The Buck Stops Here: Dealers, Compliance and Enforcement

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Agenda

• Regulations: Where Past is Prologue.
• Reputational Challenges.
• Heavily Regulated Industry.
• Costs to Dealers.
• Complaints.
• Advertising.
• UDAP.
• Deal Jackets and Documents.
• Additional Recommendations.
• Responding to an Investigation.
Regulations: Where Past is Prologue

• Old Wine in New Bottles.
• Nothing New under the Sun.
• The Household Encyclopedia (1950).
• What Can the Government Do?
• What Can You Do in Response?
What Can the Government Do?

• Prosecute.
• Regulate.
• Supervise.
What Can You Do in Response?

• Prepare for the most likely issues.
• Sort out the issues which will probably not get you into trouble.
• Think IRAC.
IRAC

• How do Regulators Think?
• IRAC
  – Issue.
  – Rule.
  – Application.
  – Conclusion.
What Are the Key Issues?
Richard Cordray, the CFPB, and the Four D’s

• Discrimination
• Deception
• Debt Traps
• Dead Ends
Why Listen to Me?

16 Years

$15,000,000

100,000 Transactions
Two Rules

• Don’t Get Noticed.
  – Complaints.
  – Advertising.

• If You Get Noticed Be Prepared.
Why Care?

• It’s all about the money.
• How to avoid paying it.
• How to avoid being selected.
• If selected, how to minimize the pain.
  – Cost.
  – Publicity.
Reputational Challenges
Dealers are a Big Target
Top Industries for Consumer Complaints

1. Automobile/car rental.
2. Home improvement/construction
3. Credit/debt.
4. Utilities.
5. Services.

Consumer Federation of America
Honesty/Ethics Rankings

1. Nurses.
2. Grade school teachers.
5. Doctors.
19. Lawyers.
22. Car salesman. 

LAST PLACE
Heavily Regulated Industry
Who Are the Antagonists?

• Federal agencies.
  – Consumer Finance Protection Bureau.

• State agencies.
  – Attorney General.
  – DMV, Consumer Affairs.

• Consumer Protection Groups, Private Bar, and Class Actions.
  – National Consumer Law Center.

• The Consumer.
Car sales: Tricks of the trade

Dateline NBC hidden camera investigation reveals deception at some dealerships
Costs to Dealers
Enormous Potential for Direct and Indirect Losses

• Fines, Penalties, and Fees.
  – CFPB, FTC, Attorney General.
• Class actions: actual damages, nominal damages, consequential, punitive, legal fees and costs.
• Negative Publicity.
• Loss of Business.
• Wasted Marketing Expenses.
Who is the Most Likely to Threaten You?

1. State Attorney General
2. State Regulator
3. Private Plaintiff/Class Action
4. FTC
5. CFPB
6. DOJ
Where Do Dealer Cases Originate?

• Consumer complaints.
• Advertising.
• Media.
• Agency observation and choice.
• The Basic Law in most of these Cases.
Consumer Complaints

• They are ransom notes.
What to Do

• Treat consumer complaints as ransom notes.
• Establish a dedicated telephone line.
• The compliance officer should address all complaints.
• Documentation is your major defense.
If You Receive a Complaint from a Governmental Agency

• Respond immediately and diplomatically, promising to cooperate.
• Request the written complaint and supporting documentation.
• Study the deal jacket and records.
• Settle minor matters.
• Consult your attorney for serious matters.
Advertising
Basic Test

1. Does the advertisement have the tendency or capacity to mislead a consumer?

2. If yes, the ad could cause a problem.

A consumer, for advertising purposes, is a person of reasonable intelligence.
### Deceptive Advertising Penalties

