

### NEW CFPB AUTO FINANCE EXAM PROCEDURES: PART 1 - PRODUCT IMPLICATIONS

ON JUNE 10, in conjunction with the CFPB's long awaited publication of a final "larger participant" rule, the Bureau released [a fifty four page auto finance focused update](#) in nine modules, to the voluminous Supervisory and Examination Manual.

The newly updated examination procedures provide great insight into the Bureau's thinking about auto finance add-on products, settling some lingering industry speculation about the regulatory spotlight on add-on products and raising new ones.

#### 1) SCOPE OF PRODUCT AUTHORITY

Many in the product industry have long maintained the Bureau has little or no authority to directly regulate product providers or administrators – and that may be true, just as the Bureau may not directly supervise automotive dealers. **In reality though, that has never been the issue for auto finance providers – the real issue is whether and how the Bureau intends to hold auto finance companies responsible for how products are financed and sold in conjunction with an auto loan.**

For those not convinced by the June 2013 Consent Orders in the [U.S. Bank/DFS](#) cases (holding both entities responsible for how GAP and vehicle service contracts were sold to consumers), **page 4 of the new examination procedures spells out three types of "Ancillary Products and Services" that are specifically subject to review in conjunction with an auto finance company examination:** "GAP Insurance", "Extended Warranty or vehicle service contract", and "Vehicle Add-Ons" defined as "back-end products...[and] other pieces of equipment or finishing items that can be purchased with the vehicle such as Lo-Jack systems, [VIN] etching (anti-theft precaution), and paint protection." **In addition, the first two examination procedures in Module 5's Optional Product section (page 42) name the following products as examples of optional products and services subject to the exam process: biweekly payment plans, payment protection, credit protection, extended warranties, debt cancellation, and debt suspension.**

**The Optional Products section answers another big scope question:** Does this product review apply for companies offering products of their own or for any company who provides additional financing for optional add on products? **Answer:** Module 5, Item 1 (page 42) states, "Determine whether the servicer [entity being examined] **offers or finances** optional products or services" (emphasis added). There is no distinction for a finance company that offers products directly or one that merely provides additional financing for optional products.

*If you currently offer or finance optional add-on products in conjunction with auto or consumer financing, get started with a product compliance and product vendor management process today.*

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#### 2) PRODUCT EXAMINATION SPECIFICS

Once it has been determined optional products are at issue, CFPB examiners are instructed to investigate the following: (See Module 5 – Pages 42-43)

- How optional products are "monitored" overall
- Monitoring/Timeliness of **product cancellations**
- Involvement of a product **service provider**
- How the lender ensures products are **optional**
- Review of product **marketing materials**
- Prominent disclosure of **product cost and terms**
- Explicit **consumer authorization** to purchase
- Specific requirements for bi-weekly pay plans

There is not a lot of new information here – previous guidance bulletins and multiple enforcement action consent orders in the add-on product space have already identified most of the above, and hinted at some, like a focus on product cancellation issues. And while an itemized instruction point for the marketing of bi-weekly pay plans is notable, the Bureau's interest in that particular product/service is well documented.

**What's missing from the exam specifics is actually what's most interesting** – while the procedures clearly include products that are "offered or financed" and offers specific direction for examining call centers, web based marketing and third party "service providers" of products for a supervised entity, **the fact that the vast majority of add-on products are actually sold by automobile dealers is curiously absent – in fact the words "auto dealer" do not appear at all in the entire exam section for Optional Products!**

How can that be? We know the CFPB knows that dealers sell add-on products offered by or financed by (or both) auto finance companies! In fact that acknowledgement appears in the very first sentence of the Ancillary Product and Services definitions on Page 4: "In addition to the actual vehicle, auto dealers and auto financiers offer ancillary services and products at the time of vehicle purchase." **One possibility is that the CFPB is signaling an intention to consider auto dealers who originate retail installment contracts in indirect auto finance transactions to be finance company "service providers" as defined in the Bureau's original service provider Bulletin [2012-03](#).**

#### 3) SERVICE PROVIDER OVERSIGHT

Signaling of intentions or not, Module 2 of the procedures beginning on page 10, sets forth the examination topics relating to service provider oversight:

- Controls for **selecting and monitoring** service providers
- Ensure SPs are **licensed or registered** (as applicable)

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### 3) SERVICE PROVIDER OVERSIGHT (...Continued)

- c) **Initial due diligence** on SPs before entering agreements
- d) **Monitoring** of screening, hiring and training of **SP employees**
- e) Ensuring SP compliance with **privacy policy**
- f) Documentation of **Audits** of SPs activities **and remediation** of concerns

The examination instructions for Service Provider Oversight include several noteworthy items and valuable guidance. **First** for example, a specific standalone directive to ensure service providers are properly “licensed or registered to the extent required” - interestingly, **has not been previously singled out** in service provider guidance. Perhaps another clue about Bureau intentions about persons or entities that actually do the selling of add on products offered or financed by supervised companies.

**Secondly**, examination inquiries into service provider due diligence are directed specifically at “**prior regulatory compliance history**” and “**existence and extent of any prior enforcement actions against the service providers**”.

**Lastly**, a directive for **privacy policy compliance with regard to data shared with service providers** by the supervised entity demonstrates the continuing spotlight on data security and privacy concerns throughout the financial services industry.

### CONCLUSIONS AND WHAT'S NEXT

The new exam procedures include some odd language choices by the Bureau – for instance, the repeated reference to GAP as an “insurance policy” and then what appears as a careful avoidance of using the “I-word” (insurance), when it comes to “credit protection” and “payment protection”. **Some might argue sloppiness or a misunderstanding of industry products or procedures. I suggest the opposite and that the Bureau’s words are carefully chosen.** While some in the insurance industry cling to a hope that the “business of insurance” remains hands-off to the Bureau and federal regulators by specific exclusion in Dodd Frank and the now seventy year old McCarran–Ferguson Act (which arguably would not apply in the context of GAP since most states have decided not to regulate GAP as insurance), I believe **the inclusion of GAP “Insurance” by name and “Credit Protection” here are clear signals of the Bureau’s intention to hold supervised entities ultimately responsible for UDAAP violations tied to optional add-on products, regardless of insurance classification, when they are connected to an auto finance transaction.**

**Next up, NEW EXAM PROCEDURES PART 2 – Lessons for Add-On Product Compliance Design.**

In the meantime, visit [FNI Resources](#) and [News](#) for previous Take Action! Newsletters and articles on Service Providers and Add On Products including the US Bank/DFS case, additional add-on product consent order summaries, product best practices and vendor management guidance.

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### PRODUCT COMPLIANCE

FNI assists financial institutions with product vendor and product marketing due diligence and documentation for new or existing add-on product programs. Compliance services also include marketing and sales process design and implementation, and ongoing program and vendor management.

### PRODUCT SOLUTIONS

FNI product programs provide real consumer value, portfolio collateral protection and enhanced profitability for financial institutions. FNI bundles superior products from expertly vetted administrators with a proprietary product compliance and management process designed to meet regulatory expectations and maximize product program benefits.

### COMPLAINT MANAGEMENT

FNI works with [LenderGripe](#), the industry’s first web based, consumer-facing complaint management system. This simple technology meets regulatory expectations for complaint management and gives clients a powerful tool for overall business management and especially Service Provider/Vendor management.



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