

**Statement of the National Automobile Dealers Association**  
*A Hearing Entitled*  
**“Examining Legislative Proposals to Preserve Consumer Choice  
and Financial Independence”**  
**Before the House Financial Institutions and Consumer Credit Subcommittee**  
**June 11, 2015**

Mr. Chairman, thank you for the opportunity to submit the comments of the National Automobile Dealers Association (NADA) to the hearing record. NADA is a national trade association that represents 16,000 franchised new car and truck dealers and collectively employs more than one million individuals. NADA members are primarily engaged in the retail sale and lease of new and used motor vehicles, and also engage in automotive service, repairs, and parts sales. Last year America’s franchised new car and truck dealers sold or leased approximately 16.5 million new cars and light duty trucks. NADA members operate in every congressional district in the country, and the majority of our members are small businesses as defined by the Small Business Administration.

**The Auto Industry Strongly Supports H.R. 1737**

In 2013, the Consumer Financial Protection Bureau (CFPB) issued guidance which threatens to eliminate a dealer’s flexibility to discount the annual percentage rates (APRs) offered to consumers to finance vehicle purchases.<sup>1</sup> The CFPB is attempting to change the \$907 billion auto financing market and limit competition *without* prior public comment and *without* analyzing the impact of its guidance on consumers.

With the CFPB’s actions likely to raise the cost of credit for car buyers, Congress should pass H.R. 1737, the “Reforming CFPB Indirect Auto Financing Guidance Act”, introduced by Reps. Guinta (R-NH) and Perlmutter (D-CO). The bill would rescind the CFPB’s flawed auto finance guidance and make the Bureau more transparent and accountable when issuing any such guidance in the future.

NADA, along with the trade associations representing businesses that make, sell, finance, auction and service motor vehicles, strongly supports H.R. 1737.<sup>2</sup> The open and transparent process required by H.R. 1737 would help determine whether the CFPB’s new auto financing policy is based on accurate analysis and is in the best interest of consumers.

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<sup>1</sup> CFPB Bulletin 2013 – 02, issued March 21, 2013: [http://files.consumerfinance.gov/f/201303\\_cfpb\\_march -Auto-Finance-Bulletin.pdf](http://files.consumerfinance.gov/f/201303_cfpb_march -Auto-Finance-Bulletin.pdf)

<sup>2</sup> See attached letter of support from NADA, the Alliance of Automobile Manufacturers, the American Financial Services Association, the American International Automobile Dealers Association, the Recreational Vehicle Dealers Association, the Recreational Vehicles Industry Association, the National Auto Auction Association, the Motorcycle Industry Council, and the National Independent Automobile Dealers Association.

## **Broad Bipartisan Support For H.R. 1737**

H.R. 1737 currently has 89 bipartisan cosponsors (49 R, 40 D) with strong support from Members across the political spectrum, including many Members of the House Financial Services Committee. The bill is identical to H.R. 5403, introduced by Reps. Stutzman (R-IN) and Perlmutter (D-CO) last Congress, which garnered 149 cosponsors (92 R, 57 D) including 30 Members of the House Financial Services Committee (19 R, 11 D). H.R. 5403 was a narrower version of another CFPB guidance transparency bill (H.R. 4811) which passed the House Financial Services Committee by a bipartisan vote of 35-24 on June 11, 2014.

## **Consumer Benefits of Dealer-Assisted Financing**

Dealer-assisted financing makes credit more readily available, makes credit cheaper, and saves Americans millions of dollars every year. The current dealer-assisted financing system offers access to thousands of banks, credit unions and other lenders all vying to provide vehicle financing to consumers. That access is what keeps the auto financing market so competitive. The automobile dealer's ability to "meet or beat" its competitors' rates produces vigorous marketplace competition that benefits consumers. In fact, a majority of car buyers choose to finance their purchases through optional, indirect financing at dealerships.

Dealers often discount interest rates to earn a customer's business. The CFPB's 2013 auto finance guidance threatens to eliminate a consumer's ability to get a lower rate at a dealership by pressuring finance sources into changing the way they compensate dealers to a "flat fee" that dealers cannot discount. This new approach would eliminate a dealer's ability to "meet or beat" a competitor's finance rate and, in the process, would limit the market competition that frequently provides customers a better APR than those offered by banks or credit unions.

