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# WHAT'S NEXT FOR CONSUMER FINANCE IN THE AUTOMOTIVE AND MOBILITY SPACE

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David Monteiro  
Eamonn Moran

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# Morgan Lewis Automotive Hour Webinar Series

Series of automotive industry focused webinars led by members of the Morgan Lewis global automotive team. The 10-part 2021 program is designed to provide a comprehensive overview on a variety of topics related to clients in the automotive industry. Upcoming sessions:

**FEBRUARY 3** | FRAND or Foe? Competition Law and SEP Licensing: Recent Developments in Europe and their Impact on the Automotive Industry

**MARCH 10** | The New On-Demand Workforce Model: Employee Benefits and Labor Issues in the Automotive and Mobility Industry

**APRIL 14** | Continuing to Capitalize on Emerging Technology in the Automotive and Mobility Space: A 100-Day Report on Biden Administration Opportunities

**JUNE 2** | Trademark and Copyright Considerations in the Automotive and Mobility Space

**JULY 14** | White Collar and Regulatory Developments Affecting the Automotive and Mobility Industry

**AUGUST 11** | Power and Opportunity: EVs, Hydrogen and Other Vehicle Power

**SEPTEMBER 15** | SPACs and Other Vehicles for Investment in the Automotive and Mobility Sectors

**NOVEMBER 10** | New Market Entry and the Anachronistic US Distribution System: What the Future Portends

**DECEMBER 8** | The IP Anatomy of the Automotive Nervous System

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# Presenters



**David Monteiro**  
Dallas  
Tel. +1.214.466.4133  
[david.monteiro@morganlewis.com](mailto:david.monteiro@morganlewis.com)



**Eamonn Moran**  
Washington, DC  
Tel. +1.202.739.5037  
[eamonn.moran@morganlewis.com](mailto:eamonn.moran@morganlewis.com)

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# **Roles of the Consumer Financial Protection Bureau and the Federal Trade Commission**

*(and the States...)*

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# The Auto Market and the Consumer Financial Protection Bureau (CFPB)

Auto loans are financed by both banks and nonbanks. Consumers can get a loan through:

Banks, credit unions, and nonbank auto finance companies provide credit to consumers both directly and indirectly. Some nonbank finance companies are "captive" nonbanks, meaning they are owned by auto manufacturers and generally do only indirect lending. Banks hold approximately a third of all auto loan balances, followed closely by captive auto lenders, credit unions, and auto finance companies.

**Direct financing**, where they seek credit directly from a lender.

**Indirect financing**, where an auto dealer typically enters into a retail installment sales contract that it then sells to a third-party.

## The Auto Market and the CFPB (continued)

- The CFPB supervises auto financing at the largest banks and credit unions. In addition, the Bureau extended that supervision to any nonbank auto finance company that makes, acquires, or refinances 10,000 or more loans or leases in a year. Those companies are considered “larger participants.”
- There are additional automobile leasing activities covered by certain consumer protections of the Dodd-Frank Act.
- Notably, most auto dealers were carved out of the CFPB’s jurisdiction when Congress established the CFPB in 2010.



# The Auto Market and the Federal Trade Commission

- **FTC Jurisdiction:**
  - Auto dealers
  - Auto lenders
  - Auto servicers
  - **Every** participant in the automotive financing marketplace **except** banks and credit unions



## § 45. Unfair methods of competition unlawful; prevention by Commission

### (a) Declaration of unlawfulness; power to prohibit unfair practices; inapplicability to foreign trade

(1) Unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful.

(2) The Commission is hereby empowered and directed to prevent persons, partnerships, or corporations, except banks, savings and loan institutions described in section 57a(f)(3) of this title, Federal credit unions described in section 57a(f)(4) of this title, common carriers subject to the Acts to regulate commerce, air carriers and foreign air carriers subject to part A of subtitle VII of title 49, and persons, partnerships, or corporations insofar as they are subject to the Packers and Stockyards Act, 1921, as amended [7 U.S.C. 181 et seq.], except as provided in section 406(b) of said Act [7 U.S.C. 227(b)], from using unfair methods of competition in or affecting commerce and unfair or deceptive acts or practices in or affecting commerce.



