UDAAP Procedure

UNFAIR, DECEPTIVE, OR ABUSIVE ACTS OR PRACTICES (UDAAP)

MicroBilt provides its personnel with the below UDAAP educational information, and inasmuch it applies to MicroBilt and any relevant products and services, MicroBilt requires adherence to the procedures and UDAAP standards and best practices set forth herein, when reviewing such products and services.

"CFPB Bulletin 2013-07

Date: July 10, 2013

Subject: Prohibition of Unfair, Deceptive, or Abusive Acts or Practices in the Collection of Consumer Debts

Under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), all covered persons or service providers are legally required to refrain from committing unfair, deceptive, or abusive acts or practices (collectively, UDAAPs) in violation of the Act. The Consumer Financial Protection Bureau (CFPB or Bureau) is issuing this bulletin to clarify the contours of that obligation in the context of collecting consumer debts.

This bulletin describes certain acts or practices related to the collection of consumer debt that could, depending on the facts and circumstances, constitute UDAAPs prohibited by the Dodd- Frank Act. Whether conduct like that described in this bulletin constitutes a UDAAP may depend on additional facts and analysis. The examples described in this bulletin are not exhaustive of all potential UDAAPs. The Bureau may closely review any covered person or service provider's consumer debt collection efforts for potential violations of Federal consumer financial laws.

A. Background

UDAAPs can cause significant financial injury to consumers, erode consumer confidence, and undermine fair competition in the financial marketplace. Original creditors and other covered persons and service providers under the Dodd-Frank Act involved in collecting debt related to any consumer financial product or service are subject to the prohibition against UDAAPs in the Dodd-Frank Act.[1]

In addition to the prohibition of UDAAPs under the Dodd-Frank Act, the Fair Debt Collection Practices Act (FDCPA) also makes it illegal for a person defined as a "debt collector" from engaging in conduct "the natural consequence of which is to harass, oppress, or abuse any person in connection with the collection of a debt,"[2] to "use any false, deceptive, or misleading representation or means in connection with the collection of any debt,"[3]

1 *See* Dodd-Frank Act, §§ 1002, 1031 & 1036(a), codified at 12 U.S.C. §§ 5481, 5531 & 5536(a). It is also prohibited for any person, even if not a covered person or service provider, to knowingly or recklessly provide substantial assistance to a covered person or service provider in violating section 1031 of the Dodd-Frank Act. *See* Dodd-Frank Act, § 1036(a)(3), 12 U.S.C. § 5536(a)(3). The principles of "unfair" and "deceptive" practices in the Act are informed by the standards for the same terms under Section 5 of the Federal Trade Commission Act (FTC Act). *See* CFPB Examination Manual v.2 (Oct. 2012) at UDAAP 1 (CFPB Exam Manual). To the extent that this Bulletin cites FTC guidance or authority, such references reflect the views of the FTC, and are not binding upon the Bureau in interpreting the Dodd-Frank Act's prohibition on UDAAPs.
2 FDCPA § 806, 15 U.S.C. § 1692d.
3 FDCPA § 807, 15 U.S.C. § 1692e. This provision also imposes affirmative obligations on "debt collectors" under the FDCPA when collecting consumer debts.

or to "use any unfair or unconscionable means to collect or attempt to collect any debt."[4] The FDCPA generally applies to third-party debt collectors, such as collection agencies, debt purchasers, and attorneys who are regularly engaged in debt collection.[5] All parties covered by the FDCPA must comply with any obligations they have under the FDCPA, in addition to any obligations to refrain from UDAAPs in violation of the Dodd-Frank Act.

Although the FDCPA's definition of "debt collector" does not include some persons who collect consumer debt, all covered persons and service providers must refrain from committing UDAAPs in violation of the Dodd-Frank Act. [6]

B. Summary of Applicable Standards for UDAAPs

1. Unfair Acts or Practices

The Dodd-Frank Act prohibits conduct that constitutes an unfair act or practice. An act or practice is unfair when:

(1) It causes or is likely to cause substantial injury to consumers;
(2) The injury is not reasonably avoidable by consumers; and
(3) The injury is not outweighed by countervailing benefits to consumers or to competition.[7]

A "substantial injury" typically takes the form of monetary harm, such as fees or costs paid by consumers because of the unfair act or practice. However, the injury does not have to be monetary.[8] Although emotional impact and other subjective types of harm will not ordinarily amount to substantial injury, in certain circumstances emotional impacts may amount to or contribute to substantial injury.[9] In addition, actual injury is not required; a significant risk of concrete harm is sufficient.[10]

An injury is not reasonably avoidable by consumers when an act or practice interferes with or hinders a consumer's ability to make informed decisions or take action to avoid that injury.[11] Injury caused by transactions that occur without a consumer's knowledge or consent is not reasonably avoidable.[12] Injuries that can only be avoided by spending large amounts of money or other significant resources also may not be reasonably avoidable.[13] Finally, an act or practice is not unfair if the injury it causes or is likely to cause is outweighed by its consumer or competitive benefits.[14]