Dealerships, of course, incur costs for serving as the "storefront" for banks, credit unions, and finance companies. Dealers only make a "profit" (which is often limited because dealers frequently lower their own compensation in order to discount the APR to beat a competitor's rate) after paying fixed costs, including: advertising, payroll, overhead, and regulatory compliance costs. This fact refutes false claims that dealer-assisted finance results in an "overcharge" to consumers.<sup>3</sup> Dealer reserve is simply the dealer's retail margin for arranging affordable and competitive financing<sup>4</sup> and represents the recovery of costs that any retailer of credit would necessarily incur.

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<sup>3</sup> Glenn Kessler, *Warren's False Claim that 'auto dealer markups cost consumers \$26 billion a year'*, Washington Post, (May 5, 2015). See also NADA, [CRL's 2011 Analysis of Dealer-Assisted Financing is Flawed and Untrue](#).

<sup>4</sup> Contractual caps between dealers and lenders limit the amount of dealer reserve, generally at about 2 percent. (Loans with longer terms typically have lower percentage rate caps than loans with terms of five years or less intense competition in the vehicle financing industry frequently prevents dealers from charging the full amount of dealer reserve permitted by their finance sources.)

## **Need For the Legislation (H.R. 1737)**

The CFPB released its guidance on March 21, 2013 without prior notice or an opportunity for public comment, alleging a “significant risk” that dealer-assisted auto financing was having a “disparate impact” on the price of credit charged to consumers in protected classes. This controversial guidance pushes auto finance sources into changing the way they compensate dealers to a flat fee approach that dealers could no longer discount for customers.

Auto dealers are committed to fair credit practices that benefit all consumers, and we believe that discrimination is completely unacceptable in auto financing or anywhere else. Dealers have demonstrated this commitment by proposing a comprehensive compliance program, based on a model developed by the U.S. Department of Justice (DOJ), to protect against unintentional discrimination while preserving the benefits of a competitive auto-finance market.<sup>5</sup>

The CFPB has based its guidance on allegations of fair credit violations without providing its complete analysis or documentation. Careful study of the CFPB guidance, however, reveals that the CFPB’s attempt to regulate auto dealers by pressuring lenders to change their business practices (1) does not address the fair credit problem the CFPB alleges<sup>6</sup>; and (2) would eliminate the ability of dealers to further discount credit in the showroom which, in turn, would likely raise credit costs and decrease access to credit for consumers.

The CFPB’s effort to eliminate dealer flexibility to offer consumers a discounted interest rate when arranging auto financing hurts consumers for two reasons. First, the CFPB is denying many customers an opportunity to receive a lower APR in the showroom. Second, a dealer’s ability to undercut competitors from a bank, credit union or another dealer puts a downward pressure on all auto loan interest rates. This downward pressure from many competitors benefits consumers.

## **CFPB’s Attempt to Fundamentally Change and Regulate the Auto Loan Market Via Guidance**

In addition to the harm the CFPB’s new policies would cause consumers, Congress should take notice that the CFPB is bringing about these detrimental changes via “guidance,” thus avoiding both the rulemaking process and coordination with the federal agencies that Congress vested with exclusive federal authority over motor vehicle dealers.<sup>7</sup>

Through its guidance, the CFPB is attempting to significantly alter the operation of a large and efficient market without following the standard rulemaking process and without considering stakeholder input, public comments, and cost/benefit analysis that are associated with it. By avoiding the rulemaking process, the CFPB did not have to reveal the methodology it employs to

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<sup>5</sup> NADA Fair Credit Compliance Policy and Program, see pgs. 3-4. [www.nada.org/faircreditprogram](http://www.nada.org/faircreditprogram)

<sup>6</sup> NADA, [Fallacy of Flats](#): Beware of Claims that Flat Fees Eliminate a Dealer’s Risk of Violating Fair Credit Laws, (2014).

<sup>7</sup> Section 1029 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) precludes the CFPB from exercising any authority over motor vehicle dealers engaged in indirect financing and further provides that the federal agencies who could exercise jurisdiction over dealers prior to the enactment of section 1029 continue to have authority over dealers.

determine whether disparate impact discrimination exists; convene a panel to ascertain what impact its new policies would have on small business; give the public and affected stakeholders an opportunity to comment on the record; and conduct a cost/benefit analysis.

A CFPB official has characterized the CFPB guidance as “simply [a] restatement of existing law.”<sup>8</sup> However, the guidance could, in fact, fundamentally change how vehicles are financed in our country. The regulatory uncertainty that the guidance has produced within the vehicle financing industry and the numerous unanswered questions from Congress and others concerning the guidance show that it is much more than a restatement of existing law.