# The Auto Market and the Federal Trade Commission

- **Backup Enforcement of Federal Financial Laws**

- Equal Credit Opportunity Act: 15 U.S.C. § 1691c(c), including Regulation B as “deemed trade regulation rule” (TRR) authority
  - Truth in Lending Act: 15 U.S.C. § 1607(c)
  - Consumer Leasing Act: 15 U.S.C. § 1607(c)
  - Fair Debt Collection Practices Act: 15 U.S.C. § 1692l(a), including statute as “deemed TRR” authority
- “Specifically committed to another Government agency”: But not the CFPB
  - Deemed TRR authority is exceptionally important in light of AMG Capital Management v. FTC Supreme Court argument



# The Auto Market and the Federal Trade Commission

- **Other TRRs: Magnusson-Moss Rulemaking**
  - 15 U.S.C. § 57a
  - Advance Notice of Proposed Rulemaking
  - Notice to Congress
  - Prior administrative enforcement or “widespread pattern”
  - Defined hearing procedures, including transcribed hearings
  - Statement of Basis and Purpose
    - Prevalence of practices
    - Manner and context of unfairness or deception
    - Economic effect of the rule, particularly on small businesses
- **But not auto dealers: 12 U.S.C. § 5519(d)**



# The Auto Market and the States

- State attorneys general and financial services regulators
  - Several state attorneys general have developed consumer protection divisions
  - Watch out for “mini-CFPBs,” including California
    - UDAP/UDAAP
    - Debt collection practices
    - Predatory lending
    - State usury caps
    - State licensing
- Some entities have faced enforcement actions from multiple states
- Massachusetts: AG Healey’s review of securitization practices in the subprime auto market—an industry-wide investigation that remains ongoing



# Recent Regulatory and Enforcement Risks

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# The CFPB's Supervisory and Examination Manual

- Provides guidance on how the Bureau monitors the bank and nonbank auto finance companies that it supervises. Examiners assess potential risks to consumers and whether auto finance companies are complying with requirements of federal consumer financial law.
- Among other things, examiners evaluate whether auto finance companies are:
  - Fairly marketing and disclosing auto financing terms
  - Providing accurate information to credit bureaus
  - Treating consumers fairly when collecting debts (including repossession process)
  - Lending fairly



# Recent CFPB Enforcement Priorities

- **Auto Loan Originations & Marketing**
  - Descriptions of benefits and limitations of add-on products
  - Disclosure of finance charges associated with auto title loans, APR and other information required by TILA in advertisements
  - Purchase of mandatory auto loan insurance coverage
  - Failure to disclose auto loan program enrollment fees/misrepresentations of amounts consumers might save
  - UDAAPs
- **Auto Loan Servicing**
  - Payments by phone
  - Loan extension agreements (and any applicable bankruptcy protections)
  - Credit reporting



# Recent CFPB Supervisory Priorities

- Automobile loan servicing deficiencies, with a focus on repossessions and billing statements
- Focus on unfair practices used by servicers to wrongfully repossess consumers' vehicles in instances where the servicer and consumer had reached an agreement to cancel the repossession
- Total vehicle loss and insurance proceeds
- Rebates for certain ancillary products
- Sale of add-on GAP products



# FTC Automotive & Mobility Finance Priorities

- “The automobile-financing market in the United States is profoundly broken.”
- Antidiscrimination
- Advertising
- Optional products
- Promulgation of auto dealer trade regulation rules
- Auto sales to the military



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.

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# Things to Watch Out For



Increased focus on UDAAP as an enforcement tool by the CFPB

Reinvigoration of the CFPB's fair lending office/access to credit concerns

Dealer markups and disparate impact discrimination theories under ECOA

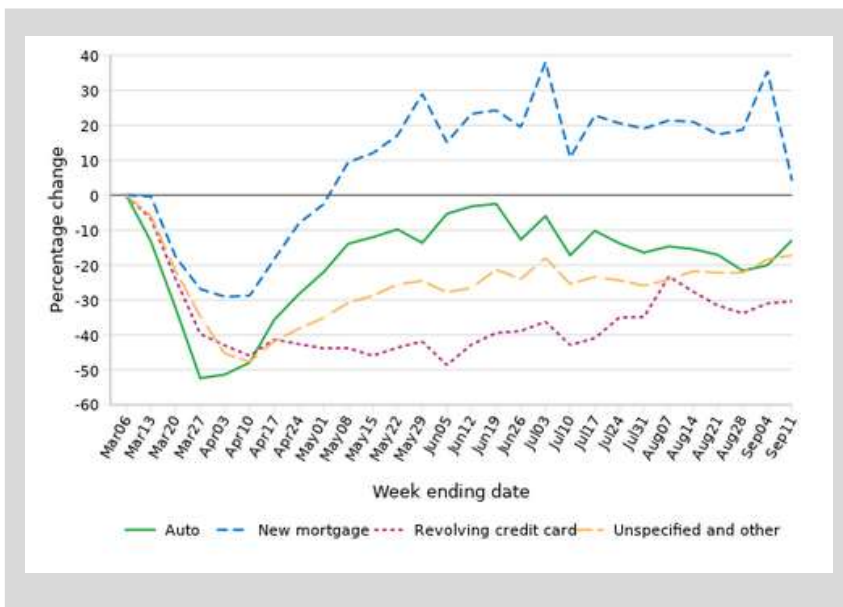
State UDAP/UDAAP actions – continued state involvement may also lead to increased class action litigation against the auto lending industry

