

The CFPB Examination Process

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Prepared on February 5, 2013

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II. CFPB Examination Authority and Process

- A. Under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”), the CFPB has the authority to conduct examinations of:
 - 1. banks, savings associations, and credit unions with assets of over \$10 billion (“large depository institutions”);
 - 2. consumer mortgage companies, payday lenders, and private education lenders;
 - 3. any “larger participant” in a market for consumer financial products or services; and

4. anyone who engages in “conduct that poses risks to consumers with regard to the offering or provision of consumer financial products and services.”¹
- B. The CFPB examination process does not differ markedly from that of the prudential regulators. Like the traditional bank regulators, the CFPB will:
1. provide a notice prior to the on-site examination (typically 30-60 days);
 2. request documents before, during, and after the examination;
 3. include interviews of key employees at the institution;
 4. conclude the examination with an examination report accompanied by a compliance rating from one (highest) to five (lowest); and
 5. communicate supervisory concerns that require correction, and in some cases may form the basis for an enforcement action.²
- C. However, the focus of CFPB examinations is quite different from traditional bank examinations. The CFPB’s focus is on the consumer experience, rather than safety and soundness.³

¹ 12 U.S.C. §§ 5514 and 5515.

² CFPB Supervision and Examination Manual 2.0 (Oct. 31, 2012), available at http://files.consumerfinance.gov/f/201210_cfpb_supervision-and-examination-manual-v2.pdf.

³ The CFPB’s central mission is “to make markets for consumer financial products and services work for Americans.” *Learn About the Bureau*, available at <http://www.consumerfinance.gov/the-bureau/>.

1. CFPB Director Richard Cordray has explained:

“We have a somewhat different approach here. We are now examining institutions for how they treat consumers. It’s not about the institution itself. It’s about the impact on consumers. It’s almost as though you take your traditional examination mode and you take that examiner and turn them around 180 degrees to look back at the public and how they’re affected rather than solely at the potential impact on the institution.”⁴

2. This focus is reflected in the CFPB’s Examination Manual, which explains the CFPB “will focus on an institution’s ability to detect, prevent, and correct practices that present a significant risk of violating the law and causing consumer harm.”⁵

3. The CFPB’s initial Supervision and Examination Manual was limited to FDIC-insured banks. Following the recess appointment of Director Cordray on January 4, 2012, the CFPB expanded its examination guidance to include nonbank supervision.⁶ Since that time, the CFPB has issued examination procedures regarding debt collection⁷

⁴ *Cordray Defends Complaint Database, Talks Qualified Mortgage Plan*, American Banker, July 9, 2012.

⁵ CFPB Supervision and Examination Manual 2.0, *supra* note 2.

⁶ Our Blog: The CFPB launches its nonbank supervision program (January 5, 2012), available at <http://www.consumerfinance.gov/blog/the-cfpb-launches-its-nonbank-supervision-program/#more-11087>.

⁷ CFPB Debt Collection Examination Procedures (October 24, 2012), available at http://files.consumerfinance.gov/f/201210_cfpb_debt-collection-examination-procedures.pdf.

and student lenders.⁸ In October 2012, the CFPB released an updated version of its Supervision and Examination Manual.⁹

III. CFPB Coordination with Prudential Regulators in the Examination of Large Depository Institutions

- A. The Dodd Frank Act requires that the CFPB “coordinate its supervisory activities with the supervisory activities conducted by prudential regulators and the State bank regulatory authorities.”¹⁰
 - 1. Such coordination includes consultation regarding examination schedules, as well as the Bureau’s use of existing examination reports and public information “to the fullest extent possible.”¹¹
- B. On June 4, 2012, the CFPB and the federal prudential regulators (the Federal Reserve, the Federal Deposit Insurance Corporation (“FDIC”), the Office of the Comptroller of the Currency (“OCC”), and the National Credit Union Administration (“NCUA”)) released a Memorandum of Understanding (MOU) dated May 16,

⁸ CFPB Education Loan Examination Procedures (December 17, 2012), available at http://files.consumerfinance.gov/f/201212_cfpb_educationloanexamprocedures.pdf.

⁹ CFPB Supervision and Examination Manual 2.0, *supra* note 2.

¹⁰ 12 U.S.C. § 5515(b)(2).

¹¹ 12 U.S.C. § 5515(b)(3).