<table>
<thead>
<tr>
<th>State</th>
<th>Year</th>
<th>Penalty</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vermont</td>
<td>2012</td>
<td>$16,000</td>
</tr>
<tr>
<td>Washington</td>
<td>2011</td>
<td>$55,000</td>
</tr>
<tr>
<td>Arizona</td>
<td>2010</td>
<td>$195,000</td>
</tr>
<tr>
<td>Massachusetts</td>
<td>2012</td>
<td>$225,000</td>
</tr>
<tr>
<td>Missouri</td>
<td>2012</td>
<td>$540,000</td>
</tr>
<tr>
<td>New York</td>
<td>2011</td>
<td>$800,000+ (55 dealers)</td>
</tr>
</tbody>
</table>
Common Advertising Issues

- Truth in Lending/Leasing.
- Bait advertising.
- Pricing.
- Rebates.
- Trade-in value.
- Zero down.
- Disclaimers and expiration dates.
- Terminology.
- Comparison advertising.
- Contests and promotions.
What Should a Dealer Do?

• Ask legal counsel to review advertising.
• FTC Website
• Check with the state Attorney General’s office for advertising guidelines.
• Check with state dealer association for advertising guidelines.
• Ask advertising firm about its due diligence.
Advertising Enforcement
Since March 2012, the FTC has engaged in 7 separate rounds of advertising enforcement against 23 auto dealerships in 15 states.

<table>
<thead>
<tr>
<th>Alabama (1)</th>
<th>Michigan (1)</th>
</tr>
</thead>
<tbody>
<tr>
<td>California (5)</td>
<td>Nevada (2)</td>
</tr>
<tr>
<td>Connecticut (2)</td>
<td>North Carolina (2)</td>
</tr>
<tr>
<td>Florida (1)</td>
<td>Ohio (1)</td>
</tr>
<tr>
<td>Georgia (1)</td>
<td>South Dakota (1)</td>
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<tr>
<td>Illinois (1)</td>
<td>Texas (2)</td>
</tr>
<tr>
<td>Maryland (1)</td>
<td>West Virginia (1)</td>
</tr>
<tr>
<td>Massachusetts (1)</td>
<td></td>
</tr>
</tbody>
</table>

The actions involved ads over all types of advertising mediums.
Types of Actions

Deception Violations
- Negative Equity Payoff Claims
- Pricing Claims
- Prize Promotion Claims
- Purchase v. Lease Claims

TILA/CLA Violations
- Failure to include required disclosures
- Failure to ensure disclosures are “clear and conspicuous”
Pricing Claims

- $0 Due at Lease Inception/$0 Down
- Availability of Advertised Price
- Balloon Payments
- Matching Tax Refunds
- Introductory “Teaser” Rates
- Limitations on APR
Operation Ruse Control (ORC)

- Announced March 26, 2015
- Involved FTC and 32 law enforcement agencies
- Described by FTC as –
  - “nationwide and cross border crackdown to protect consumers when purchasing or leasing a car, encompassing 252 enforcement actions”
  - “252 enforcement actions [that] were brought against dishonest car dealers”
ORC Actions at a Glance

- 65 of 252 actions were brought in Canada
- Remaining 187 actions were brought at both federal and state level and involved both civil and criminal charges
- Actions date back to January 2014
- Actions involved –
  - Dealers (both licensed and unlicensed)
  - Dealer employees
  - Service providers
  - Auto finance companies
  - Auto title lending companies
  - Auto loan modification companies
  - An auto parts manufacturer
Recommended

Driven

A DEALER GUIDE TO
Federal Advertising Requirements
Unfair and Deceptive Acts and Practices (UDAP)
UDAP Rule

HAS THE *TENDENCY*

OR

*CAPACITY*

TO MISLEAD A

CONSUMER
Application of UDAP

• Federal Trade Commission.
• CFPB.
  – UDAAP – additional word – Abusive.
• State Attorneys General.
• Class Actions.
• Consumer Actions.
UDAP Violations

- Payment Packing
- Advertising
- Spot Delivery (Yo-Yo Sales)
- Discrimination
- Bait and Switch
- Over Exaggeration
- Simulating Government Agency
- High Pressure Sales Tactics
- Free Conditions
- Prize Promotions
- Going Out Of Business Sales
- Negative Options
- Deceptive Services
- Direct Mail