Established public policy may be considered with all other evidence to determine whether an act or practice is unfair but may not serve as the primary basis for such determination.[15]

3 FDCPA § 808, 15 U.S.C. § 1692f. This provision also imposes affirmative obligations on "debt collectors" under the FDCPA when collecting consumer debts.
4 *See* FDCPA § 803(6), 15 U.S.C. § 1692a(6). The FDCPA also covers, as a "debt collector," a creditor who, in collecting its own debts, uses any name other than its own which would indicate that a third person is attempting to collect the debts.
5 The FDCPA also reaches any person who designs, compiles, or furnishes forms knowing such forms would be used to create the false belief in a consumer that a person other than the creditor is participating in collecting the creditor's debts. *See* FDCPA § 812, 15 U.S.C. § 1692j.
7 Dodd-Frank Act §§ 1031, 1036, 12 U.S.C. §§ 5531, 5536.
8 CFPB Exam Manual at UDAAP 2; *see also FTC v. Accusearch, Inc.,* 06-cv-105-D, 2007 WL 4356786, at *7-8 (D. Wyo. Sept. 28, 2007); FTC Policy Statement on Unfairness (Dec. 17, 1980), *available at* http://www.ftc.gov/bcp/policystmt/ad-unfair.htm.
9 CFPB Exam Manual at UDAAP 2. 10 *Id.*
11 Id.
12 Id.
13 *See id.* at 2-3.
14 Dodd-Frank Act § 1031(c)(1)(B), 12 U.S.C. § 5531(c)(1)(B); *see also* CFPB Exam Manual at UDAAP 2.
15 Dodd-Frank Act § 1031(c)(2), 12 U.S.C. § 5531(c)(2); *see also* CFPB Exam Manual at UDAAP 3.

2. Deceptive Acts or Practices

The Dodd-Frank Act also prohibits conduct that constitutes a deceptive act or practice. An act or practice is deceptive when:

(1) The act or practice misleads or is likely to mislead the consumer;
(2) The consumer's interpretation is reasonable under the circumstances; and
(3) The misleading act or practice is material.[16]

To determine whether an act or practice has actually misled or is likely to mislead a consumer, the totality of the circumstances is considered.[17] Deceptive acts or practices can take the form of a representation or omission.[18] The Bureau also looks at implied representations, including any implications that statements about the consumer's debt can be supported. Ensuring that claims are supported before they are made will minimize the risk of omitting material information and/or making false statements that could mislead consumers.

To determine if the consumer's interpretation of the information was reasonable under the circumstances when representations target a specific audience, such as older Americans or financially distressed consumers, the communication may be considered from the perspective of a reasonable member of the target audience.[19] A statement or information can be misleading even if not all consumers, or not all consumers in the targeted group, would be misled, so long as a significant minority would be misled.[20] Likewise, if a representation conveys more than one meaning to reasonable consumers, one of which is false, the speaker may still be liable for the misleading interpretation.[21] Material information is information that is likely to affect a consumer's choice of, or conduct regarding, the product or service. Information that is likely important to consumers is material.[22]

Sometimes, a person may make a disclosure or other qualifying statement that might prevent consumers from being misled by a representation or omission that, on its own, would be deceptive. The Bureau looks to the following factors in assessing whether the disclosure or other qualifying statement is adequate to prevent the deception: whether the disclosure is prominent enough for a consumer to notice; whether the information is presented in a clear and easy to understand format; the placement of the information; and the proximity of the information to the other claims it qualifies.[23]

3. Abusive Acts or Practices

The Dodd-Frank Act also prohibits conduct that constitutes an abusive act or practice. An act or practice is abusive when it:

(1) Materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service; or

(2) Takes unreasonable advantage of –
    (A) a consumer's lack of understanding of the material risks, costs, or conditions of the product or service;

16 The standard for "deceptive" practices in the Dodd-Frank Act is informed by the standards for the same terms under Section 5 of the FTC Act. *See* CFPB Exam Manual at UDAAP 5.
17 CFPB Exam Manual at UDAAP 5.
18 18 *Id.*
19 *See id.* at 6.
20 Id.
21 Id.
22 Id.
23 Id.; *see also* CFPB Bulletin 12-06, Marketing of Credit Card Add-On Products (July 12, 2012), *available at* http://files.consumerfinance.gov/f/201207_cfpb_bulletin_marketing_of_credit_card_addon_products.pdf.