“Mini-CFPBs” such as the California DFPI and the CCFPL

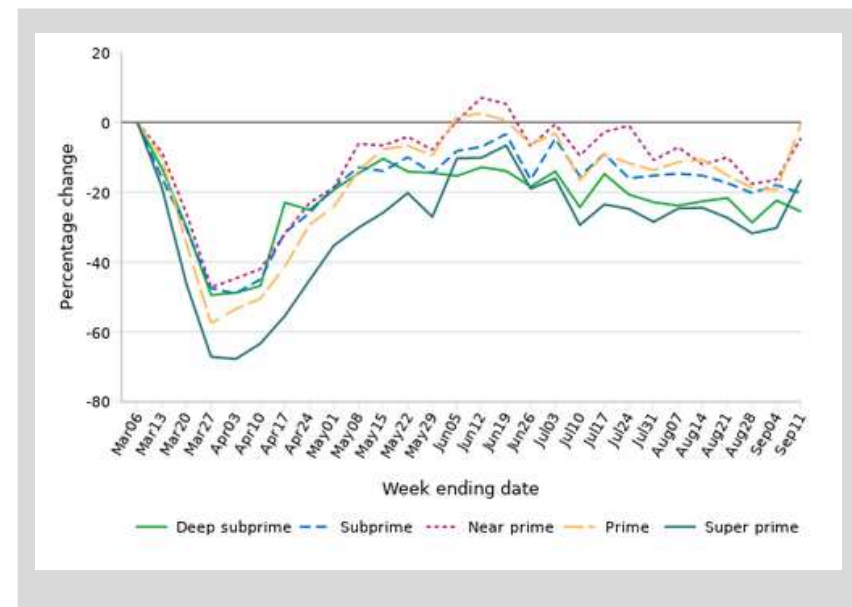
Continued impact of COVID-19

# Impact of COVID-19 on Credit Applications for Auto Loans

**Figure 1: Percentage change in credit inquiries relative to the first week of March by week ending date by inquiry category (adjusted based on historical seasonal trends)**



**Figure 2: Percentage change in auto loan inquiries relative to the first week of March by week by credit score group (adjusted based on historical seasonal trends)**



Source: Consumer Financial Protection Bureau (December 2020)

# **Fintech-Powered Innovation in the Automotive Industry**

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# **Fintech-Powered Innovation in the Automotive Industry**



**In-car payments**

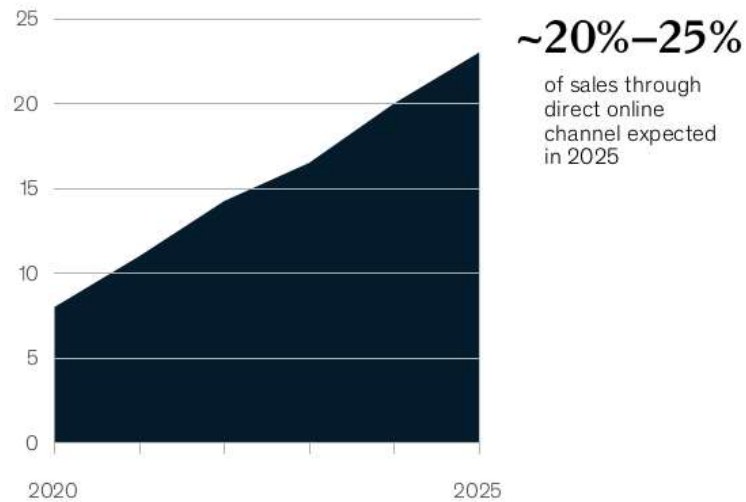
**Purchasing cars entirely online**

**Car rental and ride-sharing platforms**

# Fintech-Powered Innovation in the Automotive Industry

Auto-financing executives expect online business-to-consumer sales for auto loans and leasing to reach a market share of around 20 to 25 percent by 2025.

Expected share of online B2C sales for auto loans and leasing until 2025, % estimated by respondents



Source: McKinsey European Auto Finance Survey 2020

# Fintech-Powered Innovation in the Automotive Industry

Digital channels are becoming more important in the automotive-purchase experience.

Offline touch points still represent key parts of the car-buying journey ...

