



Consumer Financial  
Protection Bureau

# Road Map To CFPB Compliance For The Auto Finance Industry

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LOEB & LOEB Adds Value



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# Overview

CFPB – The Basics

CFPB Authority, Purpose, Oversight and News

CFPB Auto Finance Complaint Database/Company Portal Update

Regulatory Focus On Auto Financing

CFPB's First Party Collection Requirements

CFPB's First Auto Lending Enforcement Action

CFPB Auto Lending Enforcement: What's Next?

Preparing For Regulatory Scrutiny

The Compliance-Readiness Approach

Indirect Lending Example: Compliance-Readiness

Compliance Readiness Approach to Fair Lending Issues

Takeaways

Questions?



## CFPB – The Basics

- Washington's newest federal agency
- Created by the Dodd-Frank Act of 2010
- Separately-funded directly by the Federal Reserve
  - 2013 annual budget: **\$598 million**
  - Independent of the Congressional appropriation process
  - Can use civil penalties for consumer restitution, education
  - Civil penalties collected to date: \$61.5 million
  - Headed by a single Director appointed by the President
- More than 1,225 employees to date
  - CFPB's Plan: 1,350 by 2013 fiscal year end
  - **About half assigned to supervision/enforcement**
  - **90% of those are attorneys and paralegals**



# CFPB Supervisory Authority

## Large Banks

- Authority to supervise banks, thrifts and credit unions with **over \$10 billion in assets** (as well as their affiliates and certain service providers) to assess their compliance with Federal consumer financial law, evaluate their compliance management systems, and detect and assess risks to consumers and markets for consumer financial products and services.

## Nonbanks

- Authority to supervise certain nonbank consumer financial services companies. CFPB's nonbank supervision authority includes all mortgage originators, mortgage servicers, private education lenders, and payday lenders.
- Authority to supervise nonbanks that are "larger participants" in other markets for consumer financial products or services, as defined by rule.
- Authority to supervise other nonbank covered persons the Bureau finds are engaged or have engaged in conduct that poses a risk to consumers with regard to consumer financial products or services.



# CFPB's Purpose

- Primary rulemaking, supervisory and enforcement authority over entities that offer consumer financial products and services
  - Includes banks and “covered” non-banks
- Responsible for ensuring that markets for consumer financial products and services are **fair, transparent** and **competitive**



# CFPB Oversight

## Oversees “covered persons” and “service providers”

### “Covered Person”

Any entity that offers or provides “consumer financial products or services”

### “Service Provider”

“Any person that provides a **material service** to a covered person in connection with the offering or provision by such covered person of a consumer financial product or service.”

Includes all providers of outsourced services:

- Marketers
- Debt collectors
- Repossessors
- Dealers?



## Recent Developments:

- CFPB Director confirmed by the Senate – **July 2013**
  - Confirms the Bureau's authority to engage in Rulemaking, Supervision and Enforcement!
- Collections Industry Consumer Complaints added to CFPB Complaint Database – **July 2013**
- Guidance Issued on Applicability of FDCPA to Parties Collecting Debts on Their Own Behalf – **July 2013**
- Guidance Regarding Use of Proxies in Analyzing Fair Lending Practices – **Aug. 2013**
- Guidance on Duty to Investigate Disputed Credit Information Furnished by Lenders – **Sept. 2013**

