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AUTOMOTIVE FINANCE AND CONSUMER PROTECTION DEVELOPMENTS

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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 8-part 2022 program is designed to provide a comprehensive overview on a variety of topics related to clients in the automotive industry. Upcoming sessions:

JULY 13 | Part II: All Things Autonomous—Regulatory and Commercial Considerations for Delivery Robots (On and off campus), Scooters, and Drones

SEPTEMBER 14 | Part I: All Things EV—Regulatory and Commercial Considerations

SEPTEMBER 28 | Part II: All Things EV—Finance and Transactional Considerations

NOVEMBER 9 | European Antitrust and Other Regulatory Updates for the Automotive Industry



Table of Contents

- Section 01 – Introductions
- Section 02 – Roles of the CFPB, FTC and States
- Section 03 – Recent Regulatory and Enforcement Actions/Priorities
- Section 04 – Emerging Risks
- Section 05 – Key Takeaways
- Section 06 – Questions

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Roles of the Consumer Financial Protection Bureau, Federal Trade Commission, and 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, auto dealers were carved out of the CFPB’s jurisdiction (with some exceptions) when Congress established the CFPB in 2010.



The Auto Market and the CFPB (continued)

- Pending cases present serious new challenges to the CFPB's constitutional authority.
 - Five judges on the Fifth Circuit wrote in concurrence in rehearing en banc in *CFPB v. All American Check Cashing, Inc.*, No. 18-60302 (May 2, 2022) concluded that the agency's budgetary independence was unconstitutional; the majority opinion expressed no view and instructed the district court to consider any such issues on remand
 - The defendant in another pending enforcement action in the Southern District of New York has expressly made this argument as well
- Against this background, CFPB has reminded state AGs and banking regulators that they have the power to enforce the Dodd-Frank Act directly
 - Interpretive Rule, 87 Fed. Reg. 31,940 (May 26, 2022)
 - 12 U.S.C. § 5552(a)(1); actions against national banks require rulemaking
 - No limitation on auto dealers
- Nor do state AGs need the DFA: state UDAP laws already apply



The Auto Market and the Federal Trade Commission



§ 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.

• FTC Jurisdiction:

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

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 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*, 141 S. Ct. 1341 (2021)

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)**

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
- UDAAP

- **Auto Loan Servicing**

- Payments by phone
- Loan extension agreements (and any applicable bankruptcy protections)
- Credit reporting
- Charging of interest on late payments of loss damage waiver fees without disclosing the charge to consumers
- UDAAP



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 to wrongfully repossess consumers' vehicles in instances where the servicer and consumer had reached an agreement to cancel the repossession
- Collateral protection insurance
- Inaccurate payment posting/failure to follow disclosed payment application order/inaccurate payoff amounts
- Wrongful auto repossessions by servicers
 - The CFPB states that its examinations "have revealed that some servicers were engaging in unfair acts or practices by repossessing vehicles, even after consumers took intentional actions to prevent repossessions."
 - In certain examinations, the CFPB states that examiners found that auto servicers engaged in unfairly failing to obtain refunds for borrowers for add-on products that no longer provided a benefit.
 - In other instances, CFPB examiners found that auto servicers misled consumers about the amount of their final loan payments after their normal payments were deferred due to financial difficulties – largely as a result of the COVID-19 pandemic.

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 – promising to work with the FTC to address



Other Recent CFPB Developments

- **March 2022:** the CFPB published an updated exam manual for evaluating UDAAP, which notes that discrimination may meet the criteria for “unfairness” by causing substantial harm to consumers that they cannot reasonably avoid, where that harm is not outweighed by countervailing benefits to consumers or competition
 - Consumers can be harmed by discrimination regardless of whether it is intentional.
 - Discrimination can be unfair in cases where the conduct may also be covered by ECOA, as well as in instances where ECOA does not apply. For example, denying access to a checking account because the individual is of a particular race could be an unfair practice even in those instances where ECOA may not apply.
- **April 2022:** the CFPB announced that it is invoking a largely unused legal provision to examine nonbank financial companies that pose risks to consumers
 - Nonbanks whose activities the CFPB has reasonable cause to determine pose risks to consumers.
 - This authority is not specific to any particular consumer financial product or service.
- **May 2022:** the CFPB published an advisory opinion to affirm that ECOA bars lenders from discriminating against customers after they have received a loan, not just during the application process
- **May 2022:** the CFPB confirmed that ECOA requires companies to explain to applicants the specific reasons for denying an application for credit or taking other adverse actions, **even if** the creditor is relying on credit models using complex algorithms
 - “Companies are not absolved of their legal responsibilities when they let a black-box model make lending decisions,” said CFPB Director Rohit Chopra.

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



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)
- Antidiscrimination
- Advertising
- Optional products
- **Remedies**
 - \$10 million penalty
 - Express Informed Consent
 - Markup 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

- **May 27, 2020:** Commissioner Slaughter authors *Bronx Honda* concurrence
- **March 25, 2021:** Acting Chair Slaughter announces rulemaking unit in OGC
- **April 22, 2021:** Supreme Court decides *AMG Capital Management*
- **July 1, 2021:** FTC votes 3-2 to accelerate rulemaking process
- **October 12, 2021:** Commissioner Chopra resigns
- **December 10, 2021:** FTC votes 3-2 to issue Statement of Regulatory Priorities
 - Emphasis on practices that (1) injure consumers, (2) inhibit competition, and (3) result in discrimination
- **May 16, 2022:** Swearing-in of new Democratic Commissioner Bedoya

What to Watch Out For

- Increased defaults and repossessions leading to increased regulatory scrutiny
- Dealer markups and disparate impact discrimination theories under ECOA and the unfairness doctrine
- FTC rulemaking agenda
- Reassessment of the indirect auto lending market through a competition lens
- Increasing enforcement and litigation risks to loan holders
- State UDAP/UDAAP actions, jointly or in place of the CFPB

Staying Ahead of the Risks

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Emerging Risks



Fair
Everything



Competition



Third Parties



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 consider expanding the scope of your fair lending compliance program.
- **UDAAP and UDAP.** Expect more enforcement cases involving larger dollar amounts and a more aggressive UDAAP/UDAP focus.
- **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.
- **Pick your battles.** Decide in advance what positions will be worth fighting over in the face of aggressive government action.
 - but understand that if you do not raise an objection timely, you may be foreclosed from raising it forever.



Questions?

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THANK YOU

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