### **Provisions of H.R. 1737 – Minimum Safeguards For Transparency**

H.R. 1737 would rescind the CFPB’s flawed 2013 auto finance guidance and allow the agency to reissue it under an open and transparent process.<sup>9</sup> Before issuing new auto finance guidance, H.R. 1737 would require the CFPB to:

- provide notice and a period for public comment;
- make public any studies and analyses upon which the guidance is based;
- consult with the Federal Reserve Board, Federal Trade Commission and Department of Justice; and
- study the cost and impact of the guidance on consumers as well as women—owned, minority—owned, and small businesses.

The CFPB took none of these essential steps before issuing its 2013 auto finance guidance. While most guidance is technical and non-controversial, the CFPB’s auto finance guidance is different, as it threatens to: (1) eliminate a dealer’s ability to discount credit in the showroom; (2) raise credits costs; and (3) push marginally creditworthy consumers out of the auto credit market.

H.R. 1737 is a moderate bill that does not dictate a result or tie the CFPB’s hands. The bill merely ensures transparency and public notice so the public has an opportunity to analyze and comment on the CFPB’s attempt to change the auto loan market.

### **CFPB Has Failed to Answer Direct Questions From Congress For Nearly Two Years**

Despite thirteen Congressional letters sent to the CFPB that were signed by over 90 Members and Senators from both sides of the aisle, the Bureau still has not answered many essential questions about the accuracy of the analyses upon which the CFPB relies and the methodologies it employs.<sup>10</sup> The open and transparent process required by H.R. 1737 would provide a framework for those questions to be answered and would help ascertain whether the CFPB’s policies can withstand objective scrutiny.

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<sup>8</sup> “The Consumer Financial Protection Bureau’s Semi-Annual Report to Congress: Hearing before the Senate Banking, House and Urban Affairs Committee, 113th Cong., 1st Sess. 17 (2013).

<sup>9</sup> Please see the attached chart entitled, “*Adding Appropriate Safeguards to CFPB Guidance, Process required under Standard APA/Dodd-Frank Rulemaking vs. H.R. 1737*” to compare the differences between the procedures for a rulemaking and the less stringent procedures required by H.R. 1737.

<sup>10</sup> These letters can be accessed at: <https://www.nada.org/CustomTemplates/GeneralPage.aspx?id=21474838453>

The process for issuing guidance established in H.R. 1737 is consistent and in accordance with OMB's practices on agency guidance documents.<sup>11</sup> The Bulletin on "Agency Good Guidance Practices" sets forth general policies and procedures to ensure that guidance documents of Executive Branch departments and agencies are developed with appropriate review and public participation, accessible and transparent to the public, and of high quality.

### **Need for CFPB to Use Accurate and Transparent Analysis to Support Policy Decisions**

The CFPB has based its auto finance guidance on its claim that there is a significant risk of disparate impact discrimination in dealer-assisted financing. After multiple Congressional calls for additional information, in September 2014 the CFPB released a white paper concerning one element of its analysis – the use of proxy methodology to identify members of protected classes for use in determining whether disparate impact is occurring in indirect auto financing.

The scope of the CFPB's white paper, however, is very limited. It is confined to an analysis of how the CFPB determines the probability that a consumer is a member of a particular group. It does not address how the CFPB uses those probabilities to calculate either pricing disparities or the margin of error surrounding those disparities.

The CFPB's white paper also does not address the essential question of what analytical controls the CFPB uses to ensure that the consumers it is comparing are "similarly situated." And, even with regard to its primary purpose, the CFPB's own testing indicates that its proxy method, the Bayesian Improved Surname Geocoding (BISG) method, frequently fails to accurately reflect a consumer's actual race or ethnicity.

Importantly, the white paper does not reveal how the CFPB corrects these problems to ensure its classification of consumers is accurate. In a statement dated September 17, 2014, the three trade groups that represent U.S. new-car dealers – NADA, the National Association of Minority Automobile Dealers, and the American International Automobile Dealers Association – explained that, even after publication of the CFPB's white paper,

"many of the questions that Congress and others have asked remain unanswered. We look forward to rigorous peer review to ensure that the tools the CFPB is using to address fair credit concerns may actually accomplish its goals. There are legitimate, market-based reasons for disparities in interest rates - from monthly budget constraints, to the presence of more competitive offers, to inventory reduction considerations - all of which are nondiscriminatory and all of which can be documented in the transaction."