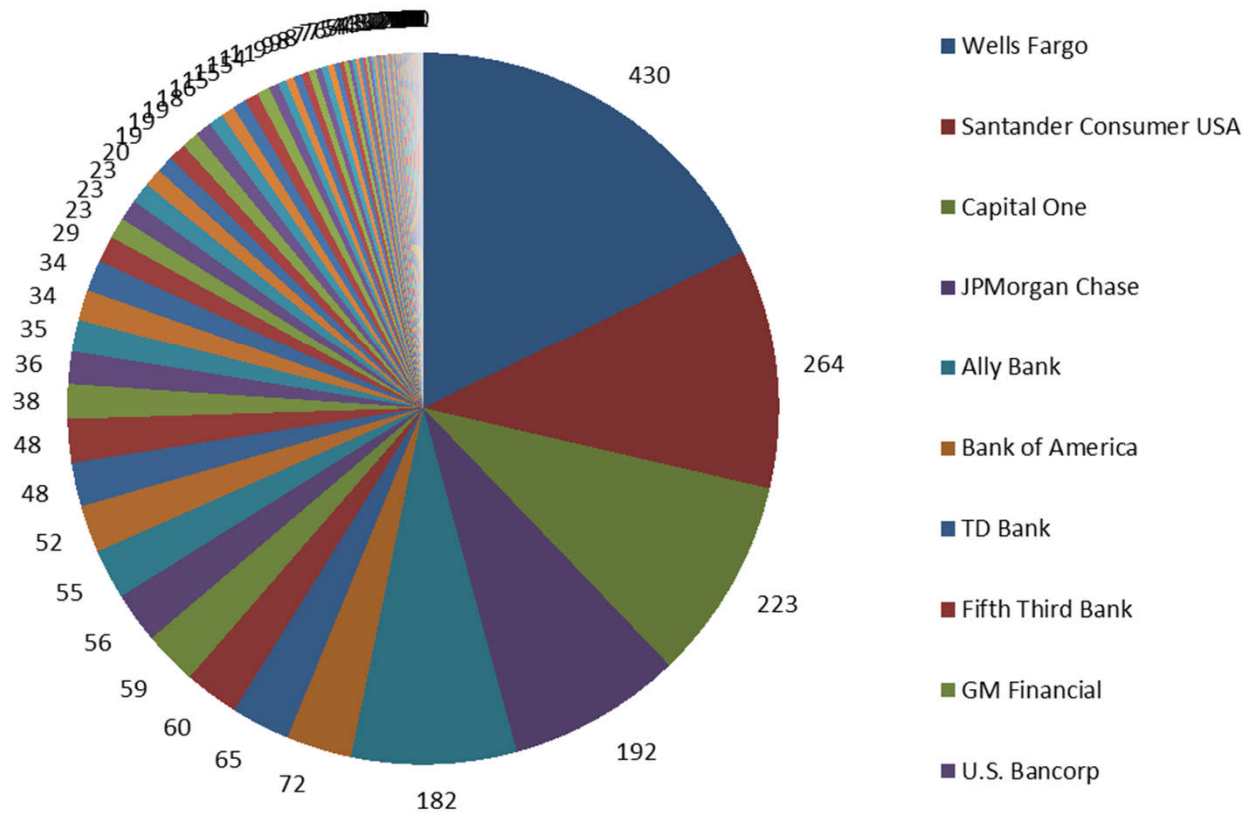




# CFPB Auto Finance Complaint Database

## CFPB Database - Auto Finance Complaints

As of Aug. 27, 2013



# Company Portal Response Guidance Update

## Supplemental CFPB Guidance issued June 2013

- **Company responses should address:**
  - **Application of customer's payments to the loan**
    - Should attach any contract or agreement on which you rely for your response to the consumer \*
    - Should include a copy of the customer's payment history \*
    - Should include any relevant account statements for the period in question \*
  - **Fees or late charges:**
    - Include any contract or agreement on which you rely for your response to the consumer \*
    - Include any applicable fee schedule \*
    - Include any related notices and/or disclosures provided to the consumer \*
    - Include any account statements for the time period in question \*

**\* Include as attachment(s) to the response**



# Company Portal Response Guidance Update

- **Repayment options:**

- Include any loan agreement and other documents signed by consumer \*
- Include any other contract or agreement on which you rely for your response to the consumer \*
- Include any related notices and/or disclosures provided to the consumer, including at the time of consummation \*
- Include any information about options available to the consumer for repayment, if applicable \*
- Contact information for the relevant bank representative
- Include customer's payment history, if relevant to the complaint \*

- **Unlawful discrimination alleged:**

- Include relevant company policy or procedures \*
- Include any correspondence between the consumer and the company \*
- Include any applications or agreements \*

**\* Include as attachment(s) to the response**



# Regulatory Focus On Auto Financing

## 1. FTC's 2011 Auto Financing Workshops

- Undisclosed dealer markups/discretion/discriminatory pricing
- “Payment packing,” “deal packing,” “power booking,” negative equity included in new loans
- Communication methods (autodialers, text messaging)
- Collection/repossession methods

## 2. 2012 DriveTime investigation

- CFPB Director promised “Buy Here Pay Here” scrutiny in Jan. 2012
- CID issued to “Buy Here Pay Here” dealer in Apr. 2012
- No enforcement actions filed to date
- Coming soon?