2012, addressing the coordination requirements of the Dodd-Frank Act.¹²

1. The MOU included guidelines for the coordination of simultaneous examinations, procedures for opting out of simultaneous examinations, and processes for inter-agency information sharing.

a. The guidelines for simultaneous and coordinated examinations include:

i. designation by the CFPB and prudential regulators of a point of contact for purposes of information sharing and coordination;

ii. coordination of supervision of institutions on both an ongoing and point-in-time basis;

iii. the sharing of drafts of reports of examination and related supervisory information prior to issuing final reports of examination; and

iv. consideration by the CFPB and the prudential regulators of any concerns raised by the other agency during the covered examination.

¹² Memorandum of Understanding on Supervisory Coordination (May 16, 2012), *available at* http://files.consumerfinance.gov/f/201206_CFPB_MOU_Supervisory_Coordination.pdf

- b. Opt-out procedures: A covered institution may request that examinations by the CFPB and prudential regulators be conducted separately. The institution must provide adequate notice regarding its request. Such requests will remain in effect until the next time the CFPB and the applicable prudential regulator plan a simultaneous exam, unless the institution requests a longer time period.

- c. Information Sharing and Confidentiality: The MOU provides that the CFPB and prudential regulators have separately executed confidentiality MOUs, and that the CFPB and the prudential regulators will share material supervisory information (including supervisory letters, supervisory actions, reports of exam, and other material supervisory information). However, the MOU also provides that “in accordance with section 1025(a)(3) of the Dodd-Frank Act, and for purposes of minimizing regulatory burden, the CFPB will, to the fullest extent possible, use reports pertaining to a Covered Institution that have been provided or required to have been provided to a Federal or State agency, and information that has been reported publicly.”

C. Although the MOU was a necessary step in the required coordination, the prudential regulators and the CFPB are

still developing the process, and the general challenges of such coordination have been noted.¹³

1. Among the issues of interest to the industry with respect to the coordination is the extent to which prudential regulators may attempt to influence CFPB examination directives or supervisory actions due to potential safety and soundness concerns.
2. The regulators (and the regulated) are likely to develop a rhythm over time, diminishing some of the coordination challenges of the Bureau's first years.

IV. CFPB Examination of Nonbanks

- A. Nonbanks newly subject to supervisory exams have undertaken significant efforts to learn about and prepare for the examination process, including conducting internal reviews and hiring consultants and law firms to review consumer compliance policies and procedures.
- B. The CFPB has reorganized internally to coordinate bank and nonbank examination approaches.¹⁴

¹³ *Oversight of Dodd-Frank Implementation: A Progress Report by the Regulators at the Half Year Mark: Hearing Before the Committee of Banking, Housing, and Urban Affairs*, 112th Cong. 71 (Feb. 17, 2011) (statement by John Walsh, Acting Comptroller of the Currency), available at <http://www.gpo.gov/fdsys/pkg/CHRG-112shrg65718/pdf/CHRG-112shrg65718.pdf>. (“[A] provision presenting potential concerns are the particular requirements for how the prudential supervisors and the CFPB conduct examinations of institutions with \$10 billion or more in size We plan to work with the CFPB to ensure appropriate oversight . . . without creating duplicative and potentially inconsistent supervision.”).

1. The CFPB was initially structured with separate divisions for large bank supervision and nonbank supervision.
2. However, the Bureau reorganized in late 2012. The reorganization retained the structure of having two supervision offices, but the two supervision offices are now divided between examinations and policy. Large bank and nonbank supervision are now merged into a single Supervision Examinations team, headed by Paul Sanford, previously Acting Assistant Director of Large Bank Supervision. The Policy team is organized by product or service market rather than by the type of financial institution. Peggy Twohig is the Assistant Director of this Office.
3. The CFPB explained the reorganization was to create “a better and more coordinated approach to the markets we supervise and a sharper line of sight across both banks and nonbanks.”¹⁵

V. Legal Issues in the Examination Process:

A. Scope

1. One open legal issue is the scope of the CFPB’s authority to require the production of documents. The Dodd Frank Act granted the CFPB the authority to “require reports and conduct examinations” on covered entities to “(1) assess compliance with consumer financial laws; (2)

¹⁴ *Realigning our supervision work*, CFPB blog entry dated December 17, 2012, available at <http://www.consumerfinance.gov/blog/realigning-our-supervision-work/>.

¹⁵ *Id.*

obtain information to assess compliance systems or procedures; and (3) detect risks to consumers and markets for consumer financial products or services.”¹⁶ This language appears to indicate that the CFPB’s authority is limited to materials that bear on consumer financial laws and related concerns.

