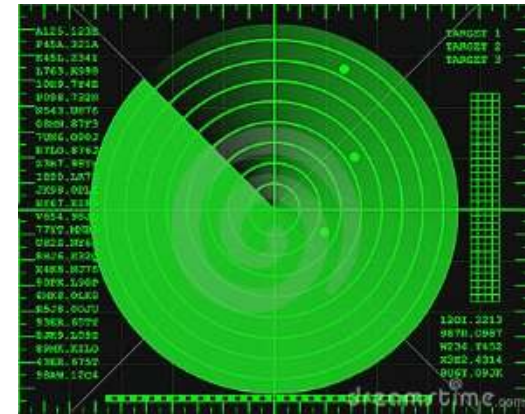


Auto Lending Compliance: Staying Off The Regulators' Radar Screen



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Overview

- The Current Regulatory Climate
- About the CFPB
- Finance Company Liability for Service Providers
- First CFPB Enforcement Actions
- Regulator Interest in Auto Financing
- CFPB: A Different Kind of Regulator
- Preparing for Regulatory Scrutiny
- Compliance-Readiness Approach
- Company Portal Example
- CFPB Authority: Does Any of This Still Matter?
- Takeaways
- Questions?



The Current Regulatory Climate

Old “Friends”



Source: United States Federal Trade Commission, www.ftc.gov



The Current Regulatory Climate *(continued)*

And New!

cfpb

Consumer Financial
Protection Bureau

Source: Consumer Financial Protection Bureau, consumerfinance.gov



About the CFPB

- The Consumer Financial Protection Bureau
- Washington's newest federal agency
- Created by the Dodd-Frank Act of 2010
- Separately funded directly by the Federal Reserve
 - 2013 annual budget: **\$541 million + civil penalties**
 - Independent of the Congressional appropriation process
 - Can use civil penalties for consumer restitution, education
 - Civil penalties collected to date: \$57.7 million (**\$600 million**)
- Headed by a single director appointed by the president
- More than 1,100 employees to date
 - CFPB's Plan: 1,350 by 2013 fiscal year end
 - **About half are assigned to supervision/enforcement**
 - **90% of those are attorneys and paralegals**



CFPB's Purpose

- The 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**



Consumer Financial
Protection Bureau

Source: Consumer Financial Protection Bureau, consumerfinance.gov



Key Definitions

- “Consumer financial product or service”
 - Includes extending credit, servicing or brokering loans, real estate services, deposits, stored value, check cashing, payment processing, credit report and debt collection
- “Covered persons”
 - Entities that offer or provide “consumer financial products or services” **as well as their service providers**



“Covered Persons”

Any person or entity that offers or provides a “consumer financial product or service”

Includes:

- Banks, thrifts, and credit unions with assets over \$10 billion
- [Consumer finance lenders](#)
- Mortgage loan originators
- Loan servicers and brokers
- Currency exchanges
- Real estate settlement companies
- Appraisers and appraisal/appraisal management companies
- Consumer credit reporting agencies
- Debt collectors
- Debt settlement and debt management services
- Check cashing, collection and guaranty services
- Lenders and brokers in certain lease-to-own arrangements



“Covered Persons” *(continued)*

- Financial and investment advisors that are not registered with the SEC
- Payday lenders
- Credit counselors
- Broker-dealers, non-depository trust companies and deposit intermediation services
- Money services businesses, wire and money transmitters
- Certain sellers or issuers of stored value cards and instruments
- **Auto dealers are expressly excluded**
- **However, service providers are “covered persons”**



Finance Company Liability for Service Providers

A “Service Provider” is:

- “[A]ny 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”
12 U.S.C. § 5481(26).

Includes all providers of outsourced services:

- Dealers?
- Marketers
- Debt collectors
- Repossessors



Finance Company Liability for Service Providers

(continued)

Supervised banks and nonbanks must manage the risks of service provider relationships, including:

- Must verify that service provider understands and is **capable of complying** with Federal consumer financial laws
- Must request and **review service provider's policies, procedures, internal controls, and training materials**
- Must take steps to ensure service provider conducts **appropriate training** and **oversight** of its employees or agents

Source: CFPB Bulletin 2012-03 (April 12, 2012)



Finance Company Liability for Service Providers

(continued)

- **Service provider contracts** should include:
 - Clear expectations about the service provider's compliance requirements
 - Appropriate and enforceable consequences for violation of compliance-related responsibilities
- Must establish **internal controls and ongoing monitoring** to determine whether the service provider is complying with Federal consumer financial law
- Must take **prompt action** to respond to any problems identified through the monitoring process

Source: CFPB Bulletin 2012-03 (April 12, 2012)



First CFPB Enforcement Actions

Credit Card Company Settlements:

