



Morgan Lewis

LATEST DEVELOPMENTS IN AUTOMOTIVE FINANCE AND CONSUMER PROTECTION

July 19, 2023

David I. Monteiro
Allen Denson
Marcos D. Sasso

Presenters



David I. Monteiro
Partner, Dallas



Allen Denson
Partner, Washington, DC



Marcos D. Sasso
Of Counsel, Century City

Morgan Lewis

Table of Contents

- Section 01 – Introductions
- Section 02 – Consumer Financial Protection Bureau (CFPB) Supervisory Priorities
- Section 03 – FTC Automotive & Mobility Finance Priorities
- Section 04 – Dealer Oversight Expectations
- Section 05 – Credit Acceptance CFPB Litigation
- Section 06 – California GAP Waiver Laws
- Section 07 – Litigation Relating to Holder Rule
- Section 08 – Litigation Unique to Pandemic
- Section 09 – Key Takeaways
- Section 10 – Questions

CFPB Supervisory Priorities

Morgan Lewis

Overview – CFPB State of Play

- Agency faces multiple challenges across multiple industries due to CFSA litigation and resulting challenges to agency authority.
- Continued reliance on blog posts and supervisory highlights to accomplish regulatory priorities.
- Heavy emphasis on “junk” fees across all industries, including auto finance.
- Reduced number of enforcement investigations by volume, but many large-dollar settlements of investigations.

Recent CFPB Supervisory Priorities

- The CFPB continues to examine auto loan servicing activities, primarily to assess whether entities have engaged in any unfair, deceptive, or abusive acts or practices (UDAAPs).
- Focus on unfair practices used by auto loan servicers by assessing late fees in excess of the amounts allowed in consumers' contracts.
- Unfair acts or practices by assessing late fees that are not enumerated in consumers' contracts.
- Charging "estimated" repossession fees that far exceed the cost of repossession.
- Abusive and unfair payment processing fees by charging fees that exceed the servicer's cost for convenience payments.



Recent CFPB Supervisory Priorities (Continued)

- Failure to refund GAP overpayments at payoff.
- Deceptive statements about loan modification approval to defaulted consumers.
- Double-billing for collateral protection insurance charges.
- Using starter-interrupt devices for consumers who were not past -due.
- Servicers making deceptive statements to consumers about the servicer's ability to suspend licenses for consumers who default.

Joint CFPB/DOJ Notification Letter re SCRA

- Issued jointly by the CFPB and Department of Justice on July 29, 2022.
- Reminds auto finance companies of the protections offered to servicemembers and their dependents.
- “Auto finance companies [informed] of the burden of identifying whether borrowers are protected by [SCRA’s repossession protections], and servicemembers are not required to give notice of military status to receive this protection.”
- Servicemembers may terminate leases early and without penalty.
- Interest rate benefits also apply to auto loans.



Compliance Bulletin 2022-04

- Issued jointly by the Offices of Supervision Policy and Enforcement on February 28, 2022
- Summarized supervisory and enforcement actions the Bureau has taken in recent years regarding auto default servicing and repossessions
- “The Bureau intends to hold loan holders and servicers accountable for UDAAPs related to the repossession of consumers’ vehicles.”
- Blog post on February 24, 2022 identified other areas of concern: increasing LTVs and lack of competition in subprime indirect auto loans – promising to work with the FTC to address



FTC Automotive & Mobility Finance Priorities

Morgan Lewis

FTC Automotive & Mobility Finance Priorities

- “The automobile-financing market in the United States is profoundly broken.”
- Anti-discrimination
- Advertising
- Optional products
- Promulgation of auto dealer trade regulation rules