2. In a January 4, 2012 Guidance Bulletin, the Bureau noted that the Bureau exercises its examination authority only for the “certain purposes” listed above, but made clear that the Bureau alone will determine whether a document request is within its authority:

“Once the Bureau has issued a request that it has determined serves one or more purposes, supervised institutions are required to provide all documents and other information responsive to the request. Supervised institutions may not selectively withhold responsive documents based on their judgment that such materials are not necessary to the Bureau’s execution of its responsibilities or that other materials would be sufficient to suit the Bureau’s needs.”¹⁷

3. The Bureau also put supervised institutions on notice that its authority is expansive:

“The supervisory process is based on the supervisor’s full and unfettered access to information, and the supervisor is entitled – indeed, duty bound – to ensure that it thoroughly

¹⁶ 12 U.S.C. §5515(a)(1).

¹⁷ CFPB Bulletin 12-01, *The Bureau’s Supervision Authority and Treatment of Confidential Supervisory Information* (Jan. 4, 2012).

understands the institution in question and has access to all information that, in its independent judgment, may bear on its supervisory responsibilities.”¹⁸

4. Finally, the Bureau has indicated it will not brook any opposition to its requests:

“Failure to provide information required by the Bureau is a violation of law for which the Bureau will pursue all available remedies. *See* 12 U.S.C. §§ 5536(a)(2), 5565.”¹⁹

B. Privilege Waiver

1. The CFPB has long taken the position that it may compel the production of privileged material.²⁰
2. This position was problematic because, *inter alia*, the CFPB was not included in the provisions of the Federal Deposit Insurance Act (12 U.S.C. §§ 1821(t) and 1828(x)) preserving privilege for materials provided to covered banking regulators and preserving the privilege of such documents

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ *See Id.* (“entities must comply with the Bureau’s supervisory requests for information.”)

when shared by one covered regulator with another.²¹

3. This omission led to concerns that production of such documents to the CFPB could constitute a waiver of the privilege.
4. The risk of waiver was even higher for nonbank financial institutions. The CFPB's argument that no waiver would occur was based in part on the transfer of powers from traditional bank regulators to the CFPB. No such transfer occurred with regard to nonbanks.
5. Moreover, any lack of privilege protection for materials submitted to the CFPB created concerns of inconsistent regulation across financial institutions.
 - a. As the American Bar Association noted in a September 20, 2012 letter to the Senate Committee on Banking, Housing, and Urban Affairs in support of legislation to extend protection for privileged materials submitted to the CFPB ("September ABA letter"), "absent legislation, smaller financial institutions may share privileged materials with their consumer protection examiner without a risk of waiver, see 12 U.S.C. § 1828(x), while larger institutions

²¹ A detailed analysis of the Bureau and privilege is found in the American Bar Association's Letter *In Re: Bureau of Consumer Financial Protection Proposed Rule on Confidential Treatment of Privileged Information*; Docket No. CFPB-2012-0010; RIN 3170-AA 20, 77 Fed. Reg. 15286 (Mar. 15, 2012), American Bar Association (Apr. 12, 2012) ("April ABA letter").

face uncertainty when they share privileged materials with the Bureau.”²²

6. In an effort to resolve the issue, on March 15, 2012 the CFPB issued a proposed rule providing that the submission by any person of information to the Bureau in the course of the Bureau's supervisory or regulatory processes would not waive or otherwise affect any privilege such person may claim under Federal or State law, and clarifying that the Bureau's provision of privileged information to another Federal or State agency would also not waive any applicable privilege.²³
 - a. On July 5, 2012, the CFPB adopted the proposed rule without modification.²⁴
7. Concerns regarding the validity of the Bureau's position on privilege waiver remained. These concerns were addressed when, on December 20, 2012, the President signed legislation that added the CFPB as an enumerated agency under sections 1821(t) and 1828(x).²⁵

²² *Re: Support of S.3394 to Ensure Consistency Regarding Privileged Materials Submitted to the Consumer Financial Protection Bureau and Other Banking Regulators*, American Bar Association (September 20, 2012).

²³ *See Confidential Treatment of Privileged Information*, 77 Fed. Reg. 15286 (March 15, 2012).

²⁴ *See Confidential Treatment of Privileged Information*, 77 Fed. Reg. 39617 (July 5, 2012) (codified at 12 C.F.R. pt. 1070).

²⁵ To amend the Federal Deposit Insurance Act with respect to information provided to the Bureau of Consumer Financial Protection, H.R. 4014 (112th Cong., 2012).