Capital One Bank – July 2012

- Agreed to pay **\$210 million** in fines and restitution in July 2012
- CFPB alleged deceptive telemarketing **performed by third parties** of “**add-on**” **credit card products** (payment protection programs, death and disability programs, credit monitoring, including identity theft protection, etc.)
- Claimed deceptive marketing practices included:
 - Misinformed consumers about the costs
 - Deceived consumers about the nature of the products
 - Misled consumer about their eligibility for and the benefits of the products
 - Misled consumers about the benefits
 - Enrolled consumers without their consent



First CFPB Enforcement Actions *(continued)*

Discover Bank – September 2012

- Agreed to pay **\$214 million** in fines and restitution
- Alleged deceptive telemarketing **performed by third parties** of **add-on credit card products** (payment protection, credit score monitoring, identity theft protection and credit card cancellation services)
- Alleged deceptive marketing practices included:
 - Misled consumers about the fact that there was a charge for the products
 - Misled consumers whether they had purchased the products
 - Enrolled consumers without their consent
 - Withheld material information from consumers about eligibility requirements for certain benefits



First CFPB Enforcement Actions *(continued)*

American Express – October 2012

- Agreed to pay **\$112.5** million in fines and restitution
- Violations by bank, affiliates and **third party affiliates** from 2003 to spring 2012
- FDIC shared results of February 2011 examination with CFPB
- Alleged violations included:
 - Deceptive Marketing Practices in Sale of Credit Cards (Unfair, Deceptive and Abusive Practices/UDAAP)
 - Age Discrimination (Equal Credit Opportunity Act/ECOA)
 - Unlawful Fees (Truth in Lending Act/TILA, Credit Card Accountability Responsibility and Disclosure Act/CARD)
 - Failure to Report Customer Disputes (Fair Credit Reporting Act)
 - Deceptive Debt Collection Practices (Fair Debt Collection Practices Act)



Follow-on Derivative Shareholder Actions

Post-CFPB Settlement Shareholder Actions:

- Capital One Bank (Virginia state court)
 - Breach of loyalty, corporate waste, unjust enrichment
- Discover (N.D. Illinois federal court)
 - Breach of fiduciary duty, corporate waste, unjust enrichment
- American Express (New York state court)
 - False and misleading statements, failure to maintain internal controls, failure to properly oversee and manage company, unjust enrichment, abuse of control and gross mismanagement



CFPB Enforcement Penalties

Statutory Penalties:

- First Tier – violation of a law, rule, final order or CFPB-imposed condition
 - Up to \$5,000 for each day violation continues
- Second Tier – **reckless** violation of a Federal consumer financial law
 - Up to \$25,000 for each day violation continues
- Third Tier – **knowing or intentional** violation of a Federal consumer financial law
 - Up to \$1,000,000 for each day violation continues



CFPB Enforcement Penalties *(continued)*

Criminal Penalties:

- CFPB must notify U.S. Attorney General if evidence of violations of federal **criminal** laws discovered
- May 7, 2013: CFPB announced a joint civil/criminal action against owner of a New York debt settlement company
 - Alleged conspiracy to commit wire and mail fraud
 - Owner, employees subject to arrest warrants
 - Government executed forfeitures of owner's restaurant, 28 bank and credit union accounts
 - Coordinated investigation with U.S. Postal Inspection Service



CFPB Enforcement Penalties *(continued)*

Equitable and Injunctive Remedies:

- Rescission or reformation of contracts
- Restitution - refund of monies or return of real property
- Disgorgement - compensation for “unjust enrichment”
- Public notification regarding the violation, including all costs of notification
- Limitations on the activities or functions of the person
- Other monetary relief
- Recovery of government's attorney's fees and costs



CFPB Enforcement Actions

Who Can Be Liable?

- Include those who provide “substantial assistance” to a covered person in engaging in an “unfair, deceptive or abusive act”
 - Directors, officers or employees charged with managerial responsibility
 - Controlling shareholders
 - Agents
 - Affiliates/other related entities
 - **Service providers**



Regulator Interest In Auto Financing

FTC's 2011 Auto Financing Workshops

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

CFPB's 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



Regulator Interest In Auto Financing *(continued)*

CFPB Bulletin 2013-02 (March 2013)

- “Indirect Auto Lending and Compliance with the Equal Credit Opportunity Act”
- CFPB warning that it will 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!
- CFPB: Requires lenders to “take appropriate measures”
 - Impose controls on dealer markup and compensation
 - **Read: Eliminate dealer discretion to mark up buy rates?**
 - Collect and analyze data for potential disparities
 - **What data do you analyze?**



Regulator Interest In Auto Financing *(continued)*

Current Fair Lending Practices Investigations

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



Regulator Interest In Auto Financing *(continued)*

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

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



The FTC's Regulatory Focus

- Dodd-Frank granted dual enforcement authority both to the CFPB and the FTC
- FTC still enforces:
 - Section 5 – “Unfair or deceptive acts or practices”
 - All FTC laws/regulations (i.e. Telemarketing Sales Rule)
 - All CFPB laws and regulations
- FTC's Sentinel Complaint System:
 - Banks/Lenders: #2 of Top 10 Consumer Complaints
 - Auto-Related: #7 of Top 10 Consumer Complaints
- Retained enforcement authority over dealers!