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<sup>11</sup> See OMB bulletin entitled "*Final Bulletin for Agency Good Guidance Practices*," issued Jan. 18, 2007. The bulletin states: "Pre-adoption notice-and-comment can be most helpful for significant guidance documents that are particularly complex, novel, *consequential*, or *controversial*." (emphasis added).

## **Questionable Accuracy of CFPB's Methodology to Determine Fair Credit Risk**

Despite multiple calls by Congress to disclose the statistical model and analysis the CFPB uses to allege disparate impact, the CFPB's release of supporting public analysis or documentation on the guidance remains limited. To test the accuracy of the CFPB's method, a study by a prominent research firm, Charles River Associates (CRA), evaluated the CFPB's methodology for measuring pricing disparities in auto finance and found several significant flaws that show the CFPB's methodology to be inaccurate, incomplete, and unreliable.

It should be noted federal law prohibits a creditor from considering or inquiring into the race or ethnicity of the borrower when extending auto credit. Therefore, to establish the race or ethnicity of the borrower, CFPB acknowledged that it relies on "proxies." The proxy method used by the CFPB is the BISG method. This statistical method makes a best guess of the borrower's race or ethnicity based on the borrower's last name and address.

CRA applied BISG to a large database of consumer mortgage transactions, where each borrower's race and ethnicity is known. The CRA study found that the CFPB's method frequently fails to correctly identify a consumer's actual race or ethnicity. For example, the study found that the CFPB's proxy methodology overestimates the number of African-Americans by 41 percent.<sup>12</sup> One of the errors that led to this miscalculation was that the CFPB incorrectly assumed the population of applicants for vehicle financing and the general population in a given zip code were the same.

Further, the CRA study determined that the CFPB's methodology is incomplete since it does not consider legitimate business reasons why dealer discounts may vary among consumers. For example, the CFPB does not consider that dealers routinely try to "meet or beat" a competing offer from a bank, credit union, or another dealer to gain a customer's business. Dealers also will discount an interest rate to move a slow-selling model. The Department of Justice has accepted these reasons as legitimate to explain disparities in credit pricing, yet the CFPB refuses both to acknowledge these neutral factors and to provide its rationale for rejecting them.

The CFPB is aware its methodology is unreliable, yet it continues to rely on flawed assumptions. Despite acknowledging its methodology overestimates some minority groups (the CFPB's own September 2014 white paper reveals that its methodology overestimates the African American population by 20 percent),<sup>13</sup> the Bureau continues to threaten enforcement actions against auto lenders in an attempt to eliminate or limit dealer discounts in the showroom.

CFPB Director Richard Cordray publicly disagreed with the conclusions of the CRA study, but did not state any basis for his disagreement. To date, the agency has yet to formally respond to this study, and it appears unlikely it ever will do so.<sup>14</sup>

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<sup>12</sup> Charles River Associates, *Fair Lending: Implications for the Indirect Auto Finance Market* at 4 (Nov. 2014).

<sup>13</sup> Consumer Financial Protection Bureau, *Using publicly available information to proxy for unidentified race and ethnicity: A methodology and assessment* at 14 (2014).

<sup>14</sup> *The Consumer Financial Protection Bureau's Semi-Annual Report to Congress: Hearing before the House Financial Services Committee*, 114<sup>th</sup> Cong., 1<sup>st</sup> Sess. (March 3, 2014). CFPB Director Richard Cordray stated at the hearing when questioned on the Charles River study: "We don't find some obligation

The current system of dealer-assisted financing is fair, competitive, and boosts access to affordable credit for consumers. Any disruption in this highly efficient model can only be justified if supported by reliable data and objective analysis. These significant flaws in the CFPB's policy could have been avoided if the Bureau had employed a process that was data- and market-driven and transparent. H.R. 1737 would provide that needed transparency.