(B) a consumer's inability to protect his or her interests in selecting or using a consumer financial product or service; or

(C) a consumer's reasonable reliance on a covered person to act in his or her interests.[24]

It is important to note that, although abusive acts or practices may also be unfair or deceptive, each of these prohibitions are separate and distinct, and are governed by separate legal standards.[25]

C. Examples of Unfair, Deceptive and/or Abusive Acts or Practices

Depending on the facts and circumstances, the following non-exhaustive list of examples of conduct related to the collection of consumer debt could constitute UDAAPs. Accordingly, the Bureau will be watching these practices closely.

- **Collecting or assessing a debt and/or any additional amounts in connection with a debt (including interest, fees, and charges) not expressly authorized by the agreement creating the debt or permitted by law.[26]**
- **Failing to post payments timely or properly or to credit a consumer's account with payments that the consumer submitted on time and then charging late fees to that consumer.[27]**
- **Taking possession of property without the legal right to do so.**
- **Revealing the consumer's debt, without the consumer's consent, to the consumer's employer and/or co-workers.[28]**
- **Falsely representing the character, amount, or legal status of the debt.**
- **Misrepresenting that a debt collection communication is from an attorney.**
- **Misrepresenting that a communication is from a government source or that the source of the communication is affiliated with the government.**

Misrepresenting whether information about a payment or nonpayment would be furnished to a credit reporting agency.[29]

24 Dodd-Frank Act § 1031(d), 12 U.S.C. § 5531(d); *see also* CFPB Exam Manual at UDAAP 9; Stipulated Final Judgment and Order, Conclusions of Law ¶ 12, 9:13-cv-80548 and Compl. ¶¶ 55-63, *CFPB v. Am. Debt Settlement Solutions, Inc.*, 9:13-cv-80548 (S.D. Fla. May 30, 2013), *available at* http://files.consumerfinance.gov/f/201305_cfpb_proposed-order_adss.pdf and http://files.consumerfinance.gov/f/201305_cfpb_complaint_adss.pdf. The Stipulated Final Judgment and Order was signed by U.S. District Judge Middlebrooks and entered on the court docket on June 6, 2013. *See* Stipulated Final J. & Order [ECF Docket Entry No. 5], 9:13-cv-80548 (S.D. Fla.).

25 CFPB Exam Manual at UDAAP 9.

26 *See* Compl. ¶¶ 34-38 & 43-44, *FTC v. Fairbanks Capital Corp.*, 03-12219 (D. Mass. Nov. 12, 2003) (alleging that the charging of late fees and other associated charges was unfair practice under Section 5 of the FTC Act and a violation of §§ 807 and 808 of the FDCPA), *available at* http://www.ftc.gov/os/2003/11/0323014comp.pdf.

27 *Id.* ¶¶ 22-25.

28 *See, e.g.*, Compl. ¶¶ 24 & 30-31, *FTC v. Cash Today, Ltd.*, 3:08-cv-590 (D. Nev. Nov. 12, 2008), *available at* http://www.ftc.gov/os/caselist/0723093/081112cmp0923093.pdf, (asserting that Cash Today engaged in unfair collection practices in violation of Section 5 of the FTC Act by, among other things, disclosing the existence of consumer's debt to employers, co-workers, and other third parties despite being told by consumers not to contact their workplaces); *FTC v. LoanPointe, LLC.*, 2:10 CV 00225- DAK, 2011 WL 4348304, at *5 -6 (D. Utah Sept. 16, 2011) (finding that disclosure of existence and amount of debt to consumer's employer without consumer's prior approval constitutes an unfair practice under the FTC Act).

29 *See, e.g., In re Am. Express Centurion Bank*, Joint Consent Order at 3 (Oct. 1, 2012), *available at* http://files.consumerfinance.gov/f/2012-CFPB-0002-American-Express-Centurion-Consent-Order.pdf. 30 *Id.*

- **Misrepresenting to consumers that their debts would be waived or forgiven if they accepted a settlement offer, when the company does not, in fact, forgive or waive the debt.[30]**

- **Threatening any action that is not intended or the covered person or service provider does not have the authorization to pursue, including false threats of lawsuits, arrest, prosecution, or imprisonment for non-payment of a debt.**

Again, the obligation to avoid UDAAPs under the Dodd-Frank Act is in addition to any obligations that may arise under the FDCPA. Original creditors and other covered persons and service providers involved in collecting debt related to any consumer financial product or service are subject to the prohibition against UDAAPs in the Dodd-Frank Act. The CFPB will continue to review closely the practices of those engaged in the collection of consumer debts for potential UDAAPs, including the practices described above. The Bureau will use all appropriate tools to assess whether supervisory, enforcement, or other actions may be necessary."

Source: http://files.consumerfinance.gov/f/201307_cfpb_bulletin_unfair-deceptive-abusive-practices.pdf

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The FTC and the Dodd-Frank Act have defined the terms unfair, deceptive and abusive as follows:

"What is "unfair"?

- The practice causes or is likely to cause substantial injury.
- The injury cannot reasonably be avoided.
- The injury is not outweighed by any benefits.