**No. 1**

Ranking of dealership visits as a factor influencing purchasing decisions

**~70%**

Car buyers who consider the dealership a major touch point for physically experiencing the car

**2-3**

Dealership visits per customer prior to purchase is still the norm

... while online touch points are increasingly shaping customer decisions and experiences

**>20%**

Use of online sources compared with offline sources during purchase-consideration period

**>80%**

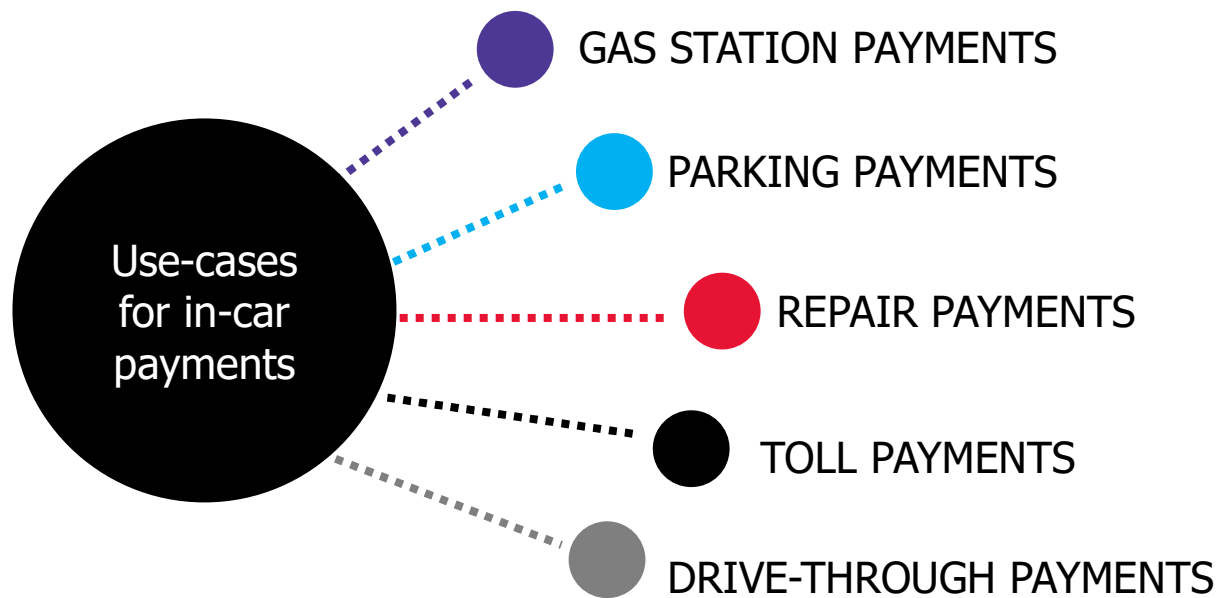
Respondents who use online sources during the purchase-consideration period

**>60%**

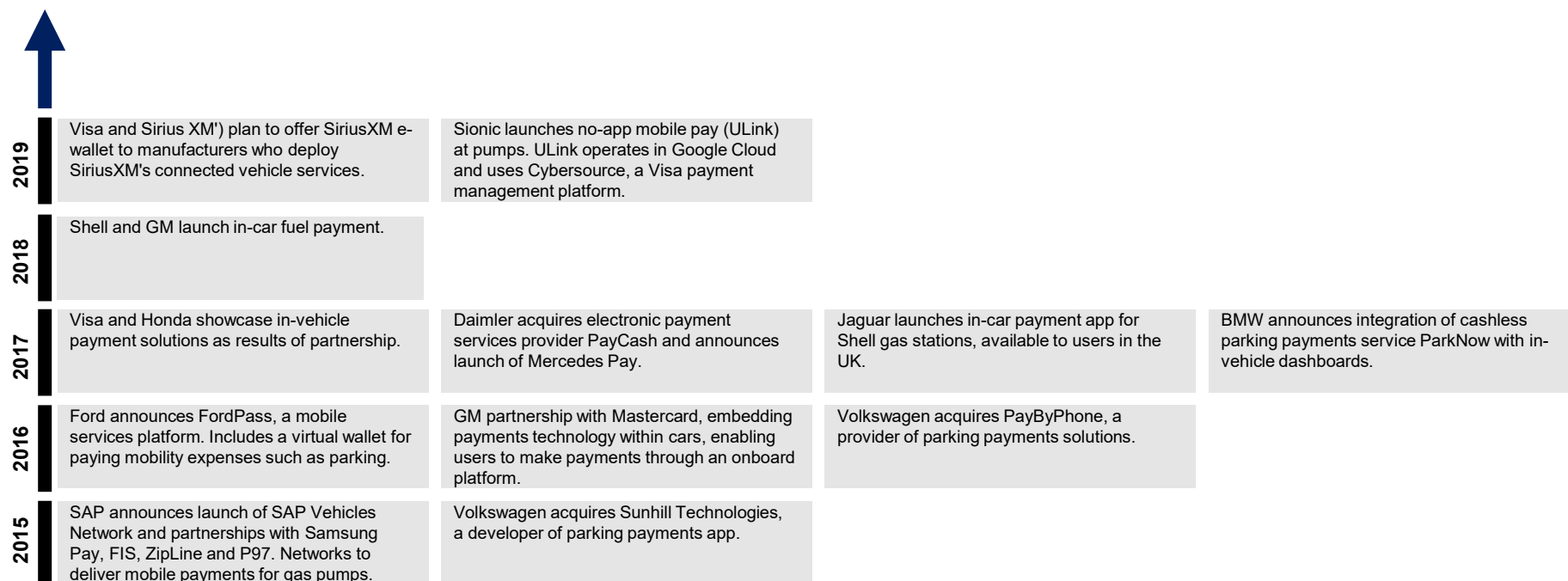
Buyers who perceive booking, paying, and reviewing additional services online as (very) appealing