### **The Ally Settlement - Based on Flawed Methodology?**

The CFPB's failure to rebut the CRA study is troubling, particularly since it has taken enforcement actions based on a methodology that has been shown to be unreliable in the area of auto finance. On December 20, 2013, the CFPB announced consent agreements into which the CFPB and the DOJ entered with Ally Financial, Inc. and Ally Bank (Ally), a major indirect auto lender, in a case which involved allegations of fair credit violations. The CFPB issued a press release stating "[t]he CFPB and DOJ determined that more than 235,000 minority borrowers paid higher interest rates for their auto loans between April 2011 and December 2013 because of Ally's discriminatory pricing system."<sup>15</sup> Yet, according to aspects of the proxy methodology the CFPB has chosen to reveal to Congress, the "235,000 minority borrowers" exist only as a probability, despite the CFPB presenting this figure in its press release as the *actual* number of minority consumers who were allegedly harmed. The CFPB's assertions of fact in its press release demonstrate why it is important for the CFPB to reveal the accuracy of the methodologies supporting its assertions.

The Ally consent agreement is not proof that the CFPB's drive to eliminate a dealer's ability to discount credit in the showroom is justified. Based on facts listed below, the Ally consent agreement appears simply to be a rational business decision made in the current regulatory atmosphere. We urge the Committee to consider the following facts:

- Ally admitted no wrongdoing in its settlement, and stated that it believed it and the dealers with which it does business did nothing wrong.<sup>16</sup> In fact, Ally could not further rebut the CFPB's assertions of fair lending violations because the Bureau refused to disclose to Ally how it calculates fair lending bias.<sup>17</sup>
- The case against Ally was based entirely on statistics and methodologies which have not been fully revealed publicly or to Congress. The public still does not know whether the Bureau takes into account legitimate factors that can affect finance rates – for example, a dealer's ability to lower its interest rate to meet a competitive offer or the customer's monthly budget constraints. Indeed, Ally released a statement when the consent order was announced saying that "based on the company's analysis of its business, it does not believe that there is measurable discrimination by auto dealers."<sup>18</sup> This statement is evidence that

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to respond to studies out there all the time in all aspects of our work."

<sup>15</sup> Press Release by the CFPB, "*CFPB and DOJ Order Ally to Pay \$80 Million to Consumers Harmed by Discriminatory Auto Loan Pricing*," (Dec. 20, 2013).

<sup>16</sup> Ally Financial Statement on Auto Financing Consent Orders, Dec. 20, 2013.

<sup>17</sup> *Consumer Financial Cover-Up – An agency won't tell employers or Congress how it calculates bias*," Wall St. Journal, (Mar. 17, 2014.)

<sup>18</sup> Ally Financial Statement on Auto Financing Consent Orders, Dec. 20, 2013.

CFPB did not perform a comprehensive regression analysis (i.e., one that includes all the relevant factors, not simply those chosen by the CFPB).

- Three days after the Ally consent order, the Federal Reserve Board approved Ally's application to become a financial holding company, enabling Ally to continue offering insurance products and other services that Ally might have been forced to discontinue. According to the *Wall Street Journal*, “Standard & Poor's Ratings Services... warned it would potentially lower the company's ratings if it failed to secure financial holding company status.”<sup>19</sup>
- According to *Automotive News*, “the CFPB was one of a number of regulators that had input on the Federal Reserve's decision on financial holding company status.” An Ally official stated that “[n]o investor publically was going to invest in us unless we got financial holding company status. And we could not do that without coming to terms with the CFPB.”<sup>20</sup>
- On March 27, 2013, Ally announced an initial public offering where the U.S. government “would sell the bulk of its stake in the company.”<sup>21</sup> (At the time of the consent order, the U.S. government had a 64 percent controlling interest in Ally.)

Although the consent order with Ally was reached over sixteen months ago, none of the \$80 million Ally paid to the CFPB as part of the settlement has been distributed to consumers. According to the *New York Times*, “One reason for the delay...is that federal authorities have found it complicated to determine which Ally customers are minorities...”<sup>22</sup>

The fact that the funds have not been distributed raises serious concerns regarding the reliability of the CFPB’s methodology and its certainty in forcing a settlement with Ally in 2013.

### **Assessing the Consumer Impact of the CFPB’s Guidance - Eliminating a Consumer’s Ability to Receive a Discounted Auto Loan**

The government’s potential elimination of the dealer’s ability to discount credit in the showroom threatens to lessen competition, thereby reducing the availability of credit and costing consumers money. In its place, the CFPB wants to create an inflexible pricing structure that would wipe out a consumer’s ability to get a dealer to “meet or beat” the best financing rate the consumer can get from another finance source. This ill-advised scheme would result in less competition, higher financing rates, and the loss of access to credit for many consumers. As a result, many consumers the CFPB is purportedly attempting to help would actually be harmed.