What is "deceptive"?

- The practice misleads or is likely to mislead.
- A "reasonable" consumer would be misled.
- The presentation, omission or practice is material.

What is "abusive"?

- The practice materially interferes with the consumers ability to understand a term or condition of a product or service.
- The practice takes unreasonable advantage of a consumer's lack of understanding of the risk, costs and conditions of a products or service.

Managing your UDAAP Risk

There is no doubt UDAAP will continue to challenge the industry, so it is essential for financial institutions to evaluate their risks and do what they can to diminish the impact violations may have on their organization. Proactive steps banks can take are:

- Regularly review features of consumer products and services. Evaluate product features and promotional materials and determine if any terms fall within the broad definition of UDAAP.

- Evaluate new products for features that could be misunderstood or ones that have been omitted.

- Review revenue streams for trends that may suggest abusive practices.

- Evaluate written and oral methods of communicating product features to customers.

- Review third-party service provider agreements to develop a clear understanding of their practices surrounding the service being provided.

- Review all bank policies and procedures for practices that suggest unfair, deceptive, or abusive practices.
- Create a consumer-friendly culture within your organization.
- Evaluate customer complaints for signs of more serious systemic problems."

"Abusive Acts Defined.

Section 1031 of the Dodd-Frank Act defined an abusive act or practice as one which either:

1) materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service; or

2) takes unreasonable advantage of -

(A) a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service;

(B) the inability of the consumer to protect the interests of the consumer in selecting or using a consumer financial product or service; or

(C) the reasonable reliance by the consumer on a covered person to act in the interests of the consumer.

Elements of Good Regulatory Risk Management.

Historically, regulatory compliance risk management has consisted of several elements. These elements, discussed below, are universal in all well run regulatory compliance risk management groups.

Governance Structures.

Someone (a person or group) within the organization has to be ultimately responsible for UDAAP compliance governance and the program framework. Often this responsibility lies within the corporate compliance department or similar risk management area. However, good

governance requires that this responsibility report up the organization to a higher level. It is common to see the reporting for this function culminate at the board committee level, such as the Risk Committee. The actual responsibility for UDAAP compliance execution generally lies within the lines of businesses.

In addition, a strong regulatory compliance function is required to be capable of credibly challenging the lines of business. In no regulatory area is this more important than in UDAAP compliance. The lack of clearly enumerated technical rules requires that the risk management function be able to convincingly articulate why a practice is potentially an unfair, deceptive, or abusive one. The lines are often blurry and issues are seldom black and white.

Policies.

Strong, concrete policies that clearly state the bank's attitude and expectations regarding the fair treatment of consumers are a foundation of effective UDAAP compliance. Framing the main policy as "fair treatment" rather than as "UDAAP compliance" is helpful in that it is more positive and helps to connect the policy to each employee's day-to-day work that impacts consumers.

Procedures.

UDAAP-related business level procedures that are specifically targeted to job duties are extremely helpful to prompt employees to make good decisions that will benefit both the bank and its customers. For example, procedures for telephone sales practices should include not only instructions for how to convey the information to the consumer and what to say to answer questions that are raised, but also procedures for how to terminate the conversation *without pressing for a sale* when the consumer appears to be confused or states that he or she does not want to purchase the product.

Risk Assessments.

Good risk management practices necessarily require that the bank identify both the risks it faces and the controls in place to mitigate the risks. A UDAAP risk assessment comprehensively identifies such risks across the enterprise and throughout the life cycle of each product and service. Measuring the effectiveness of the controls is an integral part of determining the level of residual risk remaining. Mapping the risks to each control is a great exercise to help the organization find any gaps remaining in its compliance program.

Monitoring and Testing.

A requirement for every risk management program is to regularly test the effectiveness of the processes. The risk management area is considered to be the second line of defense in the overall risk controls (the line of business processes are the first line, the internal audit function is the third.)

Implementing UDAAP monitoring and testing can be challenging since the lack of technical rules makes it hard to fashion a checklist of things to review. However, thoughtful reviews of the product on a lifecycle basis can help uncover potential issues.

Auditing.

The internal audit function was specifically mentioned in the CFPB's enforcement actions against American Express and Discover as being "inadequate" for failing to catch the UDAAP issues. Internal audit is supposed to operate as the so-called "third line of defense."

UDAAP auditing comes with the same types of challenges as UDAAP monitoring. Audit programs are generally based on very specific requirements. Since UDAAP has so few technical, concrete requirements, it is more difficult to prepare effective work programs. One approach is to audit each line of business or individual product over its entire lifecycle with a thoughtful approach to test the UDAAP risk management controls at each phase of the lifecycle.

Training.

UDAAP training is key not only to transferring awareness of UDAAP concepts to all bank personnel at every level but also to influencing a culture of fairness within the organization. All employees at leadership levels and all with customer impact should receive more specific UDAAP training no less often than annually.

