

CFPB's New Supervisory Manual Focuses on Risk to Consumers

On October 13, 2011, the Consumer Financial Protection Bureau (CFPB) released the [CFPB Supervision and Examination Manual](#) (Manual). The Manual provides the CFPB's examiners with guidelines for determining whether entities providing consumer financial products and services are complying with the consumer protection laws that are subject to the CFPB's jurisdiction. Consistent with the purpose of the agency, and not surprisingly, the Manual indicates that when the CFPB evaluates the policies and practices of an institution, it will focus on the risk to consumers and will direct its resources toward those areas with higher degrees of risk.

The Manual incorporates examination procedures developed by the Federal Financial Institutions Examination Council for many of the laws now enforced by the CFPB. The CFPB is responsible for enforcing the "federal consumer financial laws," which include nearly every existing federal consumer financial statute, as well as new mandates prescribed by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Act).¹ These include, among other things, Title X of the Act, which prohibits unfair, deceptive, or abusive acts and practices in connection with consumer financial products and services. The entities within the scope of the CFPB's supervision and enforcement authority include both insured depository institutions that have total assets over US\$10 billion ("large depository institutions") and their affiliates, and nondepository consumer financial services companies ("nonbanks"), such as mortgage lenders, payday lenders, and private education lenders.

The examination structure and approach presented in the Manual is generally similar to those employed by the other federal banking agencies (indeed, it was drafted based largely on guidance issued by the other agencies). While its drafters have estimated that approximately 75 percent of the Manual was based on existing guidance, there are aspects that are new and significant. For example, the Manual includes detailed examination procedures for mortgage servicing, which is an indication that the agency plans to devote a great deal of attention to that area. In fact, Raj Date, the *de facto* head of the CFPB in

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¹ One notable exception is the Community Reinvestment Act, regulation and enforcement of which remain with a depository institution's primary federal bank regulatory agency.



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the absence of an appointed director, stated over a month ago that the CFPB was working with other federal agencies to develop basic standards for mortgage servicing and examination thereof.²

Under the CFPB's new procedures, mortgage servicers will be subject to nine examination "modules:"

- (1) servicing and loan-ownership transfers;
- (2) payment processing and account maintenance;
- (3) customer inquiries and complaints;
- (4) maintenance of escrow accounts and insurance products;
- (5) credit reporting;
- (6) information sharing and privacy;
- (7) collections;
- (8) loss mitigation; and
- (9) foreclosures.

In preparation for examinations, mortgage servicers would be advised to analyze their practices within each of these modules and determine how their compliance policies may need to be revised or enhanced.

The CFPB has indicated that in the coming months it will release additional specific guidelines like the mortgage servicing modules to prescribe specific examination procedures organized by product and line of business. If the mortgage servicing procedures are any guide, the forthcoming guidance will likely be more detailed than that currently used by the other federal banking agencies. Each set of new procedures will provide insight into the CFPB's priorities, as well as a framework around which institutions can revise or enhance compliance policies.

In addition to focusing on the risk to consumers, the Manual states that CFPB examinations will be data-driven and that examiners should use the same procedures to examine both

the large depository institutions and the nonbanks that the CFPB supervises. The Manual will initially be used by the CFPB to examine large depository institutions. It will also be used to supervise providers of consumer financial products and services that are not depository institutions, but only after a permanent CFPB director is confirmed.

The Manual states that the CFPB expects each entity it regulates to have an effective compliance management system adapted to its business strategy and operations. It states that an effective compliance management system commonly has the following four components: (1) board management and oversight; (2) a compliance program comprised of policies, procedures, training, and monitoring and corrective action; (3) a system for responding to consumer complaints; and (4) a compliance audit program.

The Manual states that every examination will include a review of the entity's compliance management system, as well as a review for any potential unfair, deceptive, or abusive practice (UDAAP), and regulatory compliance matters presenting risks to consumers. The Manual also provides that every examination covering lending activities must include a review for discrimination and fair lending compliance.

The Manual's provisions relating to UDAAP do not provide any insight as to how the term "abusive" will be interpreted and applied in practice. While it provides examples of potentially unfair or deceptive acts or practices, the Manual does not provide any examples of abusive acts or practices. As part of the UDAAP provisions, the Manual states that examiners should evaluate whether an institution's servicing and collections practices raise potential UDAAP concerns. As noted above, mortgage servicing will receive greater regulatory scrutiny than it typically has received in the past, given the detailed procedures on mortgage servicing in the Manual. The Manual also instructs examiners to interview consumers, as necessary, if the examiner uncovers a potential UDAAP issue. This is a departure from the normal examination process of the other federal banking agencies, which generally do not interview customers.

² See *Lessons Learned from the Financial Crisis: The Need for the CFPB*, Raj Date, Special Advisor to the Secretary of the Treasury for the Consumer Financial Protection Bureau, National Constitution Center, Philadelphia, Pennsylvania (Sept. 15, 2011).

In addition to regular examinations, the CFPB plans to conduct targeted reviews, focusing on particular issues at an institution, as well as horizontal reviews, which focus on a particular issue across multiple institutions. The timing of the examinations will be based upon an assessment of risks to consumers for both large depository institutions and nondepository consumer financial services companies. However, the CFPB will also coordinate the examinations of large depository institutions with those conducted by their prudential and state regulators. We understand that the CFPB will begin examining some large depository institutions before the end of this year.

The CFPB is asking for feedback from the industry, consumer advocates, and the public on its first iteration of the Manual, which it describes as an evolving document. Providing such feedback could be an important way for affected institutions to ensure that the CFPB applies a reasonable and appropriate approach to its examinations. Further, as the CFPB updates the Manual and shifts its regulatory focus to new products and business lines, regulated entities should review and enhance corporate compliance policies to directly address the agency's new priorities and areas of concern.

Arnold & Porter LLP is available to assist you with compliance with the federal consumer financial laws and with preparation for examinations by the CFPB. For further information, please contact your Arnold & Porter attorney or:

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