Office of Commissioner
Rebecca Kelly Slaughter

UNITED STATES OF AMERICA
Federal Trade Commission
WASHINGTON, D.C. 20580

STATEMENT OF COMMISSIONER REBECCA KELLY SLAUGHTER

In the Matter of Liberty Chevrolet, Inc. d/b/a Bronx Honda

Commission File No. 1623238

May 27, 2020

The automobile-financing market in the United States is profoundly broken. Although this matter involves extreme conduct that may make it seem like an outlier, the tricks and traps that Bronx Honda used against consumers are all too prevalent at auto dealerships across the country. The complaint against and settlement with Bronx Honda and its general manager, Carlo Fittanto, highlight the perils that consumers, especially people of color, face in purchasing and financing a vehicle, and they illustrate the limited utility of one-off enforcement actions to fix a broken market. In my view, far-reaching structural reform to the automobile-financing and -sales markets is long overdue and urgently needed: First and foremost, the Commission can start by initiating a rulemaking, under the Dodd-Frank Act, to regulate dealer markup.

FTC Automotive & Mobility Finance Priorities

- *FTC & State of Illinois v. Napleton Automotive Group, Inc.* (Mar. 31, 2022)
- Anti-discrimination
- Advertising
- Optional products
- **Remedies**
 - \$10 million penalty
 - Express informed consent
 - Mark-up caps and rules



Office of the Chair

UNITED STATES OF AMERICA
Federal Trade Commission
WASHINGTON, D.C. 20580

**Statement of Chair Lina M. Khan
Joined by Commissioner Rebecca Kelly Slaughter
In the Matter of Napleton Automotive Group
Commission File No. 2023195**

March 31, 2022

For many consumers, buying a car is one of the largest purchases they will make.¹ Too often, it is also one of the most frustrating. Researching, shopping, testing, and negotiating can wear down the time and resources of even the savviest shopper. And at the end of a draining process, auto dealers often overload consumers with confusing “add-ons,” mark-ups, and a stack of opaque financing documents. These add-on products—such as guaranteed asset protection (GAP), VIN etchings, extended warranties, and anti-rust coatings—are a major money-maker for dealers.² But in many instances, consumers drive off the lot paying too much for add-ons they did not want or need.

FTC Automotive & Mobility Finance Priorities

- *FTC v. Passport Auto Group* (Oct. 18, 2022)
- Anti-discrimination
- Advertising
- Optional products
- **Decision was not unanimous**
- **Remedies**
 - \$3.3 million redress
 - Fair lending program that allows no pricing discretion whatsoever

FTC Automotive & Mobility Finance Priorities

- Motor Vehicle Trade Regulation Rule – June 23, 2022
 - Bans “bait-and-switch” deceptive advertising claims
 - Bans certain add-on products deemed “junk” or that provide no benefit to consumers and requires express consent to charge for optional products
 - Requires true “offering price” for vehicles, excluding only taxes and fees
- Director of the FTC’s Bureau of Consumer Protection claims:
 - “As auto prices surge, the Commission is taking comprehensive action to prohibit junk fees, bait-and-switch advertising, and other practices that hit consumers’ pocketbooks. Our proposed rule would save consumers time and money and help ensure a level playing field for honest dealers.”

Dealer Oversight Expectations

Morgan Lewis

Implications of the FTC TRR

- Potential interaction with FTC Holder Rule, 16 C.F.R. pt. 433
- FTC Act § 19 liability for TRR violations
- Risks of Dodd-Frank Act “substantial assistance” liability
- State UDAP law consequences
- Unintended consequences on auto securitizations



September 12, 2022

Via Electronic Submission

Sanya Shahrasbi and Daniel Dwyer
Federal Trade Commission, Office of the Secretary
600 Pennsylvania Avenue, NW, Suite CC-5610 (Annex C)
Washington, DC 20580

Re: Motor Vehicle Dealers Trade Regulation Rule—Rulemaking, No. P204800

Dear Ms. Shahrasbi and Mr. Dwyer:

The Structured Finance Association¹ (“SFA”) appreciates the opportunity to respond to the Federal Trade Commission (“FTC”) Notice of Proposed Rulemaking, “Motor Vehicle Dealers Trade Regulation Rule” (the “Proposed Rule”).² SFA is a member-based, trade-industry group encompassing all sectors of the securitization market, which currently finances \$220 billion in auto loans and leases.³ SFA and its members are supportive of the objective of the FTC to protect consumers from illegal or deceptive practices. However, we have significant concerns, as summarized below, that the Proposed Rule may have unintended consequences on the cost of funding available to auto lenders in the securitization market.