Section 1022 of the Dodd-Frank Act requires the CFPB to consider, when issuing a rule, the potential benefits and costs (including the potential reduction of consumer access to financial products and services) that could be caused by such a rule. One consequence of its avoiding the

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<sup>19</sup> Andrew Johnson, “*Ally Receives Fed Approval for Financial Holding Company Status*,” *Wall St. Journal*, Dec. 23, 2013.

<sup>20</sup> Jim Henry, “*Ally won't be a 'Trojan horse' -- Lender sticks with dealer reserve, defies CFPB*,” Feb. 3, 2014.

<sup>21</sup> Tanya Agrawal, “*U.S. government to sell most of Ally Financial stake in IPO*,” *Reuters*, Mar. 27, 2014.

<sup>22</sup> Michael Corkery, Jessica Silver-Greenberg, *Prosecutors Scrutinize Minority Borrowers’ Auto Loans*, *N.Y. Times*, Mar. 30, 2015.

rulemaking process is that the CFPB avoids having to conduct, and does not benefit from, a study into the potential impact its new policy would have on consumers. In response to a letter sent by 22 Senators, the CFPB acknowledged that it never studied how eliminating a dealer's ability to discount credit would affect the cost of credit paid by consumers.<sup>23</sup> Reducing a strong competitive force from the vehicle financing marketplace will likely raise the cost of credit for consumers.

Together, the weakening of competition and higher regulatory costs can be expected to result in higher credit costs for consumers. And, most troubling, the CFPB's actions could disproportionately hurt consumers with less-than-perfect credit since those customers will be less able to afford any higher rates and will therefore have even more limited options to buy a car or truck to meet their work and family needs.

### **CFPB is Pressuring Lenders to Change Practices Yet Takes the Position it is not Establishing New Policy**

The CFPB claims it is not pushing the industry to non-discountable flat fees, and in support of that claim it points to another compliance option in its guidance: constraining dealer discretion accompanied by monitoring. In fact, the CFPB makes actual implementation of this latter option – constraining dealer discretion and monitoring – highly impractical. This option involves “imposing controls” on dealer reserve and then monitoring dealer behavior to ensure that those controls work. However, this option presents several problems for a lender.

First, the CFPB refuses to explain the rules for monitoring – that is, the Bureau will not tell lenders how to ensure they are comparing “apples to apples.” Many aspects of a vehicle financing transaction have nothing to do with the background of the borrower, and these variables could lead to differentials in the amount of compensation a dealer gets paid for originating the financing. These include factors such as:

- the amount financed;
- the presence of a competing offer from another financing source;
- the borrower's budget constraints;
- the length of the loan; and
- the presence of a manufacturer subvention of the rate (for example, a special promotional program on a certain model vehicle).

If neutral, business-related factors such as these are the reason why the amount of a dealer's finance compensation varies from consumer to consumer, there is no unlawful discrimination. Hence, to do a proper comparison, these variables need to be held constant as part of the

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<sup>23</sup> Letter from the Hon. Richard Cordray, Director, CFPB to Senators Portman (R-OH) and Shaheen (D-NH) (Nov. 4, 2013.)

CFPB's analysis. But the CFPB will not let lenders know which factors, if any, should be held constant in completing a disparate impact review.

Second, the CFPB still refuses to divulge the numerical basis point threshold at which the Bureau concludes that statistically significant pricing disparities exist. The CFPB apparently wants lenders to monitor dealer behavior without stating at what threshold disparate impact begins.

The Bureau's guidance requires indirect auto lenders to estimate which controls and thresholds the CFPB would find appropriate. This lack of clarity indicates there really is no safe harbor that can be achieved through "monitoring." Moreover, the CFPB has stated the analytical controls necessary to measure disparate impact are determined on a "case by case"<sup>24</sup> basis which is contrary to the intent of "guidance" meant to govern the behavior of an entire industry. The CFPB has not offered one example of a discretionary dealer compensation approach that indirect finance sources can adopt which is consistent with its guidance.

### **NADA's Fair Credit Compliance Program**

Despite the fact that the CFPB's fair credit allegations are unsubstantiated, auto dealers are committed to fair and equal credit, and in January 2014, NADA released its *Fair Credit Compliance Policy & Program*.<sup>25</sup> This program is based on a model to manage fair credit risk developed by the DOJ. The DOJ's model is superior to the CFPB's guidance in that it addresses fair credit risk without decreasing competition and harming consumers. The DOJ model has also been embraced by the National Association of Minority Automobile Dealers and the American International Automobile Dealers Association. This compliance program addresses fair credit risk where it matters – in the showroom – while preserving a dealer's ability to discount credit.

