

September 5, 2014

Auto Initiative Update and Next Steps

Internal – Sensitive and Pre-decisional
Confidential Supervisory Information



Consumer Financial
Protection Bureau

Progress Toward the Two Key Objectives of the Auto Initiative

1. Addressing Discrimination

- Tools:
 - Compliance bulletin
 - Supervisory / Enforcement activity covering [REDACTED] of market
 - Ally public consent order
 - [REDACTED] confidential MOUs
- Outcomes:
 - Broad adoption of robust CMS
 - Broad adoption of consumer remuneration ([REDACTED])
 - Broad consideration of alternative structures
 - [REDACTED] adopted NDC
 - [REDACTED] adopted lower caps
 - [REDACTED] adopted lower caps

2. Encouraging Alternatives

- Tools:
 - Compliance bulletin
 - Ally public consent order
 - [REDACTED] confidential MOUs
 - Industry engagement
- Outcomes:
 - [REDACTED] adopted lower caps
 - [REDACTED] CEO indicated an intent to move to flat fees
 - [REDACTED] internal task force is preparing for conversion to flat fees “when inflection point in the market occurs”
 - Enhanced dealer compliance
 - Broad desire for global resolution

Next Steps Toward the Two Key Objectives of the Auto Initiative

1. Addressing Discrimination

- Tools (upcoming developments):
 - Comprehensive Compliance Statement (Supervisory Highlights: Auto Edition) – 9/18
 - Release of proxy whitepaper and refined code
 - Supervisory Activity
 - Completion of [REDACTED] confidential MRAs
 - Larger Participant Rule: Auto – 9/18
 - Completion of [REDACTED] confidential MOU
 - Completion of [REDACTED] confidential MOU
 - [REDACTED] PARR letters
 - Information requests to [REDACTED]
 - Enforcement Activity
 - Fifth Third public enforcement action
 - Non-bank PARR letters (Honda, [REDACTED], Toyota, and [REDACTED]) and potential enforcement actions

2. Encouraging Alternatives

- Tools (upcoming developments):
 - Comprehensive Compliance Statement (Supervisory Highlights: Auto Edition) – 9/18
 - Message re Alternatives: the Bureau is supportive of NDC and lower caps
 - Upcoming supervisory and enforcement resolutions provide opportunities to implement alternatives
 - Anticipated DOJ public enforcement actions
 - [REDACTED] (FDIC referral)
 - [REDACTED]
 - Industry engagement
 - Dialogue with trades, lenders – ongoing
 - RC Address to NADA Regulatory Affairs Cmtee – 9/9
 - Auto Field Hearing – 9/18
 - First Auto Industry Convening -- 9/18
 - Second Auto Industry Convening – early October

Three Industry-Generated Proposals for Global Resolution

Retain Discretion and Engage in Robust Dealer Pricing Monitoring

- Past CFPB Statement: *Indirect auto lenders that choose to retain dealer markup and discretionary compensation policies should be aware of the fair lending risks of such policies. They can help protect themselves and their consumers by implementing systems for monitoring and corrective action by:*
 - *sending communications to all participating dealers, stating the lender's expectations with respect to ECOA compliance;*
 - *conducting regular analyses of both dealer-specific and portfolio-wide loan pricing data for potential disparities;*
 - *commencing prompt corrective action against dealers when analysis identifies unexplained disparities on a prohibited basis; and*
 - *promptly remunerating affected consumers.*

Narrow Discretion and Engage in Light Dealer Pricing Monitoring

- 9/18/2014 CFPB Statement: *[Our supervisory activity identified significantly lower caps, of 50 or 100 basis points, in place at some lenders.] These significant limits on discretionary pricing considerably reduced or nearly eliminated markup disparities for the particular product or channel subject to the limit, in some circumstances.*
- Proposed CFPB Message: Narrower discretion allows light dealer pricing monitoring.
 - No dealer-specific pricing analyses
 - No dealer corrective action program
 - Annual portfolio-wide analysis serves as confirmation
 - The incidence of discriminatory disparities is rare/nonexistent, requiring infrequent consumer remuneration
 - Lenders would maintain compliance management systems to monitor for compliance with all federal consumer laws, including ECOA