Third-Party Oversight Guidance

- Final interagency guidance from OCC, FRB, and FDIC issued on June 6, 2023
- Flexible and risk-based, but sets parameters that regulators have begun enforcing
- Key elements:
 - Planning
 - Due diligence and selection
 - Contract negotiation
 - Ongoing monitoring
 - Termination
- Applicability to dealer relationships?

FEDERAL RESERVE SYSTEM

[Docket No. OP-1752]

FEDERAL DEPOSIT INSURANCE CORPORATION

RIN 3064-ZA26

DEPARTMENT OF THE TREASURY

Office of the Comptroller of the Currency

[Docket ID OCC-2021-0011]

Interagency Guidance on Third-Party Relationships: Risk Management

AGENCY: The Board of Governors of the Federal Reserve System (Board), the Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC), Treasury.

Credit Acceptance CFPB Litigation

Morgan Lewis

Credit Acceptance Litigation

- On January 4, 2023, the CFPB and the NY Attorney General sued subprime auto finance lender, Credit Acceptance Corporation (CAC)
- According to the Bureau:
 - “Credit Acceptance obscured the true cost of its loans to car buyers, leading to severe financial distress for borrowers and subjecting them to aggressive debt collection tactics on loans its own systems predicted that borrowers can’t afford to repay.”
- The Complaint contains a number of novel legal theories, including:
 - **Hidden Finance Charges:** The Bureau attacked the core business model by claiming that CAC encourages dealers to manipulate the prices of vehicles solely based on borrowers’ projected performance and causes both inflated principal balances and violation of state usury laws.
 - **Ability to Repay:** The Bureau claims that CAC made loans without regard to consumers’ ability to repay and that it profited when consumers defaulted.
 - **Add-on Products:** CAC used financial incentives that caused dealers to add extra products to loans and ignored instances where consumers believed that the add-ons were required as a condition of receiving auto loans.

Credit Acceptance Litigation (Continued)

- Key Questions:
 - Does the CFPB believe that assignment discounts are finance charges?
 - Is the CFPB action an end-run around Dodd-Frank's removal of auto dealers from the CFPB's authority?
 - Does the CFPB's theory circumvent the Holder Rule?
 - Is there now an ability-to-repay requirement for the auto finance market?

California GAP Waiver Laws

Morgan Lewis

General Gap Waiver: A.B. 2311

- Took effect **January 1, 2023**
- Creates requirements for **new detailed disclosures** at the time of purchase
- Requires notices of **ownership transfer** of the RIC
- Imposes a **4% price cap** on GAP waiver; bars GAP waiver below **70% LTV**
- Sets mandatory GAP **cancellation triggers** and allows borrower cancellation
- Creates specific obligations for **refund calculations**
- Creates statutory treble damages **against the holder of the RIC** for certain violations of the servicing requirements
- Does **not** apply to:
 - Loans
 - GAP insurance
- Amends Cal. Civil Code §§ 2981, 2982, 2982.2, 2983.1; adds Cal. Civil Code § 2982.12

Military Lending: S.B. 1311

- Took effect **January 1, 2023**
- Designed to work in parallel with Military Lending Act, 10 U.S.C. § 987
- Prohibits and voids security interests in personal property that would otherwise avoid application of MLA
 - Excludes “motor vehicle, off-highway vehicle, trailer, vessel, or aircraft” without defining those terms
 - Creates uncertainty as to coverage of certain motorized products
- Prohibits and voids security interests in motor vehicles that would otherwise avoid application of MLA if the “loan also funds the purchase of a credit insurance product or credit-related ancillary product”
- On the face of the statutory text, it applies only to:
 - A “covered member” under MLA, **not** dependents
 - A “loan,” not an RIC
- Adds Cal. Mil. & Vet. Code § 408.1

Litigation Relating to Holder Rule

Morgan Lewis

The Issue

- While the Holder Rule permits a consumer to pursue all claims and defenses against the current holder of a consumer credit contract, “recovery hereunder by the debtor shall not exceed amounts paid by the debtor.”
- Does the Holder Rule’s cap on recovery include attorneys fees and costs?