Source: McKinsey Automotive Retail Consumer Survey (China, Germany, United States)

# Connected Cars: In-Car Payment Technology



# Connected Cars: In-Car Payment Technology



Source: "Auto FinTech Industry Trends," Financial Technology Partners. December 2017; Morgan Lewis Market Research



# In-Car Payment Technology & Money Transmission



- State licensing and reporting requirements
- Varying definitions of “money transmission” versus “payment processing”

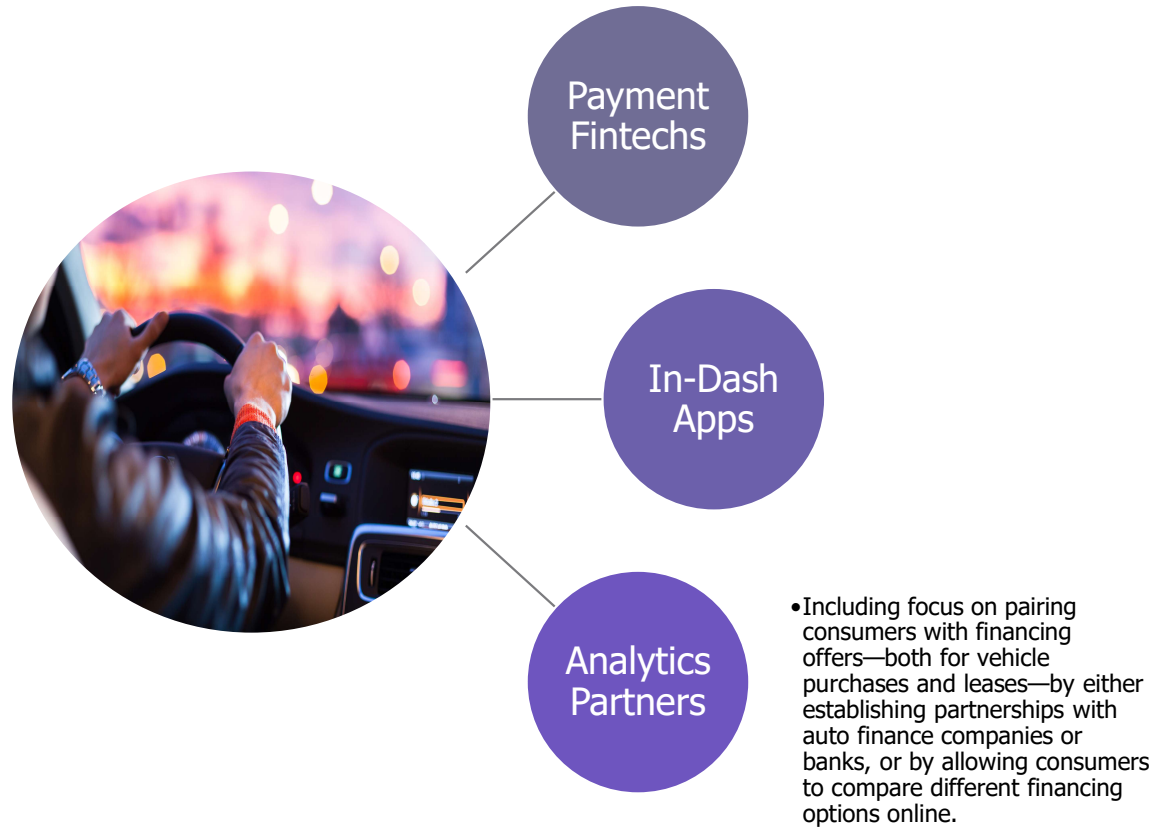


- Federal registration, anti-money laundering requirements
- Closed loop vs. open loop