Management Reporting.

Financial institutions, like all businesses, run on metrics. UDAAP/fairness related metrics are essential to understanding the level of UDAAP compliance risks at any point in time. Developing these metrics requires a careful review of products, services, and processes to determine what are the indices of key UDAAP or fairness risks.

Establishing Fairness Principles.

Effective UDAAP risk management requires a more strategic, proactive approach. A good first step is to establish commonly understood principles of fairness for the entire bank to follow. These principles can help to shape the bank's culture and guide the elements of the UDAAP compliance program. The purpose of formulating these principles is to bring all parties to the table so that all agree on what "fairness" looks like for the institution.

There are four principles that can be easily conveyed to the bank as a whole and can be used to evaluate fairness in financial products throughout their lifecycles from product design all the way through to the servicing stage:

1. *Understandability:* The consumer should be easily able to grasp the concepts (i.e., terms and conditions) of the product. If it is too complicated, it carries greater UDAAP risk.

2. *Predictability:* Consumers should be able to understand how the product will work in the future and, for example, how they can avoid fees or penalties. Complicated overdraft protection plans sometimes are not predictable enough for the consumer to avoid overdraft fees. Hence they can carry elevated UDAAP risks.

3. *Value:* There must be a real benefit for the consumer. An example of a case where the consumers received no value is when cardholders paid for identity theft protection each month but did not activate the service so they got no benefit.

4. *Appropriateness:* If a product is inappropriate for the consumer, it is likely has some fairness issues. An example is the marketing and sale of secured credit card products to individuals who would qualify for prime products. Secured credit cards are almost always more costly. By taking advantage of a consumer who does not understand that he or she could qualify for something more appropriate, the institution is running a risk of violating the abusive standard.

Once these fairness principles are understood and agreed upon, other more proactive risk management processes can be implemented.

Make a Cultural Commitment.

To begin with, bank leadership must make a strong commitment to cultivating a culture of fairness. Communication is a key component beginning with the "tone at the top." Culture is created from the top of the house—the messaging from executive leadership has to be strong and unequivocal. To move the cultural needle, a consistent internal messaging campaign should be forthcoming from the bank's leadership.

Institute Proactive Risk Scans.

Risk managers, including regulatory compliance, legal, and operational risk areas all must establish systems to scan the risk horizon for emerging issues from the regulatory agencies, new litigation, and within the bank's own operational areas where new products and promotions all have the potential for UDAAP risks.

Align Incentives.

Incentives for all bank employees with UDAAP-relevant jobs should have performance measures for UDAAP. Incentive compensation should be reviewed rigorously to ensure that no one is incented for bad behavior.

Review New Products.

Rigorous new product initiative processes should include UDAAP screens so that all new ideas for products and services are reviewed for fairness issues. New products and promotions must be thoroughly tested operationally in order to make sure they work as they will be advertised. Finally, ensuring that consumers understand each product through the use of focus groups and the like is a key to avoiding deception issues in the future.

Establish Complaint Management Programs.

Arguably the most important risk management tool for UDAAP compliance management is a robust complaint management program. Capturing the data on all complaints and resolving them is just the beginning. Complaints should be analyzed for their root cause and the trends analyzed to determine where changes should be made within products and in the UDAAP compliance program itself.

Be Proactive in Identification and Remediation of Issues.

While it seems intuitive that an organization should attempt to identify its own problems and remediate them as quickly as possible, in the litigious environment in which all corporations live, this activity is sometimes not encouraged as much as it should be. However, proactive financial organizations that successfully deal with UDAAP compliance in the future will aggressively find and fix their own problems.

The CFPB mentioned this concept of proactive compliance management in its guidance on Responsible Conduct issued in June 2013. This guidance provides an understanding of when the CFPB will give an institution "credit" for a proactive compliance culture and program during an examination.

Questions that will be germane to the determination include whether there was a culture of compliance and what the "tone at the top" was. The guidance provides a roadmap for rewarding an institution that encourages proactive compliance management:

. . . a party may proactively self-police for potential violations, romptly self-report to the Bureau when it identifies potential violations, quickly and completely remediate the harm resulting from violations, and affirmatively cooperate with any Bureau investigation above and beyond what is required. If a party meaningfully engages in these activities, which this bulletin refers to collectively as "responsible conduct," it may favorably affect the ultimate resolution of a Bureau enforcement investigation."

Reference: 2012 CFPB Examination Manual

"UNFAIR, DECEPTIVE, OR ABUSIVE ACTS OR PRACTICES (UDAAP) EXAMINATION PROCEDURES

Examination Objectives

• To assess the quality of the credit union's compliance risk management systems, including internal controls and policies and procedures, for avoiding unfair, deceptive, or abusive acts or practices (UDAAP).