# Regulatory Focus On Auto Financing

## 3. Fair Lending Practices Investigations

- Ally Bank March 2013 disclosure: under investigation
- *Bloomberg/WSJ reports*: CID's issued to banks, auto manufacturer financing arms
- Justice Department focus: **discretionary pricing** by dealers as potential ECOA violations
- CFPB focus: **add-on products** (warranties, insurance) as potential UDAP violations
  - Adequacy of price disclosures?
  - Misrepresentations?



# Regulatory Focus On Auto Financing

## 4. CFPB Bulletin 2013-02 (March 2013)

- “Indirect Auto Lending and Compliance with the Equal Credit Opportunity Act”
- CFPB to hold auto loan finance companies responsible for discriminatory practices by dealers
  - Based on the “disparate impact test” – statistical discrimination
  - Ostensibly results from dealer discretion in loan pricing
  - Subject to legal challenge!
- Requires lenders to “take appropriate measures”:
  - Impose controls on dealer markup and compensation
  - **Eliminate dealer discretion to mark up buy rates?**
  - Collect and analyze data for potential disparities



# Regulatory Focus On Auto Financing

## CFPB's Fair Lending Compliance "Must-Have's"

1. Up-to-date fair lending *policy statement*.
2. Regular *fair lending training* - employees, officers, Board members
3. ***Compliance monitoring*** - policies for reducing fair lending risk.
  - For example, controls on ***dealer discretion***.
4. ***Review of lending policies*** for potential fair lending violations
  - For example, potential disparate impact.
5. ***Analyze loan data*** for disparities on a prohibited basis in pricing, underwriting, or other aspects of the credit transaction.
6. Regular ***evaluation of loan marketing***.
7. Meaningful ***oversight by management and the board of directors*** of fair lending compliance.



# Regulatory Focus On Auto Financing

## 5. First Party Debt Collection Bulletin (2013-07)

- CFPB notifies companies that “covered persons” that collect their own debts must comply with Fair Debt Collection Practices Act (FDCPA) prohibitions
- Even though the FDCPA does not apply to “first party” collectors, FDCPA violations will be treated as UDAAP violations





# CFPB's First Party Collection Requirements

In collecting debts, “Covered Persons” cannot:

- Collect a debt (incl. interest, fees or other charges) not authorized by an agreement or permitted by law.
- Fail to post payments on a timely basis or credit timely payments to a consumer’s account and charge late fees.
- Take possession of property without the legal right to do so.
- Reveal the consumer’s debt, without the consumer’s consent, to the consumer’s employer and/or co-workers.
- Falsely represent the character, amount, or legal status of the debt.
- Misrepresent that a debt collection communication is from an attorney.



# CFPB's First Party Collection Requirements

In collecting debts, “Covered Persons” cannot:

- Misrepresent that a communication is from a government or government-affiliated source.
- Misrepresent if information about a payment or nonpayment will be furnished to a credit reporting agency.
- Misrepresent to consumers that their debts will be waived or forgiven if they agree to accept a settlement offer.
- Threaten any action that the collector does not intend to take.
- Threaten any action that the collector does not have authority to pursue, including false threats of lawsuits, arrest, prosecution or imprisonment for non-payment of a debt.



# CFPB's First Auto Lending Enforcement Action

## U.S. Bank/Dealers' Financial Services – June 2013

- Agreed to pay restitution of at least **\$6.5 million** to service members in connection with automobile loans offered through their Military Installment Loans and Educational Services (MILES) program:
  - U.S. Bank liability: \$3.2 million or more
  - DFS liability: \$3.3 million
- Alleged inadequate disclosures, improper marketing associated with:
  - Failure to disclose fees and payment schedules associated with loans, misleading marketing of costs and coverage of add-on products (vehicle service contracts, GAP insurance policies)
- Bureau said USB's and DFS's cooperation was taken into consideration in avoiding higher penalties.



# CFPB Auto Lending Enforcement

## What's Next?

- DriveTime/“Buy Here, Pay Here” action?
- Dealer discretionary pricing action (ECOA)?
- Add-on product marketing (U.S. Bank/DFS)?
- FDCPA/UDAAP collection violation?
- FCRA credit furnishing/reporting violation?