# Working with Partners

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# Mitigating Risks: Working with Partners



# Mitigating Risks and Gauging How Well a Fintech Partnership Fits

- **Questions to Ask a Potential Fintech Partner**

- Do you understand the laws that apply to you, and do you follow them?
- Do you have a dedicated legal and compliance team in place, with requisite experience?
- Do you have a positive relationship with the appropriate regulators?
- Are you required to be licensed in any capacity, and if so, do you already have the appropriate license(s) in place?
- How do you ensure that throughout the lifecycle of a partnership, problems or issues are resolved efficiently and fairly?
- What do you do with customer data, and what do you say you do?
- How secure are your systems, and how secure do you say they are?
- Do you have a proven approach to combat fraud, particularly for new online-only accounts and identity verification?
- How do you control and monitor product iteration?
- Do you have other fintech partnerships?
- What is the long-term sustainability of your fintech business?

- **Questions to Ask Internally**

- Are there other potential reputational issues or risks?
- Are you prepared to exercise a robust third-party vendor management program?
- Determine if the fintech's values align with those of your institution.

# Emerging Compliance Risks

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# Fair Lending

- Racial justice and equity priorities
- FTC rulemaking
- More aggressive FTC enforcement
- CFPB guidance and rulemaking: downstream pressure
- Department of Justice role
- UDA(A)P versus ECOA
- **Coordinated federal approach**

# Military Lending & Servicing

- Servicemembers Civil Relief Act, 50 U.S.C. §§ 3901-4043
  - Repossession relief
  - Lease relief
- Military Lending Act, 10 U.S.C. § 987
- **State mini-SCRA laws**
  - **Md. Code, Public Safety § 13-704(b)(2)**: Applies federal SCRA protections to all National Guard activations 14 consecutive days or longer
  - **Ohio Rev. Code § 5919.29(B)**: Applies federal SCRA protections to all National Guard activations

## SUBCHAPTER I—GENERAL PROVISIONS

### § 3911. Definitions

For the purposes of this chapter:

#### (1) Servicemember

The term “servicemember” means a member of the uniformed services, as that term is defined in section 101(a)(5) of title 10.

#### (2) Military service

The term “military service” means—

(A) in the case of a servicemember who is a member of the Army, Navy, Air Force, Marine Corps, or Coast Guard—

(i) active duty, as defined in section 101(d)(1) of title 10, and

(ii) in the case of a member of the National Guard, includes service under a call to active service authorized by the President or the Secretary of Defense for a period of more than 30 consecutive days under section 502(f) of title 32 for purposes of responding to a national emergency declared by the President and supported by Federal funds;

(B) in the case of a servicemember who is a commissioned officer of the Public Health Service or the National Oceanic and Atmospheric Administration, active service; and

(C) any period during which a servicemember is absent from duty on account of sickness, wounds, leave, or other lawful cause.

“So far in 2020, **the National Guard has mobilized more Guard members, for longer, than at any time since World War II,**” said Air Force Lt. Col. Devin Robinson, director of public affairs for the Air National Guard, in a statement emailed to Military Times.”  
– *Army Times* (Dec. 13, 2020)