• To identify acts or practices that materially increase the risk of consumers being treated in an unfair, deceptive, or abusive manner.

• To gather facts that help determine whether the credit union engages in acts or practices when offering or providing consumer financial products or services that are likely to be unfair, deceptive, or abusive.

• To determine, in consultation with EIC or Field Examiner Supervisor, whether an unfair, deceptive or abusive act or practice has occurred and whether further supervisory or enforcement actions are appropriate.

General Guidance

Based on the results of the risk assessment of the credit union, examiners should review for potential unfair, deceptive, or abusive acts or practices, taking into account a credit union's marketing programs, product and service mix, customer base, and other factors, as appropriate. Even if the risk assessment has not identified potential unfair, deceptive, or abusive acts or practices, examiners should be alert throughout an examination for situations that warrant review.

Document Review

a. To initially identify potential areas of UDAAP concerns, obtain and review copies of the following to the extent relevant to the examination:

- Training materials.
- Lists of products and services, including descriptions, fee structure, disclosures, notices, agreements, and periodic and account statements.
- Procedure manuals and written policies, including those for servicing and collections.
- Minutes of the meetings of the Board of Directors and of management committees, including those related to compliance.
- Internal control monitoring and auditing materials.
- Compensation arrangements, including incentive programs for employees and third parties.
- Documentation related to new product development, including relevant meeting minutes of Board of Directors, and of compliance and new product committees.
- Marketing programs, advertisements, and other promotional material in all forms of media (including print, radio, television, telephone, Internet, or social media advertising).
- Scripts and recorded calls for telemarketing and collections.
- Organizational charts, including those related to affiliate relationships and work processes.
- Agreements with affiliates and third parties that interact with consumers on behalf of the credit union.
- Consumer complaint files.
- Documentation related to software development and testing, as applicable.

Management and Policy-Related Examination Procedures

1. Identify potential UDAAP concerns by reviewing all relevant written policies and procedures, customer complaints received by the credit union or by the Division of Credit Unions (DCU), internal and external audit reports, statistical and management reports, and examination reports. Determine whether:

a. The scope of the credit union's compliance audit includes a review of potential unfair, deceptive, or abusive acts or practices.

b. The compliance audit work is performed consistent with the audit plan and scope.

c. The frequency and depth of audit review is appropriate to the nature of the activities and size of the credit union.

d. Management and the Board of Directors are made aware of and review significant deficiencies and their causes.

e. Management has taken corrective actions to follow up on any identified deficiencies.

f. The credit union's compliance programs ensure that policies are being followed through its sampling of relevant product types and decision centers, including sales, processing, and underwriting.

g. The credit union has a process to respond to consumer complaints in a timely manner and determine whether consumer complaints raise potential UDAAP concerns.

h. The credit union has been subject to any enforcement actions or has been investigated by a regulatory or law enforcement agency for violations of consumer protection laws or regulations that may indicate potential UDAAP concerns.

2. Through discussions with management and a review of available information, determine whether the credit union's internal controls are adequate to prevent unfair, deceptive or abusive acts or practices. Consider whether:

a. The compliance management program includes measures aimed at avoiding unfair, deceptive, or abusive practices, including:

- Organization charts and process flowcharts;
- Policies and procedures; and
- Monitoring and audit procedures.

b. The credit union conducts prior UDAAP reviews of advertising and promotional materials, including promotional materials and marketing scripts for new products.

c. The credit union evaluates initial and subsequent disclosures, including customer agreements and changes in terms, for potential UDAAP concerns.

d. The credit union reviews new products and changes in the terms and conditions of existing products for potential UDAAP concerns.

e. The credit union has a thorough process for receiving and responding to consumer complaints and has a process to receive complaints made to third parties, such as the Better Business Bureau, the CFPB, or the DCU.

f. The credit union evaluates servicing and collections for UDAAP concerns.

g. The credit union has established policies and controls relating to employee and third- party conduct, including:

- Initial and ongoing training;
- Performance reviews or audits;
- Discipline policies and records of disciplinary actions;
- Third-party agreements and contractual performance standards;
- Compensation programs; and o Monitoring.

h. The credit union's internal control processes are documented.

i. Computer programs are tested and documented to ensure accurate and timely disclosures to consumers.

3. Potential Areas for Transaction Testing

Through a high-level assessment of the credit union's products, services, and customer base, identify areas for potential transaction testing. This process should determine whether:

a. The credit union does not underwrite a given credit product on the basis of ability to repay.

b. A product's profitability depends significantly on penalty fees or "back-end" rather than upfront fees.

c. A product has high rates of repricing or other changes in terms.

d. A product combines features and terms in a manner that can increase the difficulty of consumer understanding of the overall costs or risks of the product and the potential harm.

e. Penalties are imposed on a customer when he terminates his relationship with the credit union.

f. Fees or other costs are imposed on a consumer to obtain information about his account.

g. A product is targeted to particular populations, without appropriate tailoring of marketing, disclosures, and other materials designed to ensure understanding by the consumers.