C. Other Privilege Issues

1. *Authority to Require Provision of Privileged Materials:* The legislation on privilege waiver did not address whether the CFPB has the authority to *require* the production of privileged documents.
 - a. The April ABA letter also challenged the CFPB's assertion that it and the prudential regulators could require production of privileged documents. The letter noted that although banks often produce privileged materials to banking agencies, "the ABA is not aware of any reported Federal appellate court case holding that Federal banking regulators – or any other Federal agencies – can require production of privileged materials, nor do the Federal banking statutes contain such authority."²⁶
 - b. In response to comments regarding the proposed rule expressing concerns that the Bureau lacked the authority to compel privileged information, and the rule would not effectively preserve the privileged nature of information submitted to the Bureau, the CFPB stated that it "continues to adhere to the position that it can compel privileged information pursuant to its supervisory authority," and because the provision of such privileged information

²⁶ See April ABA letter, *supra* note 21.

to the Bureau is not voluntary, it does not result in a privilege waiver.²⁷

2. *Broad and/or Non-Supervisory Use:* Some have raised concerns that the CFPB will view the newly enacted privilege protections as an invitation to request privileged materials as a matter of course.

a. However, the CFPB has made repeated assurances that it will take a careful approach to requesting privileged materials, including that it will:

i. Request privileged materials only when the underlying “information is material to its supervisory objectives” and only when it “cannot practicably obtain the same information from non-privileged sources;²⁸

ii. give “due consideration” to any “request[] to limit the form and scope of any supervisory request for privileged information;²⁹

iii. make only “supervisory requests” for privileged information to advance only “supervisory objectives,” meaning

²⁷ See Confidential Treatment of Privileged Information, *supra* note 24 at 39619.

²⁸ Confidential Treatment of Privileged Information, *supra* note 24 at 39620. *See also* Bulletin 12-01, *supra* note 17 at 3.

²⁹ Confidential Treatment of Privileged Information, *supra* note 24 at 39620. *See also* Bulletin 12-01, *supra* note 17 at 3.

that requests for privileged materials will not be made in enforcement contexts;³⁰ and

iv. “not routinely share confidential supervisory information with agencies that are not engaged in supervision” and that it will “only in very limited circumstances” share such information “with law enforcement agencies, including State Attorneys General.”³¹

b. Going forward, the CFPB should also clarify unresolved questions including:

i. When, if ever, it will request privileged materials reflecting the advice or work product of outside counsel in an adversarial proceeding, such as civil litigation;

ii. When, if ever, it will seek materials relating to self-testing by supervised institutions. Such requests may discourage supervised institutions from engaging in self-testing.

³⁰ Confidential Treatment of Privileged Information, *supra* note 23 at 39620. *See also* Bulletin 12-01, *supra* note 17 at 2-3.

³¹ Confidential Treatment of Privileged Information, *supra* note 23 at 39621 (quoting Bulletin 12-01 at 5).

c. There are a host of additional reasons for the CFPB to limit its use of privileged material:

i. *The value of the privileges to supervised institutions and the CFPB:* The attorney-client privilege and work-product protections are of significant importance to regulated institutions, and encourage parties confronted with difficult legal problems to engage in candid and open communications with counsel. Frequent requests by the CFPB for privileged materials could chill institutions from seeking the guidance of counsel, to the detriment of the institutions and consumers alike.

ii. *Litigation risk for the CFPB.* Overreaching by the CFPB with respect to privileged materials could lead to litigation that would force a court to decide whether the CFPB may compel the production of such materials. Such a decision could also implicate the authority of the prudential banking regulators to compel the production of privileged materials.

D. Enforcement Attorneys at Exams

1. The CFPB's examinations have also diverged from traditional bank examinations by including enforcement attorneys. While this practice is apparently intended to increase the agency's efficiency (by allowing examiners to understand the role of enforcement, and enforcement attorneys to understand the examination process), it has raised legitimate concerns that the presence of enforcement attorneys has a chilling effect on the supervisory process by causing institutions to be less willing to share information freely with the agency.
2. In November of 2012, the CFPB Ombudsman noted concerns with this practice in its first annual report, and recommended that (1) the CFPB review implementation of the policy; and (2) until that review is complete, the CFPB should establish ways to clarify the Enforcement Attorney role in practice at the supervisory examination.
3. To date, the CFPB has not responded to the report's recommendations. CFPB staff have repeatedly stated, in response to industry concerns about the practice, that there is nothing to worry about because (1) the presence of enforcement attorneys does not mean the Bureau is any more likely to recommend enforcement and (2) prudential regulators routinely consult with enforcement staff on examination matters.