- Simulated Checks
- Trade In
- Cash
- Rebate
- Coupon
- Pay Off on Trade In
- Bank Fee
- Extended Service Agreements
- Car Care Service Plan
- Delivery Fees
- Packs
- Reserve
- N/A = National Average
UDAP Violations

- Misrepresenting the Residual Factor
- Use of N/A
- Equity Build Up
- 3 Day Right of Rescission
- Dealer Preparation
- Multiple Security Deposits
- Different methods and assumptions to calculate payments
- Money Factor vs. Interest Rate
- Taxes and fees
- Lessee pay all taxes up front
- Battery, Tire, Lease Fees
- Sales and use taxes
- Decreasing Term Life Insurance
- Decreasing Disability Insurance
- Decreasing Credit Life Insurance
- Unemployment Insurance
- Payment Interruption Insurance
- Negative Equity
- Mercenary Sales
- Yield Spread Premium
- Residual Based Financing
- Many others
Deal Jackets and Documents
<table>
<thead>
<tr>
<th>Four Square</th>
<th>Notice to Cosigner</th>
<th>Lease Contract</th>
</tr>
</thead>
<tbody>
<tr>
<td>Menu</td>
<td>Waiver of Service Contract</td>
<td>GAP Agreement</td>
</tr>
<tr>
<td>Buyer’s Order</td>
<td>We Owe (Due Bill)</td>
<td>Service Contract</td>
</tr>
<tr>
<td>Retail Installment Sale Contract</td>
<td>Vehicle Appraisal</td>
<td>Vehicle History Disclosure</td>
</tr>
<tr>
<td>Buyer’s Guide</td>
<td>Addendum Sticker</td>
<td>Memorandum of Understanding</td>
</tr>
<tr>
<td>Privacy Notice</td>
<td>Power of Attorney</td>
<td>Monroney Label</td>
</tr>
<tr>
<td>Report of Cash Payments</td>
<td>Payoff Verification</td>
<td>Credit Insurance Contract</td>
</tr>
<tr>
<td>Credit Application</td>
<td>Odometer Statement</td>
<td>Life Insurance Contract</td>
</tr>
<tr>
<td>Statement of Credit Denial</td>
<td>Agreement to Provide Insurance</td>
<td>Etch and Tire Insurance</td>
</tr>
<tr>
<td>Arbitration Agreement</td>
<td>Bailment Agreement</td>
<td>Rebate Form</td>
</tr>
</tbody>
</table>
Document Law

- In Addition to UDAP.
- Finance contract: TILA, Reg. Z, RISA, contract law, UCC, UDAP.
- Lease contract: CLA, Reg. M, contract law, UCC, UDAP.
- Buyer’s order: UDAP, UCC, contract law.
- Credit application: FCRA.
- Service contract: Magnuson-Moss.
Document Management

• Last defense to a complaint, CID, subpoena, or an investigation.
• They need to be current and correct.
• Maintain only necessary documents in the deal jacket.
  – Discard the rest.
Additional Recommendations
Recommendations

• Establish a Compliance Management System.

• Appoint a compliance officer.

• Compliance officer should become certified through a training program.

• Take advantage of free sources of compliance information and support.

• Rely on reputable vendors that can substantiate their due diligence.
Recommendations

• Use standardized documentation.
• Know minimum legal and regulatory requirements.
• Internally audit transactions.
• Conduct regulatory reviews at the direction of your compliance officer.
• Review document management procedures.
Recommendations

• Discuss all products with every customer.
• Subscribe to compliance and industry periodicals.
• Maintain menu log.
• Adopt the NADA’s Fair Credit Compliance Policy & Program.
• Adopt NADA’s Advertising Guidelines
• Require a signed menu of the final transaction.
Recommendations

• Invest in ongoing training.
• Protect against rogue employees.
• Document management procedures.
• Hire an attorney who understands car law.
• Utilize a consultant.
• Beware of payment packing and the common illegal practices.
Compliance Management System