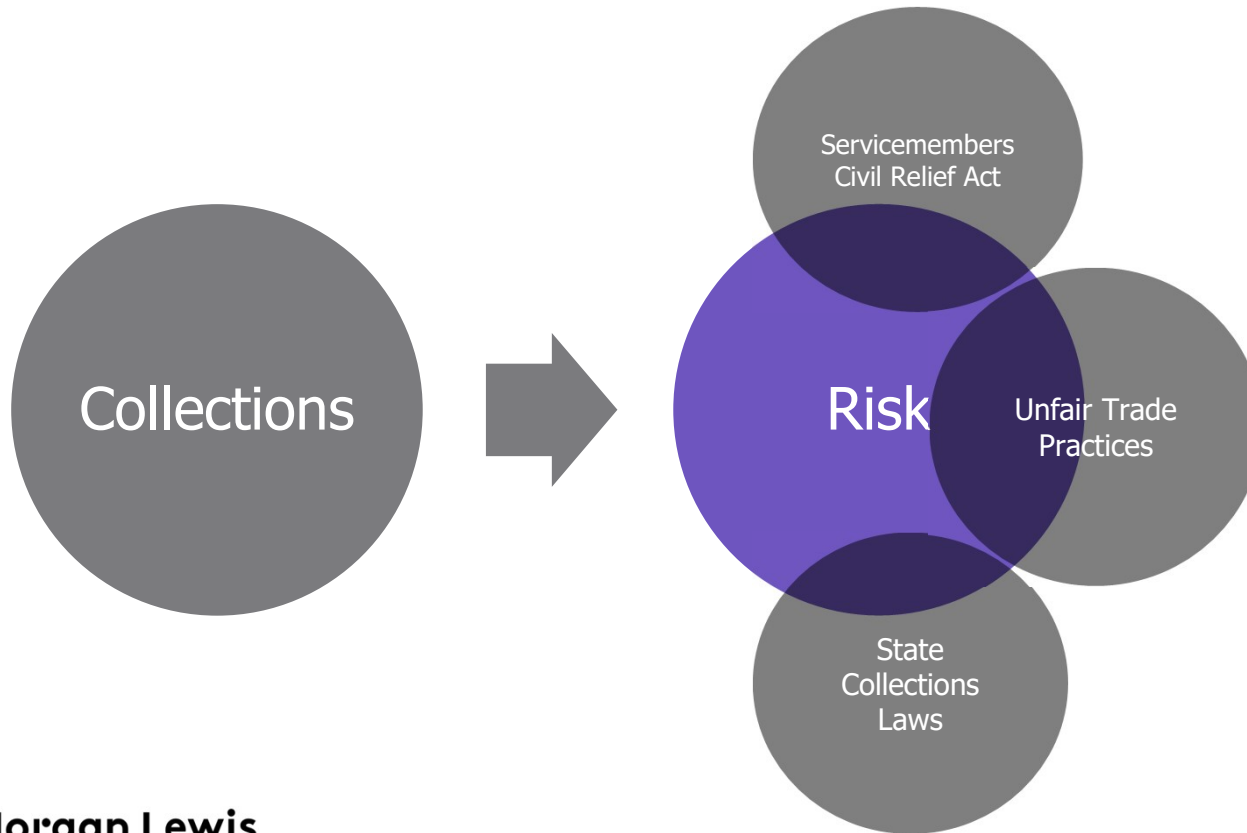
# California Enforcement

- New California agency with substantially strengthened resources and authority
- Aggressive licensing requirements
  - Cal. Fin. Code §§ 22000-22780
- Focus on scrutinizing retail installment sales contract practices
  - Cal. Civil Code §§ 2981-2984.6
  - Cal. Civil Code §§ 1801-1812.20
  - Opinion Letter No. OP 7667 (Dec. 20, 2019)
  - Cal. Fin. Code § 22054 (anti-evasion rule)





# Servicing & Collections



# Key Takeaways

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# Key Takeaways

- **Expect FTC rulemakings.** Monitor and participate in the proceedings.
- **Fair lending expectations will be more demanding.** Now it is a good time to reevaluate your fair lending compliance program.
- **State servicemember protections may be triggered.** Watch out for narrow readings of federal statutes.
- **UDAAP and UDAP.** Expect more enforcement cases involving larger dollar amounts and a more aggressive UDAAP/UDAP focus.
- **The pros and cons of fintech partnerships.** With benefits come risks, some of which may surprise you. Conduct due diligence before striking the deal and monitor the relationship closely afterwards.
- **Planning ahead.** Need to harness digital and analytical capabilities to address the current pandemic and new modes of engagement that may be here to stay.