The framework of the DOJ model is simple:

- A dealer who adopts the Program establishes a "Standard Dealer Participation Rate" – a standard retail margin – for its dealership;
- In each and every transaction, the dealer adds the Standard Dealer Participation Rate to the bank or finance company wholesale buy rate to establish the retail APR that the dealer offers to all prospective customers; and
- The Standard Dealer Participation Rate, which would generally be a set number of basis points, is the same for every deal and its amount is determined by the individual dealer.

The DOJ prudently recognized that eliminating the discounting of credit in the showroom would deprive consumers of the ability to obtain a lower, discounted rate from the dealer when there is a legitimate business reason for the lower rate, i.e., a reason that is unrelated to the customer's background. (In contrast, the CFPB's guidance could entirely eliminate a

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<sup>24</sup> Letter from the Hon. Richard Cordray to Rep. Colleen Hanabusa (D-HI) 3 (Feb. 6, 2014).

<sup>25</sup> This guidance can be found at [www.nada.org/faircreditprogram](http://www.nada.org/faircreditprogram)

customer's ability to negotiate a lower interest rate in the showroom.) The DOJ model allows for a downward deviation from the Standard Dealer Participation Rate – but only if one of seven good faith, pro-competitive situations is present. Examples of these pro-competition situations include where the consumer has access to a more competitive rate from another dealer or lender or where the consumer has a budget constraint. Thus, the DOJ model addresses fair credit concerns by promoting a standardized approach while preserving flexibility to allow consumers to benefit from today's competitive auto financing marketplace.

## **Conclusion**

The CFPB's 2013 auto finance guidance was issued under a closed process with no transparency. The indirect vehicle financing model is efficient, competitive, and provides access to affordable credit to consumers in all credit tiers. Congress should direct the CFPB to be transparent and seek public input regarding the auto finance guidance to ensure the CFPB is using reliable, complete, and accurate analysis before it tampers with the \$907 billion auto lending market through guidance.

Congress created the CFPB to protect consumers – and a transparent process is the best means to ensure that the CFPB develops policy positions that are in the consumer's best interest. Congress is rightly concerned that the CFPB in its auto finance guidance is:

- pressuring finance sources to move to flat fees, based on information and analysis that has been shown to be flawed;
- denying ordinary Americans the right to negotiate a lower interest rate in the showroom, and the right to seek a better deal;
- dictating the manner and amount of dealer compensation without regulatory, enforcement or supervisory jurisdiction over dealers; and
- proceeding without considering the impact of the guidance on consumers.

Passage of H.R. 1737 would create a process to correct the flawed CFPB auto lending guidance without encroaching on the CFPB's structure, jurisdiction, or authorities. CFPB should be encouraged to work with the impacted stakeholders. The retail auto industry has provided the CFPB with a better approach that directly addresses fair credit risk and preserves market flexibility and competition for the benefit of the consumer.

Mr. Chairman, H.R. 1737 is a modest, bipartisan bill that would require the CFPB to reexamine its flawed auto finance guidance in an open and transparent manner. On behalf of America's franchised auto dealers and their customers, we urge the Committee to pass H.R. 1737.



**AUTO ALLIANCE**  
DRIVING INNOVATION®



**American International  
Automobile Dealers®**



June 10, 2015

Dear Representative:

We, the undersigned organizations who represent businesses that make, sell, finance, auction and service motor vehicles are writing to express our strong support for H.R. 1737, the “Reforming CFPB Indirect Auto Financing Guidance Act.” This bipartisan bill, introduced by Reps. Guinta (R-NH) and Perlmutter (D-CO), would rescind the Consumer Financial Protection Bureau’s (CFPB) flawed 2013 auto finance guidance and allow the CFPB to reissue it under a more transparent and better informed process. This new bill is identical to H.R. 5403, which garnered 149 cosponsors last Congress.

H.R. 1737, drafted by members of the House Financial Services Committee on a bipartisan basis, currently has 62 bipartisan cosponsors. In addition to rescinding the 2013 guidance, H.R. 1737 would require that, prior to issuing any new guidance related to indirect auto financing, the CFPB:

- provide notice and a period for public comment;
- make public any studies, data, and analyses upon which the guidance is based;
- consult with the Federal Reserve Board, the Federal Trade Commission and the Department of Justice; and
- study the cost and impact of the guidance on consumers as well as women-owned, minority – owned, and small businesses.