# Preparing for Regulatory Scrutiny

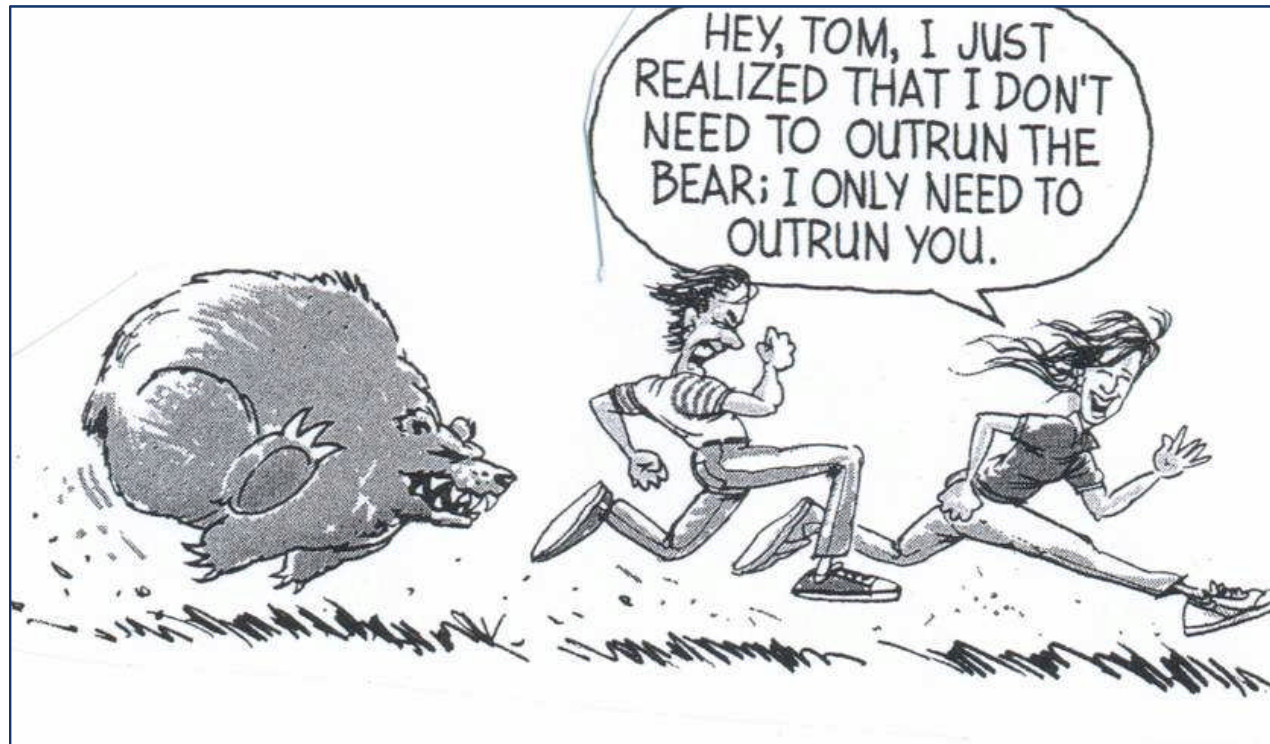
Regulatory scrutiny will happen!

What do you need to do to be ready?

- You don't have to be perfect!
- Just be able to demonstrate you are working at it!



# Preparing for Regulatory Scrutiny



# Preparing for Regulatory Scrutiny

## “Compliance-readiness” approach:

1. Understand the applicable laws.
2. Create appropriate policies and procedures.
3. Train your employees to implement those policies.
4. Monitor your compliance.
5. Listen to the market!
  - Create a “market feedback loop”

**Document each step!**



# Indirect Lending Example: Compliance Readiness

- Indirect auto lenders (those who loan through dealers) are likely “creditors” under ECOA
  - Statutory definition of “creditors” is very broad
  - ECOA defines “creditors” as **those who regularly participate in a credit decision**, including setting the terms of the credit
  - Standard lending practices of indirect auto lenders likely constitute participation in a credit decision

Source: Patrice Ficklin Fair Lending Director, CFPB

- Federal Reserve webinar (August 6, 2013)





# Indirect Lending Example: Compliance Readiness

## Dealer Markup and Fair Lending Risk

- CFPB view: Giving dealers discretion to set loan terms (dealer markup) is a source of fair lending risk based on research and prior litigation.
- Could result in disparities based on race, national origin and other prohibited bases.
- Markup policies that permit dealer-level or portfolio-wide disparities on prohibited bases could violate ECOA.



# Indirect Lending Example: Compliance Readiness

## Alternative Methods of Compliance

1. Impose controls on dealer markup and compensation policies.
  - Requires lenders to monitor and address the effects of such policies through:
    - Dealer communications
    - Regular analysis
    - Prompt corrective action
    - Consumer remuneration
2. Or, eliminate dealer discretion.
  - Requires flat fee or other non-discretionary compensation method.



