- Director Chopra focused on “digital redlining” and “algorithmic discrimination”
- Patrice Ficklin has warned industry about discrimination (uneven levels of assistance) as COVID-related protections expire
  - Default management (especially for foreclosures and repossessions)
  - Consumers relying on public assistance (e.g., source of income discrimination)

# CARES Act Violations / Consumer Protection During COVID-19

- Failure to adhere to mortgage loss mitigation requirements
- Failure to adhere to credit reporting requirements
- Failure to clearly and consistently describe and offer loss mitigation to non-residential loan workouts or deferrals
- Inadequate garnishment policies and procedures
- Discrimination in offering PPP loans

# Misuse or Misappropriation of Consumer Data

- Increasing focus on data protection / recognition that consumer data can be a company's most vital asset
- Director Chopra is focused heavily on consumers' right to control their data and where they choose to bank
- Expect to see enforcement actions prohibiting banks or finance companies from using data obtained through allegedly deceptive means
- Expect to see UDAAP violations for misuse or misappropriation of data

# Recent Enforcement Actions Against Banks

- Major CFPB Settlements – 2022

- Carrington Mortgage (failure to provide protections and report credit accurately under the CARES Act)
- Hyundai Capital (inaccurate credit reporting – FCRA)
- Regions Bank (authorize positive settle negative – UDAAP)
- Bank of America (handling of disputes for prepaid cards – EFTA, UDAAP)
- U.S. Bank (unauthorized accounts for cards, LOCs, deposit accounts – TILA, TISA, FCRA, UDAAP)
- Bank of America (garnishment practices – UDAAP)
- Wells Fargo (UDAAP – misapplied loan payments, wrongful foreclosures and auto repossessions, incorrectly assessed fees and interest, APSN)

# Recent Enforcement Actions Against Banks

- Major CFPB Settlements – 2023
  - Bank of America (charged NSF fees for represented items - UDAAP)
  - Bank of America (opened credit card accounts and pulled credit reports without consumer authorization and “deceived” customers regarding rewards programs - UDAAP, TILA and FCRA)



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# **Prudential Bank Regulator Update**

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# General Observations on Prudential Bank Regulators

- FRB, OCC and FDIC all stepping up intensity of CMS exams and scrutiny of practices susceptible to fair lending or UDAP violations
- Increase in MRAs, MRBAs, MRIAs and referrals to DOJ for fair lending violations
- More frequent demands for look backs and restitution
- Heightened expectations of roles and responsibilities for the three lines of defense and third-party oversight
- More prescriptive in how to format reports and record observations
- FDIC using AI technology to sift through copious amount of data exported from loan origination systems



# Prudential Regulators Focused on Traditional Fair and Responsible Banking Issues

- Fair lending statistical disparities
  - Pricing, underwriting, exceptions, redlining
  - Robust fair lending compliance program / overall strength of CMS
- UDAP
  - APSN, NSF fees, marketing, disclosures, taking unfair advantage of financially vulnerable consumers
  - FDIC most active in issuing guidance on NSF fees
    - Minnesota Bankers Association and MN bank sued FDIC in July 2023 for being arbitrary and capricious in issuance of guidance on NSF fees for represented items; claiming APA violation; seeking injunctive relief
- Accurate credit reporting (deposit accounts and credit accounts)
- Model governance
  - Fair and responsible use of artificial intelligence and machine learning in marketing, underwriting, pricing, fraud detection
  - Increased expectations on oversight by Compliance of internal modelers and consultants that develop and run models

# Overview of Focal Points in Fair Lending Exams and Investigations

- Redlining Cases
  - DOJ settlements with City National Bank, Park National Bank, Lakeland Bank, Trustmark National Bank, Cadence Bank and more
  - Two dozen+ open investigations at DOJ – banks of all asset sizes (even less than \$1B in assets)
  - Some redlining cases initiated without referral from regulator
    - Claims lodged against banks with Outstanding or Satisfactory CRA ratings
  - DOJ using key search terms in email and text searches of bank employees to identify evidence of racial animous
  - Rural banks scrutinized for creating assessment areas on edge of metropolitan areas but not taking full MSA as assessment area or “REMA”
  - N.D. Ill. ruling on motion to dismiss in Townstone Financial lawsuit filed by CFPB
    - Court ruled ECOA does not protect prospective borrowers
    - Limited impact of court decision on industry due to Fair Housing Act protections

# Overview of Focal Points in Fair Lending Exams and Investigations (cont.)

- Heavy focus in exams on exceptions due to discretion in underwriting decisions
  - Detailed documentation of decisions essential
  - Criticism of fair lending models that do not include all factors used in underwriting
  - Some banks now required to manually capture data from credit reports that cannot be systematically captured
- LEP services continue to be viewed as an important tool in expanding access to credit to underserved markets; banks remain concerned about cost and burden of operationalizing services and potential UDAP of serving customers who may experience language barrier in opening accounts

# Overview of Focal Points in Fair Lending Exams and Investigations (cont.)

- Fair and responsible use of AI and ML
  - Compliance Department expected to know inputs and how models work
- Appraisal bias
  - Banks are now expected to have processes in place to address bias claims
- Not just about mortgage – stay focused on cards, auto, personal lines
- Do not lose sight of expectations to avoid “unfair discrimination” outside ECOA
- Consumer groups are mystery shopping and reporting findings to regulators and other agencies with fair lending and UDAP enforcement authority (local, state, federal)



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# Key Take Aways

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# Key Take Aways

- If your bank originates mortgages, take a hard look at your branch and LPO locations and the geographic distribution of your mortgage lending activity to assess whether your assessment area is properly delineated
- Consider a deep dive into your institution's fees for all products to assess whether the fee is commensurate with the service being delivered and whether fees are clearly and accurately disclosed
- Evaluate the effectiveness of your three lines of defense to ensure that there are controls to prevent and detect gaps in compliance with policies, procedures, regulations and laws



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# Questions

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