Eliminate Discretion and Eliminate Dealer Markup Monitoring

- Past CFPB Statement: *Industry participants have identified several possible models of nondiscretionary dealer compensation. One model compensates dealers using the same flat amount for each loan. Under another model, dealers are paid a flat percentage of the amount financed. Alternatively, a lender could develop a hybrid system in which compensation was tied to both the amount financed and the duration of the contract. Both of these latter approaches are examples of nondiscretionary compensation systems that allow for differences in compensation based on loan amount and potentially term and hence differ from a flat fee approach. These are a few examples of potential non-discretionary compensation systems that mitigate fair lending risk. There could be many other possibilities.*
- Proposed CFPB Message: Eliminating discretion eliminates the need for dealer markup monitoring.
 - Lenders would maintain compliance management systems to monitor for compliance with all federal consumer laws, including ECOA

Working Plan Elements

- Supervisory Matters (see attached tracker)
- Enforcement Matters (see attached tracker)
- Supervisory Highlights
- Continued Outreach
- Evaluate Compensation Models
- White Paper on Proxy Method
- Field Hearing
- LP Rule on Auto

Complete Supervisory Highlights (FL/SUP)

- Publish stand-alone issue of Supervisory Highlights regarding resolution of supervisory matters

- Next Steps: FL is currently drafting Supervisory Highlights
 - Pre-Clearance complete
 - Bureau-wide Clearance in progress
 - Final Legal Clearance and Director approval by week of Sept. 8
 - Ready for Publication by September 18
 - Current institutions include: [REDACTED]
Potential institutions include [REDACTED]

- **Goal:** Publication by September 18, 2014

Continued Outreach (Mkts/EA)

- Continuing outreach function with specific institutions and consumer groups on alternative dealer compensation
- Recent/Next Steps:
 - AFSA Law Committee Meeting (6/18 in MN)
 - NIADA (Independent Dealers) Conference (6/24-6/25 in NV)
 - Allied Solutions Conference (7/14-16 in CA)
 - NADA CFPB dialogue re: broad solutions (ongoing)
 - CBA Auto Finance Committee (9/30 in DC; speaking)
 - FICO World Conference (11/12-13 in CA; speaking)
- **Goal:** Continue and maintain open dialogue with relevant stakeholders

Evaluate Compensation Models (RMR)

- Continue evaluation of possible alternative dealer compensation models
- Completed:
 - Evaluate [REDACTED] markdown model (OR)
- Next Steps:
 - Evaluate the impact of the NADA-CFPB straw person: lower cap plus flat fee
 - RMR, SEFL, and Legal are reviewing the new NADA proposal for potential legal issues and whether it would be the optimal obtainable solution
 - Cap reduction analysis underway for [REDACTED] | [REDACTED]
 - Sketch of potential market impact (“white board exercise”) pending
 - Deadline: Complete by end of September
 - Evaluate the impact of adopting a stringent CMS
 - Potential data: Ally, [REDACTED]
 - Deadline: On-going, no deadline
 - ~~Develop responses regarding non-discretionary compensation models, including NADA markdown proposal (No longer relevant)~~
 - Analysis of implemented Pilot programs when data becomes available
- **Goal:** Determine Bureau’s public position on various dealer compensation models.

White Paper on Proxy Method (OR)

- Complete and publish white paper on Bureau's proxy methodology and its accuracy
 - Preclearance completed
 - Bureau-wide clearance underway
- Prepare proxy computer code for publication along with proxy white paper
 - Final edits to code complete and third party validation underway
 - Code and documentation being staged on web platform by T&I developers and reviewed by Legal
- **Goal:** Publish white paper and code on September 18, 2014

LP Rule on Auto (Regs)

- Proceed with larger participant rule for auto finance market
- Announced in Unified Agenda and elsewhere
- RMR is currently developing a proposed rule
 - Deadline: September 18, 2014 Announcement
 - Policy Committee presentation – June 26
 - Bureau-wide clearance complete; reviewing and integrating comments

- **Goal:** Publish larger participant rule September 18, 2014

Field Hearing (EA)

- Host Auto Finance Field Hearing on September 18, 2014
 - Location: Indianapolis
 - Deliverables:
 - Supervisory Highlights
 - LP Proposed Rule
 - Proxy White Paper and Code
 - Follow-on Industry Roundtable
 - Invitation Only
 - 20-25 industry participants
 - Dealers; Lenders; Captives; other Federal Agencies
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- **Goal:** Host auto finance field hearing on September 18, 2014