Transaction-Related Examination Procedures

If upon conclusion of the management and policy-related examination procedures, procedural weaknesses, or other UDAAP risks require further investigation, conduct transaction testing, as necessary, using the following examination procedures. Use judgment in deciding to what extent to sample individual products, services, or marketing programs. Increase the sample size to achieve confidence that all aspects of the credit union's products and services are reviewed sufficiently. Consult with EIC or Field Examiner Supervisor to obtain assistance with the sampling process.

1. Marketing and Disclosures

Through a review of marketing materials, customer agreements, and other disclosures, determine whether, before the consumer chooses to obtain the product or service:

a. All representations are factually based.

b. All materials describe clearly, prominently, and accurately:

- costs, benefits, and other material terms of the products or services being offered;
- related products or services being offered either as an option or required to obtained certain terms; and
- material limitations or conditions on the terms or availability of products and services, such as time limitations for favorable rates, promotional features, expiration dates, prerequisites for obtaining particular products or services, or conditions for canceling services.

c. The customer's attention is drawn to key terms, including limitations and conditions, that are important to enable the consumer to make an informed decision.

d. All materials clearly and prominently disclose the fees, penalties, and other charges that may be imposed and the reason for the imposition.

e. Contracts clearly inform customers of contract provisions that permit changes in terms and conditions of the product or service.

f. All materials clearly communicate the costs, benefits, availability, and other terms in language that can be understood when products are targeted to particular populations, such as reverse mortgage loans for the elderly.

g. Materials do not misrepresent costs, conditions, limitations, or other terms either affirmatively or by omission.

h. The credit union avoids advertising terms that are generally not available to the typical targeted consumer.

2. Availability of Terms or Services as Advertised

Evaluate whether product(s) and service(s) that consumers are receiving are consistent with the disclosures and policies. For each product and service being reviewed, select a sample that:

a. Is sufficient in size to reach a supportable conclusion about such consistency;

b. Includes, as appropriate, transactions from different origination and underwriting channels — for example, different geographical areas or different sectors of the credit union's organization structure; and

c. Includes approved and/or denied accounts.

Determine whether:

a. Consumers are reasonably able to obtain the products and services, including interest rates or rewards, as represented by the credit union.

b. Consumers receive the specific product or service that they request.

c. Counter-offers clearly, prominently, and accurately explain the difference between the original product or services requested and the one being offered.

d. Actual practices are consistent with stated policies, procedures, or account disclosures.

3. Availability of Actual Credit to the Consumer

Evaluate whether the credit union represents the amount of useable credit that the consumer will receive in a truthful way. Consider whether:

a. The available credit is sufficient to allow the consumer to use the product as advertised and disclosed to the consumer.

b. The fees and charges, typically imposed on the average targeted customer, both initially and throughout the term of the loan, remain in a range that does not prevent the availability of credit.

c. The credit union honors convenience checks when used by the customer in a manner consistent with introductory or promotional materials and disclosures.

4. Employees and Third Parties Interacting with Consumers

Evaluate how the credit union monitors the activities of employees and third-party contractors, marketing sales personnel, vendors, and service providers to ensure they do not engage in unfair, deceptive, or abusive acts or practices with respect to consumer interactions. Interview employees and third parties, as appropriate. Specifically, consider whether:

a. The credit union ensures that employees and third parties who market or promote products or services are adequately trained so that they do not engage in unfair, deceptive, or abusive acts or practices.

b. The credit union conducts periodic evaluations or audits to check whether employees or third parties follow the credit union's training and procedures and has a disciplinary policy in place to deal with any deficiencies.

c. The credit union reviews compensation arrangements for employees, third-party contractors, and service providers to ensure that they do not create unintended incentives to engage in unfair, deceptive, or abusive acts or practices, particularly with respect to product sales, loan originations, and collections.

d. Performance evaluation criteria do not create unintended incentives to engage in unfair, deceptive, or abusive acts or practices, including criteria for sales personnel based on sales volume, size, terms of sale, or account performance.

e. The credit union implements and maintains effective risk and supervisory controls to select and manage third-party contractors and service providers.