The States' Regulatory Focus

- Tight Economy → Pressure to Generate **REVENUE\$**
- CFPB Authority Questions → Opportunity for States?
- Joint enforcement encouraged by Dodd-Frank
 - Authorizes state claims based on CFPA violations
 - UCL actions based on CFPA violations?
 - First Joint CFPB/state action already brought in FL
- Enforcement authority over auto dealers!



CFPB: A Different Kind of Regulator

- Consumer focus ➔ **complaint-driven**
 - Debt collection naturally generates complaints!
- Broad legal jurisdiction
 - UDAAP, fair lending, electronic transactions, FDCPA and more
- Extensive powers
 - Rulemaking, supervision & enforcement actions
 - Damages, civil penalties & injunctive relief
- Commitment to transparency
 - Provides excellent guidance – Supervision Manual
 - But...no excuse for not being ready!



CFPB Supervision Manual: The Rules of the Road

- Available on the CFPB's website:
[consumerfinance.gov](https://www.consumerfinance.gov)
- 924 pages covering all areas of CFPB jurisdiction
- Key compliance sections:
 - Compliance Management Systems
 - UDAAP – Unfair, Deceptive or Abusive Practices
- Numerous other provisions that apply to consumer lending
 - Fair lending practices (ECOA)
 - Debt collection (FDCPA)
 - Electronic transactions (EFTA)



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 *(continued)*



“Hot Issues” That Will Draw Scrutiny

- Add-on products
- Fair lending – disparate impact
- Telephone/text message communications
- FDCPA compliance – stale debts
- Collection using social media
- Secret phone recordings



Preparing for Regulatory Scrutiny *(continued)*

“Compliance-readiness” steps:

- Understand the applicable laws
- Create appropriate policies and procedures
- Train your employees to implement those policies
- Document your compliance
- Listen to the market!
 - Create a “market feedback loop”



Illustrating The Compliance Readiness Approach

CFPB's "Company Portal" program

- Secure web link between a company and the CFPB
- CFPB forwards consumer complaints to company
- Allows company to provide "real-time" responses
- Consumers can track their complaints to resolution
- CFPB evaluates respective positions, determines if follow up is needed
- Companies "control their own destiny," as full participants in an open process



What is the Company Portal?

HOME INSIDE THE CFPB GET ASSISTANCE PARTICIPATE LAW & REGULATION

[SUBMIT A COMPLAINT](#)

HOMEASK CFPBAUTO LOANSMY CAR HAS BEEN REPOSSESSED, AND I WAS TOLD IT ...



AUTO LOANS

My car has been repossessed, and I was told it will be sold. What can I do?

UPDATED SEPT. 3, 2012

Under state law, a lender must notify you of a private or public sale. If your vehicle will be sold at a public sale, you have the right to bid on the vehicle. If a private sale will be made, you have the right to pay the full loan amount and the repossession costs and have the car returned to you. You may have other rights and obligations under state law.

GET HELP

[Submit a Auto Loan complaint](#)

We'll forward your issue to the company, give you a tracking number, and keep you updated on the status of your complaint.

[Tell us your story, good or bad, about your experience with consumer financial products.](#)

MORE INFORMATION ON

[repossession](#)

[f](#) [t](#) [e](#) [p](#) Print

THIS ANSWER WAS

[Helpful](#) [Too long](#)

[Confusing](#) [Incorrect](#)

[About these answers](#)



What is the Company Portal? *(continued)*

GET HELP

Submit a Auto Loan complaint

▶ We'll forward your issue to the company, give you a tracking number, and keep you updated on the status of your complaint.

Tell us your story, good or bad, about your experience with consumer financial products. ◀



What is the Company Portal? *(continued)*



[Log in](#)

File a vehicle loan or consumer loan complaint

We'll forward your issue to the company, give you a tracking number, and keep you updated on the status of your complaint.