- Establish a compliance program.
- Establish a board with management oversight.
- Appoint a permanent compliance officer who reports to that board.
- Respond to consumer complaints with a protocol.
- Have routine audits examining how the program is functioning and can be improved.
Compliance Management System

- It does not have to be expensive.
- But, it requires planning and documentation.
- Especially documentation.
- Show the world that you are paying attention to the law.
Responding to an Investigation
Responding to an Investigation

- Always agree to cooperate.
- Study the problem.
- Request all documentation from agency.
Responding to an Investigation

• Contact superiors.
• Hire a lobbyist.
• Don’t overreact.
• Seek to participate in wording of any press release or settlement agreement.
• Maintain contact with that agency or AGO.
Responding to a Subpoena

• Request a meeting.
• Attempt to limit extent of subpoena.
• Rolling production of documents.
At the Meeting

• Agree to cooperate.
• If you are in error, admit the error.
• Attempt to educate.
• Be prepared to offer a reasonable resolution.
• Explore the issues.
• Demonstrate your due diligence.
H.R. 1737

• “Reforming CFPB Indirect Auto Financing Guidance Act”
• Introduced April 13, 2015
• Nullifies CFPB Bulletin 2013-02
• Requires that, prior to issuing future guidance on any topic related to indirect auto financing, the Bureau must -
  • Provide for public notice and comment
  • Make publicly available all studies, data, methodologies, analyses, and other information relied upon by CFPB in preparing such guidance
  • Consult with the FRB, FTC, and DOJ
• Study the cost and impact of the guidance on consumers as well as women-owned, minority-owned, and small businesses
On June 25, 2015, the U.S. Supreme Court held that a “disparate impact” theory of liability exists under the Fair Housing Act.

Did the court pave the way for similar actions under the Equal Credit Opportunity Act?

When will this issue be resolved?
“Three of the nation’s largest indirect auto lenders are poised to limit discretionary pricing for dealers after regulators accused them of allowing partners to mark up loans at higher rates to minorities, according to confidential documents.”

AHFC Response
Entered into Consent Order (7/14/15)

Toyota Financial Response
“Toyota Financial said it ‘currently has no plans to change our pricing model’ despite the order.’

- Automotive News (7/1/15)

NMAC Response
“...The discussions are exploratory in nature as we work to protect our customers’ ability to choose financing options that fit their specific needs and to negotiate the best rates possible.”

- Automotive News (7/1/15)
American Banker

CFPB

“The significant limitation of dealer discretion, which in turn reduces fair lending risk, is one of the goals we have been seeking with respect to the indirect auto matters, and this settlement proposal attains this goal.”
Recommended Action

- **Key Features**
  - Rebranded
  - Optional
  - Modeled on a DOJ fair credit risk mitigation program
  - Involves establishing a Standard DP Rate and only deviating for preset legitimate business reasons
  - Requires training, review, oversight, and reporting

- Available at [www.nada.org/faircredit](http://www.nada.org/faircredit)
Regulation through Enforcement

“[DOJ and the CFPB] announced today a groundbreaking settlement....”

“The settlement is especially noteworthy because of the company’s commitment to significantly limit the discretion of car dealers to charge interest rate markups on Honda loans.”

“Honda’s proactive decision to move to a new pricing and compensation system demonstrates industry leadership and represents a significant step towards protecting consumers from discrimination.”

“...other auto lenders should take note of today’s action....”

“We hope that Honda’s leadership will spur the rest of the industry to constrain dealer markup to address discriminatory pricing.”

DOJ Press Release (7/14/15)
Emerging Area

- Advertising that the dealership has conducted a safety inspection or certification on a used vehicle when –
  - the vehicle is subject to an open safety recall, and
  - this fact is not disclosed.

- Consider prominently disclosing in such ads any qualifying information such as –
  - the fact that the advertised vehicle may be subject to recalls for safety issues that have not been repaired, and
  - how consumers can determine whether the advertised vehicle is subject to an open recall (www.safercar.gov).

- Consult with legal counsel on appropriate actions for your dealership.
Questions?