The FTC's Position

- In 2019, the FTC opined that the Holder Rule's cap includes attorneys fees and costs only if "the holder's liability for fees is based on claims against the seller that are preserved by the Holder Rule Notice"
- However, the cap did not apply to any claim that separately provided for attorneys fees that were "independent of claims or defenses arising from the seller's misconduct"
- 84 Fed.Reg. 18711, 18713 (May 2, 2019)
- In 2022, the FTC issued an advisory opinion, clarifying that the "Holder Rule does not limit recovery of attorneys' fees and costs when state law authorizes awards against a holder."

California Appellate Courts Weigh In

- Lafferty v. Wells Fargo Bank, 213 Cal.App.4th 545 (2018). Holder Rule cap includes attorneys' fees where claim arises solely from Holder Rule Notice
- Spikener v. Ally Financial, Inc., 50 Cal.App.5th 151 (2020). Same. Also holding that FTC's position is entitled to deference.
- Pulliam v. HNL Automotive Inc., 60 Cal.App.5th 396 (2021). No. Holder Rule cap does not apply to attorneys' fees and FTC's position is not entitled to deference.

California Supreme Court Decides Split

- Pulliam v. HNL Automotive Inc., 13 Cal.5th 127 (May 2022)
- Cap does not apply where debtor seeks attorneys fees and costs pursuant to California's prevailing party statute.
- The Holder Rule is ambiguous, at best, as it limits recovery "by the debtor" where attorney fees are paid to the debtor's attorney.
- The FTC's interpretation is not inconsistent, as FTC recognized that state law could provide the basis for recovery of fees against a holder.
- In California, a prevailing party is entitled to costs as well as attorney fees if provided for by statute.
- United States Supreme Court denied cert. (Jan. 2023).

What Now?

- Dealer fraud cases in California are more problematic for holder—consider requiring dealer buyback where permitted instead of demanding indemnity or tendering defense
- Pulliam resolves any ambiguity in California, but be mindful of its potential application in other states

Litigation Unique to Pandemic

Morgan Lewis

Is Requiring a Leased Vehicle to Be Returned at an Affiliated Dealer an Antitrust Violation?

- No!
- Many finance companies instituted policies during the height of the pandemic that prohibited an unaffiliated third-party dealer from purchasing a leased vehicle
- Calabasas Luxury Motorcars, Inc. (Starr) sued automotive finance companies claiming that the policies violated California's antitrust and unfair competition laws
- Courts made clear that the policies did not violate antitrust law

Does California Law Permit a Lessee to Surrender a Leased Vehicle to Any Dealership, Even an Unaffiliated Dealership?

- No!
- Addressed by courts in *Calabasas Luxury Motorcars* Decisions

Is a Lessee Entitled to Insurance Proceeds Where Leased Vehicle Is Declared a Total Loss?

- No!
- Kumar v. Ally Fin. Inc., No. 2:22-cv-05184-SVW-MRW, 2022 WL 16962283 (C.D. Cal. Oct. 17, 2022), reconsideration denied sub nom. Kumar v. Ally Fin. Inc., No. 2:22-cv-05184SVW-MRW, 2022 WL 18228183 (C.D. Cal. Dec. 1, 2022)

Key Takeaways

Morgan Lewis

Key Takeaways

- **Parallel Enforcement.** Expect continued cooperation (or collusion) between federal regulators such as the CFPB, FTC and their state counterparts. This is a now-frequent occurrence that we are seeing across multiple industries.
- **Junk Fees.** While “junk” is a subjective and ultimately meaningless term, federal regulators are placing heavy scrutiny on fees that are passed onto consumers both in originations and servicing contexts.
- **Understand third-party risks.** Conduct due diligence on prospective lending partners, dealers, servicers, repossession agents, and others. Identify key risk indicators and monitor for changes.
- **Litigation.** Be wary that California often stands apart from other states in finding ways to provide additional protections for consumers.