## Questions?

**David Monteiro** | Partner, Dallas | [david.monteiro@morganlewis.com](mailto:david.monteiro@morganlewis.com)

**Eamonn Moran** | Of Counsel, Washington, DC | [eamonn.moran@morganlewis.com](mailto:eamonn.moran@morganlewis.com)

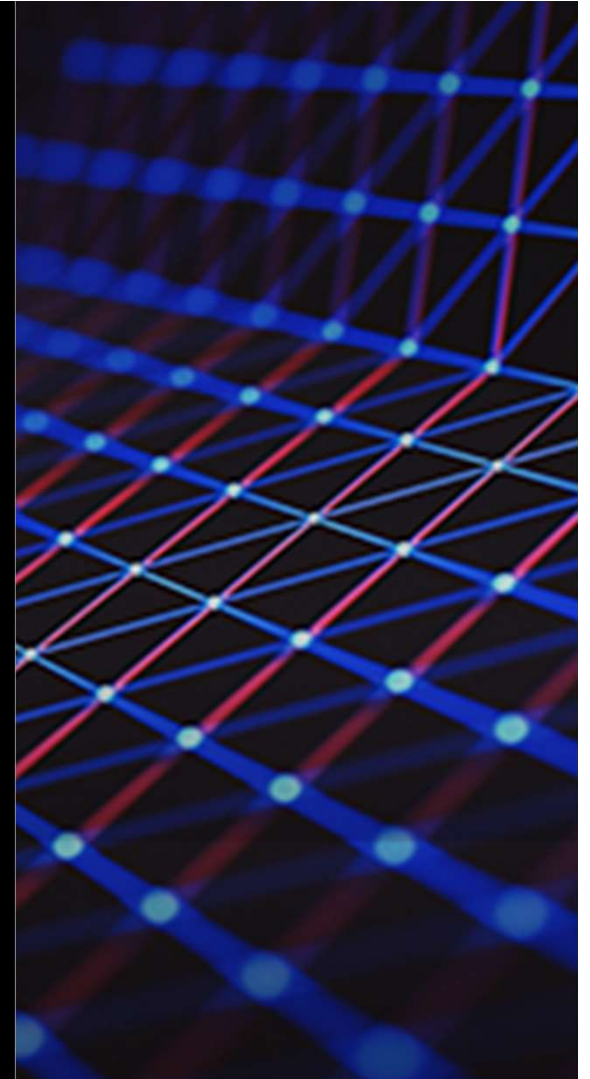
# Coronavirus COVID-19 Resources

We have formed a multidisciplinary **Coronavirus/COVID-19 Task Force** to help guide clients through the broad scope of legal issues brought on by this public health challenge.

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To help keep you on top of developments as they unfold, we also have launched a resource page on our website at [www.morganlewis.com/topics/coronavirus-covid-19](http://www.morganlewis.com/topics/coronavirus-covid-19)

If you would like to receive a daily digest of all new updates to the page, please visit the resource page to [subscribe](#) using the purple "Stay Up to Date" button.



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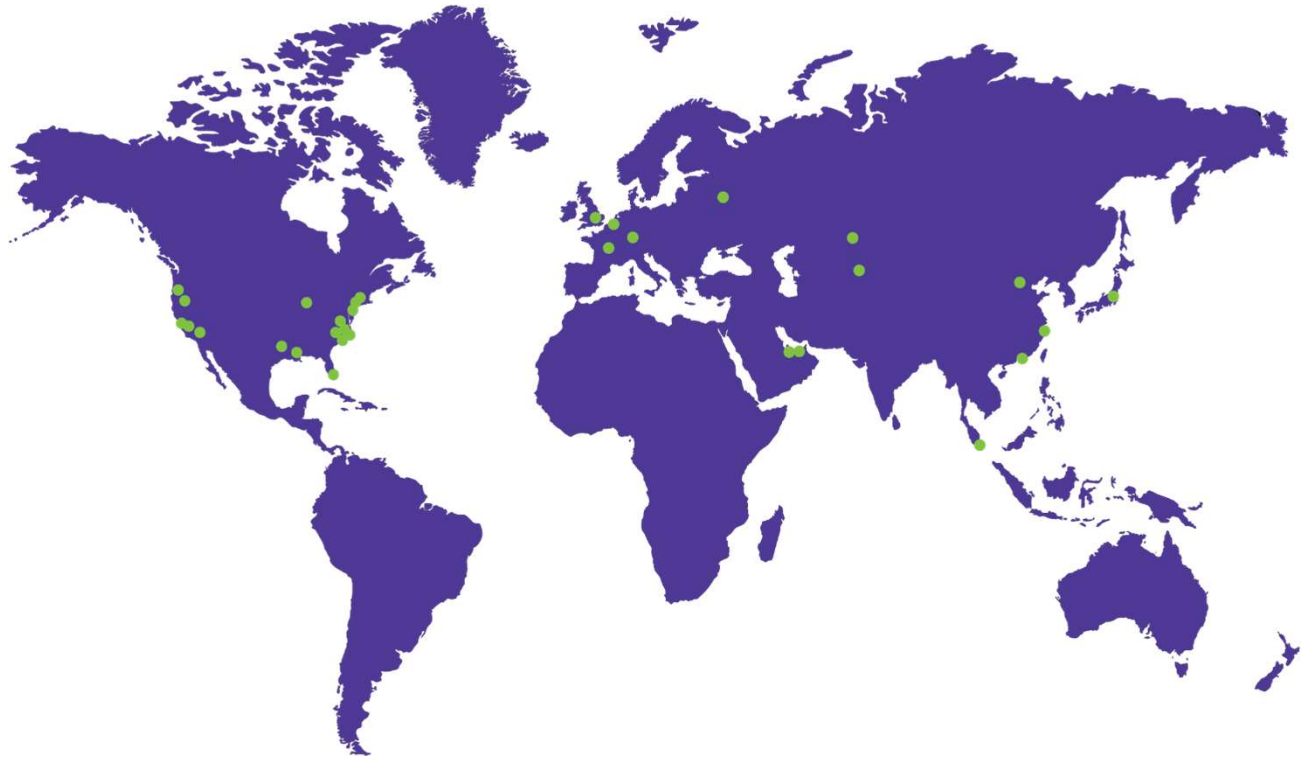
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