1. **What happened?**
2. Desired resolution
3. My information
4. Product information
5. Review

Describe what happened so we can understand the issue... *

4000 characters remaining

[Form trouble?](#)
[Chat now.](#)



Source: Consumer Financial Protection Bureau, consumerfinance.gov

What is the Company Portal? *(continued)*

1. What happened?
2. Desired resolution
3. My information
4. Product information
5. Review

Describe what happened so we can understand the issue... *

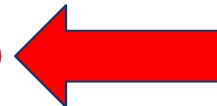
4000 characters remaining

[Form trouble?](#)
[Chat now.](#)

My loan is a(n) *

Do you believe the issue involves discrimination? (Optional)

Yes No



Source: Consumer Financial Protection Bureau, consumerfinance.gov

Implementing Company Portal Participation

- Understand program rules, procedures (“the law”)
 - CFPB’s “Company Portal Manual”
- Prepare appropriate policies and procedures
 - Assign responsibility
 - Actions required
 - Responses to CFPB – 15 days / 60 days
 - Communications with consumers
 - Deadlines for responses
 - Tracking, monitoring, reporting complaints, responses and resolutions
- Implement employee training on procedures
 - Create training and testing materials
 - Document completion of training and/or retraining



Implementing Company Portal Participation

(continued)

- Create your own consumer complaint “feedback loop”
 - Track your execution of “Company Portal” procedures
 - Track consumer complaints from all available sources:
 - BBB websites
 - Nielsen “Buzz alerts”
 - Google alerts
 - Consumer websites (scambusters.org, etc.)
 - Analyze the data obtained
 - Identify patterns
 - Resolve complaints
 - Revise procedures in response to ineffective or unresolved issues



Illustrating The Compliance Readiness Approach

Participating in the Company Portal program:

- Opens a communication channel with the CFPB
- Signals company's willingness to cooperate
- CFPB's short deadlines encourage faster resolutions
- Transparent process allows CFPB to observe company's proactive responses to complaints
- Allows you know what the CFPB (and other agencies) know about you!



“Company Portal”: Bottom Line

Upsides:

- Establish a good relationship with the CFPB
- Know what regulators know about your complaints
- “Real time” opportunity to respond

Downsides:

- If you do a poor job of responding to complaints ... you’re going to have problems no matter what!
- Don’t say anything that you wouldn’t want to read in the papers



CFPB Authority: Does Any of This Still Matter?

Noel Canning v. National Labor Relations Board

- Court of Appeals for the District of Columbia (Feb. 2013)
- Held President Obama’s “recess appointments” of three NLRB board members on January 4, 2012 “**constitutionally invalid**”
 - Found that the U.S. Senate was in session on that day
- CFPB Director Cordray was also appointed that same day
- If the Court’s ruling is upheld and applied to the CFPB:
 - The Bureau’s powers could be substantially curtailed
 - Many of its 2012 actions, including some of its new rules and enforcement actions, could be overturned
- NLRB has appealed to the U.S. Supreme Court



CFPB Authority: Does Any of This Still Matter?

(continued)

State Natl. Bank of Big Spring v. Timothy Geithner

- Filed in District of Columbia federal court (July 2012)
- Challenges:
 - Constitutionality of the CFPB Structure
 - Lack of accountability to Congress and the President
 - Unsupervised appropriations process
 - Single director vs. Commission structure
 - “Recess Appointment” of the CFPB’s Director
 - Significant, since many of the CFPB’s powers were designed to commence upon the Director’s appointment
 - Claimed “end run” around Congressional approval (“checks and balances”)
- Motion to dismiss pending before District Court



CFPB Authority: Does Any of This Still Matter?

(continued)

If the CFPB Director's appointment is **unconstitutional**:

- Bureau's powers will be limited until a Director can be properly appointed:
 - Can only make rules under pre-existing laws that were transferred to the CFPB's authority
 - Can supervise banks over \$10B in assets

- Until a Director is appointed, the CFPB cannot:
 - Make any new rules or bring enforcement actions based on its UDAAP authority
 - Supervise non-bank entities (or their service providers)



What Does That Mean for Supervised Entities?

- If the Director's appointment is overturned, "covered" businesses have **more time to prepare**
- If the Director's appointment is upheld, the Bureau will likely increase its activity, including bringing **many more enforcement actions** against businesses and their service providers
- Either way, the CFPB is not going away and providers of consumer financial products and services (**and their service providers**) will have to comply with the Bureau's rules



Takeaways

- There are now **52** sets of regulators out there
- The CFPB is a new and different kind of regulator
- Bureau's transparency requires better preparation
- "Compliance readiness" approach is needed to meet the CFPB's compliance expectations
- CFPB's Supervision Manuals provide a wealth of information for compliance management and preparedness
- Lenders must scrutinize their policies and disclosures for dealer pricing and add-on product sales
- Financial service companies are responsible if their products or services harm consumers
 - Whether caused by your employees or not!



Takeaways *(continued)*

- Lenders must supervise their service providers:
 - Vet them upfront to ensure they understand and are capable of complying with the law!
 - Request and review their policies, procedures, internal controls and training materials
 - Make sure they conduct appropriate training and oversight of their employees and agents
 - Develop your own policies, procedures, internal controls and training materials guiding your supervision of your service providers
 - Document the steps you take to supervise your service providers!



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.