**This is the entire scope of the bill.** By design, H.R. 1737 does not impinge on the CFPB’s structure, jurisdiction, or authorities.

H.R. 1737 is needed to produce a more informed guidance compared to the 2013 guidance, which lacked public input, transparency, consultation with the CFPB’s sister agencies and, by the CFPB’s own admission, any study of the impact of the guidance on consumers. As a consequence of being issued

without these essential safeguards, the CFPB's guidance could potentially (1) eliminate a dealer's ability to discount credit in the showroom; (2) raise credits costs; and (3) push marginally creditworthy consumers out of the auto credit market entirely.

Apart from the fact that guidance should not be used as a means to make sweeping policy and market changes, the CFPB auto guidance does not effectively manage fair credit risk in the showroom, which is its purported goal. The Department of Justice (DOJ), however, has created a better approach to address fair credit risk without decreasing competition and harming consumers. The DOJ model was used as a template for a comprehensive compliance program that the National Automobile Dealers Association, National Association of Minority Automobile Dealers, and American International Automobile Dealers Association issued last year to their respective members. This compliance program addresses fair credit risk where it matters -- in the showroom -- while preserving a dealer's ability to discount credit.

Thirteen Congressional letters signed by over 90 Members and Senators on both sides of the aisle have been written to the CFPB asking questions and expressing concern regarding its auto guidance. Nonetheless, many essential questions still remain unanswered. The open and transparent process required by H.R. 1737 would provide a framework for those questions to be answered, and to ascertain whether the CFPB's new policy can withstand public scrutiny.

Since the 1920s, credit has been the lifeblood of America's auto industry. H.R. 1737 is a moderate, bipartisan process bill that does not direct a result or tie the CFPB's hands, but merely gives the public an opportunity to scrutinize and comment on the CFPB's attempt to change the auto loan market via "guidance."

**We respectfully ask you to protect consumers and support this good government bill by cosponsoring H.R. 1737.** Thank you for your consideration.

Sincerely,



Peter Welch  
President, National Automobile Dealers  
Association



Mitch Bainwol  
President and CEO, Alliance of Automobile  
Manufacturers



Chris Stinebert  
President and CEO, American Financial Services  
Association



Cody Lusk, AIADA  
President, American International Automobile  
Dealers Association



Frank Hackett  
CEO, National Auto Auction Association



Steve Jordan  
Executive Vice President, National Independent  
Automobile Dealers Association



Phil Ingrassia  
President, The National RV Dealers Association



Richard Coon  
President, Recreation Vehicle Industry  
Association



Tim Buche  
President and CEO, Motorcycle Industry Council

# Adding Appropriate Safeguards to CFPB Guidance

## *Process required under Standard APA/Dodd-Frank Rulemaking vs. H.R. 1737*

<b>Informal APA Rulemaking under Dodd-Frank Act*</b>	<b>H.R. 1737</b>
Public Notice in <i>Federal Register</i> (Must include contents specified in 5 USC § 553(b))	Provide notice and a period for public comment (CFPB decides length of public comment period)
Must make public, at the time of the notice, the studies, data, and analyses upon which the agency relies, and any other information important to providing an opportunity for informed public comment	Make public any studies, data, and analyses upon which the guidance is based
Cost Benefit Analysis (Pertaining to both consumers and covered persons, including the potential reduction of access by consumers to financial products or services resulting from the rule)	Study the cost and impact of the guidance on consumers as well as women-owned, minority-owned, and small businesses (strict cost benefit analysis not required)
Consultation with Other Federal Agencies to Ensure Consistency of Rules	Consult with the Federal Reserve Board, the Federal Trade Commission and the Department of Justice
Regulatory Flexibility Act Analysis/May Require Small Business Advocacy Review (SBREFA) Panels (comprehensive and lengthy process requiring coordination with SBA's Office of Advocacy and OIRA (OMB))	No provision
Statement of Basis and Purpose	No provision
Response to All Significant Comments	No provision
Right to Petition for Repeal of Rule	No provision
Financial Stability Oversight Council (FSOC) Review	No provision

\* Informal APA Rulemakings under the Dodd-Frank Act may require additional process.