# Indirect Lending Example: Compliance Readiness

## How Do Regulators Examine for Violations?

- Guidance Provided by the 2009 Interagency Fair Lending Examination Procedures:
  1. Look for the following risk factors:
    - Complaints/lawsuits
    - Policies/procedures allowing discretion in pricing and/or exceptions
    - Compensation based on terms/conditions of the loan
    - Loan data indicating pricing disparities on a prohibited basis.



# Indirect Lending Example: Compliance Readiness

## How Do Regulators Examine for Violations?

2. Determine borrower's race, ethnicity and gender.
  - Race/ethnicity – use U.S. Census data to geocode loans to determine the predominant minority populations in borrower's living area.
  - Ethnicity (Hispanic) – use surnames of borrowers based on U.S. Census list of common Spanish surnames.
  - Gender – apply U.S. Census list of common female and male first names to first names of all single borrowers.



# Indirect Lending Example: Compliance Readiness

## How Do Regulators Examine for Violations?

3. Compare pricing of loans between various populations:
  - Race/ethnicity – Compare pricing of loans in areas with predominantly minority populations against loans in predominantly non-minority areas.
  - Ethnicity (Hispanic) – Compare pricing of loans to Hispanics against loans to non-Hispanics.
  - Gender – Compare pricing of loans to single female borrowers against loans to single male borrowers.



# Indirect Lending Example: Compliance Readiness

## Federal Reserve's Advice to Mitigate Fair Lending Risk:

1. Review and address pricing discrimination complaints.
2. Review policies, procedures, rate sheets and dealer agreements to determine level of dealer discretion in loan pricing.
3. Review dealer agreements to determine if financial incentives are based on the price of the loans
4. Provide training to relevant parties.



## Indirect Lending Example: Compliance Readiness

### Federal Reserve's Advice to Mitigate Fair Lending Risk:

5. If there is elevated risk and sufficient volume, perform a statistical analysis of the loans.

- Compare by predominant minority, ethnicity and gender
- Compare loan pricing of various categories against one another: with markups, with negative markups (markdowns) and with no markups.
- Compare loan pricing both within dealers and across dealers.
- Perform these analyses on a quarterly basis, looking back at the previous one-year period.



# Indirect Lending Example: Compliance Readiness

## Federal Reserve's Advice to Mitigate Fair Lending Risk:

### 6. Address any unexplained disparities:

- Make offers of restitution to consumers
- Change policies and procedures
- Change dealer agreements





# Compliance-Readiness Approach to Fair Lending

1. Understand the ECOA requirements for auto finance companies.
2. Implement policies and procedures based guidance provided by the CFPB/other regulators:
  - Evaluation of discriminatory pricing complaints
  - Review of discretionary pricing programs
  - Review of dealer incentives based on loan pricing
  - Statistical evaluation of loans with elevated risk
  - Responses to unexplained disparities



# Compliance-Readiness Approach to Fair Lending

3. Implement internal and external training to ensure that the policies and procedures are rolled out to all relevant personnel.
  - Document all training, including materials, testing and any follow up with particular employees, groups.
4. Monitor execution of compliance steps.
  - Document evaluation of complaints, policies, agreements, incentives, statistical loan reviews and follow-up/remediation measures.



# Compliance-Readiness Approach to Fair Lending

5. Monitor the “voice of the market.”
  - Open channels of communication with actual borrowers as well as with those who are denied:
    - Website, customer service, surveys
    - Complaints, other customer interactions
  - Track external sources of consumer communications
    - CFPB’s Company Portal
    - Communications from other regulators
    - BBB, other consumer complaint websites
  - **Document/Follow-up/Resolve/Report !**



# Takeaways

1. The CFPB is now fully functional and operating in all three of its spheres: Rulemaking, Supervision and Enforcement.
2. The Bureau is issuing a steady stream of guidance on auto lending issues that must be monitored and incorporated into operations and procedures.
3. Lenders need to scrutinize complaints, policies and procedures, agreements and disclosures for a wide range of issues, including dealer pricing, add-on products, collections.
4. The Compliance Readiness approach is an effective way to address the CFPB's compliance expectations.
5. The most important step in the Compliance Readiness approach is documenting the measures you are taking and maintaining that documentation in a form that can easily be produced.



# Questions?



# Thank You!

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Please email me if you would like to be added to our list for periodic alerts on CFPB and FTC developments and other issues relevant to consumer financial companies.



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