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LEGAL UPDATES

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# Texas Court Vacates CFPB's Revised UDAAP Exam Manual and Its New Anti-Discrimination Guidance

In a not-entirely-unexpected ruling, Judge J. Campbell Barker of the U.S. District Court for the Eastern District of Texas recently vacated the Consumer Financial Protection Bureau's (CFPB) updated Unfair, Deceptive, or Abusive Acts or Practices (UDAAP) exam manual, which sought to police "discrimination" in the financial services industry using a novel legal theory. The court's decision, which was determined on two alternative grounds, provides much needed relief to the financial services industry.

## **The updated UDAAP exam manual**

On March 16, 2022, the CFPB issued a revised UDAAP exam manual expressly stating that an act or practice that discriminates or results in discrimination is "unfair" under the bureau's UDAAP authority—representing a vastly new interpretation of a standard that has been set forth in the law for 80-plus years.

Notably, the CFPB stressed that, by defining acts and practices that discriminate or result in discrimination as "unfair," the bureau could reach certain acts or practices that might otherwise not be prohibited under the Equal Credit Opportunity Act (ECOA). For instance, while discrimination related to depository products might not be prohibited under ECOA (because, with some exceptions depending on their characteristics, deposit accounts are not "credit"), it could be prohibited as an unfair practice under UDAAP. In addition, the CFPB stated that it expected examiners to require covered entities to "show their processes for assessing risks and discriminatory outcomes, including documentation of customer demographics and the impact of products and fees on different demographic groups." The CFPB did not define "customer demographics." Needless to say, the new exam manual

represented an attempted substantial (and vague) expansion of the CFPB's authority to police "discriminatory" acts or practices.

## **The lawsuit**

Following the exam manual's release, the U.S. Chamber of Commerce and other plaintiffs sued the CFPB and its director, Rohit Chopra. According to Chamber of Commerce Executive Vice President and Chief Policy Officer Neil Bradley, "The Consumer Financial Protection Bureau is operating beyond its statutory authority and in the process creating legal uncertainty that will result in fewer financial products available to consumers." In particular, the plaintiffs argued that the new directive violated the Administrative Procedures Act because it represented a "legislative rule" requiring notice and comment rulemaking. Plaintiffs also argue that the Dodd-Frank Act did not give the CFPB the authority to regulate discrimination except under specific circumstances, such as through ECOA. Finally, the plaintiffs contended that the exam manual should be vacated because the CFPB's funding structure violates the United States Constitution's appropriations clause under binding Fifth Circuit Precedent.

The parties ultimately filed cross motions for summary judgment, and the court issued its decision granting the plaintiffs' motion on September 8, 2023.

## **The court's decision vacating the exam manual**

The court granted plaintiffs' motion for summary judgment on the grounds that, per the Fifth Circuit's decision in *CFSI v. CFPB*, the funding structure of the CFPB is unconstitutional.

It also granted plaintiffs' motion on the independent grounds that characterizing discrimination as "unfair" went beyond the CFPB's authority as defined by the Dodd-Frank Act. In so concluding, the court invoked the "major questions doctrine," stating that the issue of discrimination is of major economic and political significance. The court concluded that Congress rarely authorizes disparate-impact liability, and when it does, it does so in narrow circumstances to avoid constitutional questions.

## **What this means to you**

The Eastern District of Texas ultimately vacated CFPB's changes to the UDAAP manual, providing welcome relief to covered entities subject to the updated exam manual. This relief is especially welcome since, according to a July 11, 2023 motion for a status conference filed by the plaintiffs, "the CFPB recently announced that it is pursuing enforcement investigations based on its novel legal theory challenged in this case [and] [a]s time goes on, the irreparable harms to Plaintiffs' members—who must adopt costly compliance procedures to comply with the update—are piling up."

It is certainly our experience that the new UDAAP exam manual increased the level of regulatory uncertainty in the financial services industry and has resulted—and continues to result—in increased compliance costs. Unlike ECOA—which is limited in scope to credit products and applies to a defined set of protected classes—the definition of discrimination under the updated UDAAP manual has no apparent limiting principles. And this lack of limiting principles affects compliance and risk management: for instance, when analyzing data for potential disparate impact patterns, it becomes much more difficult to know what, exactly, to look for when disparities are not bound by a defined set of protected classes.

More encouraging still is the fact that the court decided in favor of the plaintiffs on alternative grounds. Thus, even if the United States Supreme Court rules in favor of the CFPB in the *CFSA* case, or even if it decides to find that the CFPB's funding structure is unconstitutional, but elects not to vacate prior agency action, the CFPB's new UDAAP exam manual will remain vacated.

**Contact us**

If you have questions regarding this decision or the CFPB's UDAAP authority, please contact Christopher Friedman, Marci Kawski, Alex McFall, or your Husch Blackwell attorney.