PUBLICATION

CFPB Proposes Federal Oversight of Auto Financing Companies

Authors: Blair B. Evans
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On September 17, 2014, noting the auto lending discrimination it has uncovered at banks, the Consumer Financial Protection Bureau (Bureau or CFPB) announced its plan to further extend its reach under the Dodd-Frank Act by proposing to amend the Code of Federal Regulations, allowing it to oversee larger non-bank auto finance companies for the first time at the federal level. The new rules would involve the inclusion within the Bureau's supervisory capacity grants of credit for the purchase of an automobile, refinancings of such credit obligations, purchases or acquisitions of such credit obligations, as well as automobile leases, and purchases or acquisitions of such automobile leases.

The CFPB currently has supervisory authority over most large banks and has initiated enforcement actions against several that engage in indirect auto lending. These enforcement actions have resolved alleged violations of federal consumer financial laws. While the Bureau's enforcement actions against banks have resulted in approximately $56 million in restitution and penalties in connection with hundreds of thousands of auto financing transactions, non-bank auto finance companies represent a much larger segment of the auto lending market but have not been subject to federal regulation. Through this proposal, the CFPB seeks to extend its regulatory oversight to financing entities that make, acquire or refinance at least 10,000 loans per year. It estimates that 38 entities meet this level and combined account for 90% of auto loans in the U.S. The CFPB would be supervising these entities to ensure their compliance with federal consumer financial law.

The Bureau states that the purpose of this move to include automobile financing within its jurisdiction and the Bureau's general mission "would be best served by covering automobile leasing more broadly." CFPB Director Richard Cordray justifies the Bureau's proposed rules, stating that they will allow it to "root out discrimination and ensure consumers are being treated fairly across this market." In the Bureau's Summary of the proposed rule, it suggests that the auto leasing market should be included within its supervisory reach "because of the important role that automobiles and related financing play in consumers' lives," noting that cars have become essential for working people and citing that 90% of today's workforce commutes to work via automobile.

By means of inclusion of the automobile financing industry within its supervisory scope, a clear goal of the CFPB appears to be the prohibition of discriminatory pricing in the auto finance market. This objective was previously expressed in the March 2013 *CFPB Bulletin*, which warned indirect auto lenders of the potential for "disparate impact" discrimination caused by dealer participation or "markup" and resulting differences in interest rates to similarly positioned borrowers. Other goals evident in the proposed rules include ensuring that auto lenders:

- Fairly market and disclose auto financing terms.
- Provide accurate information or payment histories to credit bureaus.
- Treat consumers fairly in collection actions.

In its proposed rules, the CFPB states a number of expected benefits to the subjection of larger participants of the automobile financing market to the possibility of Bureau supervision, including, among other things:

- Creation of an incentive for larger participants to allocate additional resources and attention to compliance with federal consumer financial laws, potentially leading to an increase in the level of compliance.
- Provision of more protections already mandated by law to consumers.
- Incentivizing automobile lenders to comply with regulations consistent with those with which credit unions and depository institutions must already obey.

The Bureau recognizes that increasing compliance results in increased costs, which will likely be passed on to the consumers and could restrict their financing choices. It justifies the increased costs, however, by arguing that the automobile financing market will adjust with smaller financers – who are not covered by the new rule and thus do not incur the increased costs of supervision – offering "more attractive transaction terms" than the larger, covered participants, therefore deterring the larger participants from increasing their prices in response to the proposed rule. This rationalization presumes that the larger participants thus simply absorb the increased cost of supervision without having the ability to pass on the cost to its customers.

In an effort to limit their risks, the CFPB advises auto lenders to internally monitor discretionary pricing policies and address the effects of markup policies, and to limit or eliminate discretionary markups.

The Bureau's proposal was published in the Federal Register on October 8, 2014. As such, the proposed rules will be open for comment until December 7, 2014, 60 days after its publication.