Questions

Morgan Lewis

Biography



David I. Monteiro

Dallas

+1.214.466.4133

david.monteiro@morganlewis.com

David Monteiro focuses his practice on counseling companies facing government investigations and enforcement litigation. A former enforcement attorney with the Federal Trade Commission's Bureau of Consumer Protection, Division of Financial Practices, David guides financial institutions, retailers, technology firms, and other companies in complying with state and federal consumer protection laws and regulations, responding to examinations and investigations, and defending against government litigation. David has experience in building, implementing, and overseeing complex, large-scale customer remediation programs both to address self-identified compliance issues and to comply with consent orders.

Biography



Allen Denson

Washington, DC

+1.202.739.5257

allen.denson@morganlewis.com

Allen Denson represents financial institutions and fintech companies that are forced to defend their business practices against federal and state financial regulators. Allen guides clients through agency investigations, litigation, and regulatory inquiries involving both safety and soundness and consumer protection issues. He also advises clients on the application of federal banking and consumer protection laws. A former senior attorney at the Office of the Comptroller of the Currency (OCC), Allen has developed a boots-on-the-ground understanding of regulatory agencies.

Biography



Marcos D. Sasso

Century City

+1.310.907.1064

marcos.sasso@morganlewis.com

With nearly two decades of expertise, Marcos D. Sasso advises large national banks, credit card issuers, and other financial services companies in all aspects of consumer financial services litigation and enforcement proceedings. Marcos defends clients in class actions and mass arbitrations, and against high-volume filers of individual consumer claims in federal and state trial and appellate courts and arbitrations across the US. Marcos routinely counsels clients on compliance with state and federal laws on debt collection, credit reporting, unfair business practices, and other consumer protection statutes.

Morgan Lewis Automotive Hour Webinar Series

Series of automotive industry focused webinars led by members of the Morgan Lewis global automotive team. The 8-part 2023 program is designed to provide a comprehensive overview on a variety of topics related to clients in the automotive industry.

- **JANUARY 18** | Warranty Claims and Trends in the Automotive Industry
- **FEBRUARY 22** | Key Issues Facing the EV Industry in 2023
- **MARCH 29** | Recent Trends and Developments in Automotive Class Actions
- **APRIL 19** | 2023 Congress: Potential Impact on EVs
- **JUNE 21** | Advancements in Autonomous Vehicles
- **JULY 19** | Latest Developments in Automotive Finance and Consumer Protection
- **SEPTEMBER 20** | Human Rights Violations and Supply Chain Issues: Impacts on the Automotive Industry
- **NOVEMBER 15** | IP Considerations for EVs and Beyond

[REGISTER NOW](#) for upcoming webinars!