5. Servicing and Collections

Evaluate whether servicing and collections practices raise potential UDAAP concerns, by considering whether**:**

a. The credit union has policies detailing servicing and collections practices and has monitoring systems to prevent unfair, deceptive or abusive acts or practices.

b. Call centers, either operated by the credit union itself or by third parties, effectively respond to consumers' calls.

c. The credit union ensures that employees and third party contractors:

- represent fees or charges on periodic statements in a manner that is not misleading;
- post and credit consumer payments in a timely manner;
- apply payments in a manner that does not unnecessarily increase customer payments, without clear justification;
- only charge customers for products and services, such as insurance or credit protection programs, that are specifically agreed to;
- mail periodic statements in time to provide the consumer ample opportunity to avoid late payments; and o do not represent to consumers that they may pay less than the minimum amount without clearly and prominently disclosing any fees for paying the reduced amount.

d. The credit union has policies to ensure compliance with the standards under the Fair Debt Collections Practices Act to prevent abusive, deceptive, or unfair debt collection practices.

e. Employees and third party contractors clearly indicate to consumers that they are calling about the collection of a debt.

f. Employees and third party contractors do not disclose the existence of a consumer's debt to the public without the consent of the consumer, except as permitted by law.

g. The credit union avoids repeated telephone calls to consumers that annoy, abuse, or harass any person at the number called.

6. Interviews with Consumers

If potential UDAAP issues are identified that would necessitate interviews with consumers, consult with the EIC or DCU Field Examiner Supervisor."

REFERENCE: 2012 CFPB Examination Manual

Source: https://dfi.wa.gov/documents/credit-unions/compliance-manual/udaap-procedures.pdf

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"**CFPB Examination Procedures 2011 UDAAP 1 Unfair,**

Deceptive, or Abusive Acts or Practices Introduction

Unfair, deceptive, or abusive acts and practices (UDAAPs) can cause significant financial injury to consumers, erode consumer confidence, and undermine the financial marketplace. Under the Dodd-Frank Act, it is unlawful for any provider of consumer financial products or services or a service provider to engage in any unfair, deceptive or abusive act or practice.[1] The Act also provides CFPB with rule-making authority and, with respect to entities within its jurisdiction, enforcement authority to prevent unfair, deceptive, or abusive acts or practices in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service.[2] In addition, CFPB has supervisory authority for detecting and assessing risks to consumers and to markets for consumer financial products and services.[3]

As examiners review products or services, such as deposit products or lending activities, they generally should identify the risks of harm to consumers that are particular to those activities.

1 Dodd-Frank Act, Title X, Subtitle C, Sec. 1036; PL 111-203 (July 21, 2010).
2 Sec. 1031 of the Act. The principles of "unfair" and "deceptive" practices in the Act are similar to those under Sec. 5of the Federal Trade Commission Act (FTC Act). The Federal Trade Commission (FTC) and federal banking regulators have applied these standards through case law, official policy statements, guidance, examination procedures, and enforcement actions that may inform CFPB.
3 Sec. 1024; Sec. 1025(b)(1); Sec. 1026(b) of the Act.

Examiners also should review products that combine features and terms in a manner that can increase the difficulty of consumer understanding of the overall costs or risks of the product and the potential harm to the consumer associated with the product.

These examination procedures provide general guidance on:

- The principles of unfairness, deception, and abuse in the context of offering and providing consumer financial products and services;

- Assessing the risk that an institution's practices may be unfair, deceptive, or abusive;

- Identifying unfair, deceptive or abusive acts or practices(including by providing examples of potentially unfair or deceptive acts and practices); and

- Understanding the interplay between unfair, deceptive, or abusive acts or practices and other consumer protection statutes.

EXAMINATION OBJECTIVES

- To assess the quality of the regulated entity's compliance risk management systems, including internal controls and policies and procedures, for avoiding unfair, deceptive, or abusive acts or practices (UDAAP).

- To identify acts or practices that materially increase the risk of consumers being treated in an unfair, deceptive, or abusive manner.

- To gather facts that help determine whether a regulated entity engages in acts or practices when offering or providing consumer financial products or services that are likely to be unfair, deceptive, or abusive.

- To determine, in consultation with Headquarters, whether an unfair, deceptive or abusive act or practice has occurred and whether further supervisory or enforcement actions are appropriate.

GENERAL GUIDANCE

Based on the results of the risk assessment of the entity, examiners should review for potential unfair, deceptive, or abusive acts or practices, taking into account an entity's marketing programs, product and service mix, customer base, and other factors, as appropriate. Even if the risk assessment has not identified potential unfair, deceptive, or abusive acts or practices, examiners should be alert throughout an examination for situations that warrant review.

1. Document Review

To initially identify potential areas of UDAAP concerns, obtain and review copies of the following to the extent relevant to the examination:

- Training materials.
- Lists of products and services, including descriptions, fee structure, disclosures, notices, agreements, and periodic and account statements.
- Procedure manuals and written policies, including those for servicing and collections.
- Minutes of the meetings of the Board of Directors and of management committees, including those related to compliance.
- Internal control monitoring and auditing materials.
- Compensation arrangements, including incentive programs for employees and third parties.
- Documentation related to new product development, including relevant meeting minutes of Board of Directors, and of compliance and new product committees."

Source: http://www.cfpaguide.com/portalresource/Manual%20-%20UDAAP.pdf