DREHER TOMKIES LLP

ALERT

FOR CLIENTS AND FRIENDS OF DREHER TOMKIES LLP

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CFPB ISSUES SUPERVISORY HIGHLIGHTS REGARDING DISCRIMINATION IN AUTO FINANCING

The Consumer Financial Protection Bureau (CFPB) Supervisory Highlights describe the CFPB's experience during the last two years reviewing auto financing and its recommendations for avoiding discriminatory practices. From its review of auto financing, the CFPB concluded that discretionary pricing policies have resulted in discrimination against African-American, Hispanic, and/or Asian and Pacific Islander borrowers in violation of the Equal Credit Opportunity Act (ECOA). According to the CFPB, some creditors use discretionary pricing policies while not adequately monitoring and controlling the fair lending risk associated with these policies.

The targeted ECOA review of auto financing that resulted in the Supervisory Highlights included a review of creditor policies, procedures and fair lending compliance management. CFPB examination teams also conducted statistical analyses of three areas: credit approvals and denials, buy rates and any discretionary markup or adjustment to the buy rate. The CFPB concluded that one indicator of fair lending risk is policies and procedures that allow for broad discretion in underwriting, pricing and compensation decisions. The CFPB recommends strong fair lending compliance management as a preventative measure, including limits on discretionary markups, and self-monitoring, including statistical analyses to identify disparities on a prohibited basis.

The CFPB noted that information on race, ethnicity and sex is typically not collected as part of an auto financing transaction or a transaction involving other non-mortgage consumer credit products. Thus, the CFPB used proxy methods, citing as an example of a common method for proxying the probability that an applicant is Hispanic or Asian, use of the surname database published by the Census Bureau.

According to the CFPB, significant limits on markup, such as a limit of 100 basis points, may reduce fair lending risk and significantly reduce the need for certain compliance management activities. The CFPB found that creditors that did not implement significant controls on discretionary pricing adjustments and did not engage in strong compliance management, often had statistically significant disparities in dealer markup.

The CFPB identified the following features as elements of a strong fair lending compliance program:

- An up-to-date fair lending policy statement;
- Regular fair lending training for all employees involved with any aspect of the institution's credit transactions, as well as all officers and board members;
- Ongoing monitoring for compliance with fair lending policies and procedures;
- Ongoing monitoring for compliance with other policies and procedures that are intended to reduce fair lending risk (such as controls on loan originator discretion);
- Review of creditor policies for potential fair lending violations, including potential disparate impact;
- Depending on the size and complexity of the institution, regular statistical analysis of credit data for potential disparities on a prohibited class basis in pricing, underwriting or other aspects of the credit transaction;
- Regular assessment of the marketing of credit products; and
- Meaningful oversight of fair lending compliance by management and, where appropriate, the institution's board of directors.

Although the CFPB acknowledged that limiting or eliminating discretionary pricing and dealer compensation are not the only ways to mitigate risk, creditors using discretionary pricing and/or dealer compensation should have strong compliance programs and monitoring in place to avoid discrimination.

Creditors should consider the CFPB's recommendations to be prepared for a Fair Lending Review and develop a fair lending compliance program. Do not hesitate to contact us for advice and assistance in developing a strong compliance program. ❑

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