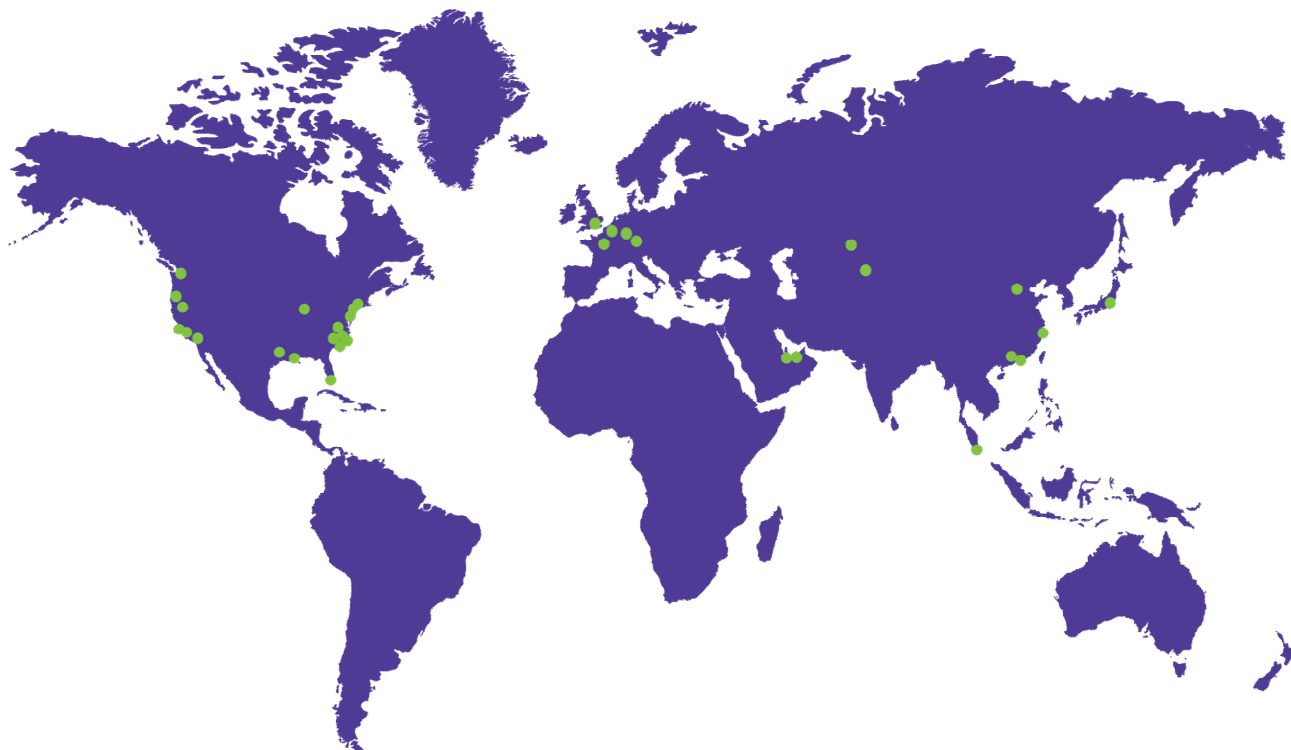


Our Global Reach

Africa
Asia Pacific
Europe
Latin America
Middle East
North America

Our Locations

Abu Dhabi
Almaty
Astana
Beijing
Boston
Brussels
Century City
Chicago
Dallas
Dubai
Frankfurt
Hartford
Hong Kong
Houston
London
Los Angeles
Miami
Munich
New York
Orange County
Paris
Philadelphia
Pittsburgh
Princeton
San Francisco
Seattle
Shanghai
Shenzhen
Silicon Valley
Singapore
Tokyo
Washington, DC
Wilmington



THANK YOU

© 2023 Morgan, Lewis & Bockius LLP
© 2023 Morgan Lewis Stamford LLC
© 2023 Morgan, Lewis & Bockius UK LLP

Morgan, Lewis & Bockius UK LLP is a limited liability partnership registered in England and Wales under number OC378797 and is a law firm authorised and regulated by the Solicitors Regulation Authority. The SRA authorisation number is 615176.

Our Beijing and Shanghai offices operate as representative offices of Morgan, Lewis & Bockius LLP. In Hong Kong, Morgan, Lewis & Bockius is a separate Hong Kong general partnership registered with The Law Society of Hong Kong. Morgan Lewis Stamford LLC is a Singapore law corporation affiliated with Morgan, Lewis & Bockius LLP.

This material is provided for your convenience and does not constitute legal advice or create an attorney-client relationship. Prior results do not guarantee similar outcomes. Attorney Advertising.