October 25, 2023

The Hon. Rohit Chopra
Director
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552

***Re*: Supervisory Highlights, Issue 30, Summer 2023**

Dear Director Chopra:

The American Financial Services Association (AFSA[1]) appreciates that the Consumer Financial Protection Bureau (CFPB) periodically publishes Supervisory Highlights to share key examination findings. The Supervisory Highlights are helpful to the financial services industry to understand the CFPB's perspective on certain practices. Compliance professionals, for example, can gain insights into new or updated areas of focus in supervisory reviews drawn from specific examinations, if the CFPB provides sufficient details about the facts of the examinations and their analysis of the legal and regulatory requirements affected. The purpose of this letter is to identify areas of concern in the Summer 2023 edition of the Supervisory Highlights that do not provide either sufficient detail about the facts or the analysis of the facts.

Supervisory Highlights are not intended to take the place of regulations, nor should they be used to create new legal obligations. Using the Supervisory Highlights to paint specific actions as unfair or deceptive with broad brushstrokes can be dangerous, especially when the CFPB fails to provide sufficient details about the underlying facts of the investigations or the application of its analysis to those facts. AFSA takes this opportunity to point out one recent example from the Summer 2023 edition of the Supervisory Highlights[2] that covers findings from CFPB supervisory examinations completed from July 2022 to March 2023 in the areas of auto origination, auto servicing, consumer reporting, debt collection, deposits, fair lending, information technology, mortgage origination, mortgage servicing, payday and small dollar lending, and remittances.

The Supervisory Highlights discusses an issue in Section 2.2.1 "Collecting interest on fraudulent loan charges." The issue described by the CFPB is referred to in the industry as "powerbooking" and is not appropriately characterized as "fraudulent loan charges." Powerbooking is not a common practice, and banks, finance companies, and dealers have procedures in place to help reduce this type of fraud. However, in instances where this practice occurs, the CFPB

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[1] Founded in 1916, AFSA is the national trade association for the consumer credit industry, protecting access to credit and consumer choice. AFSA members provide consumers with many kinds of credit, including traditional installment loans, mortgages, direct and indirect vehicle financing, payment cards, and retail sales finance.
[2] Consumer Financial Protection Bureau's Supervisory Highlight, Issue 30, Summer 2023. https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_supervisory-highlights_issue-30_2023-07.pdf

misunderstands both (a) where the fault lies in this practice when identifying it as an "abusive act or practice," and (b) its authority over the practice given that it is unrelated to the consumer transaction and causes no consumer injury.

The term "powerbooking" refers to instances in which an auto dealer misrepresents to the finance source the features of the financed vehicle, i.e., such as whether there are leather seats, a navigation system, or a bedliner in a pickup. From the dealer's perspective, the purpose of this misrepresentation is to overstate the value of the collateral, thus favorably influencing the finance source's decision about whether to purchase a retail installment sale contract, and on what terms. The value of the collateral is a key component of a finance source's evaluation, as it represents the relative strength of the creditor's lien, and the ratio of the credit extended compared to such value (the LTV ratio). The LTV ratio is instrumental in evaluating both the likelihood of default and the severity of the loss for the finance source, were a default to occur. In these situations, it is the finance source that is harmed - the customer and dealer are in possession of the vehicle and know perfectly well what features are on the vehicle and the price of the vehicle with those features. "Powerbooking" is fraud in which the finance source is misled so that it is more likely to approve the deal at all, and so that it will offer <u>more beneficial terms</u> to the customer than the collateral otherwise supports. Ironically, <u>consumers who enter into retail installment sale contracts with dealers who engage in powerbooking should generally get more favorable financing than they would absent the fraud on the finance source.</u>

In the Supervisory Highlights, the CFPB assumes, without discussion and without logical basis, that if the dealer misrepresents the options on a vehicle to the finance source, the dealer must have made the same misrepresentation to the consumer regarding the vehicle *and* sold the vehicle at price consistent with the inflated features. That is simply not the case, especially when the consumer can readily see the vehicle's options when inspecting and test driving the vehicle and agreed to the selling price thereafter.

The CFPB conflates two separate transactions. In the first transaction, the consumer and dealer agree upon a vehicle and negotiate the selling price. In connection with this first transaction, the consumer views and often test drives the vehicle and, thus, is able to observe whether the vehicle has leather seats, a navigation system, or a bedliner, and negotiate the selling price accordingly. Accordingly, features are not misrepresented to the consumer. Based on the negotiated selling price of the vehicle, the dealer and consumer determine the amount of credit (the "loan" amount) needed to complete the transaction (the L in LTV). This occurs before a final request for credit is made to a finance source, and before any "powerbooking" can occur. This sequence means "powerbooking" does not result in an inappropriate inflation of selling price or resulting "loan" amount. Contrary to the CFPB's assertion, this does not injure the consumer – the dealer and consumer agreed upon the vehicle to be sold, the selling price of that vehicle, and amount of credit necessary to purchase that vehicle before the fraud ever occurs.

In the second transaction, the retail installment sale contract is sold by the dealer to the finance company. This is a business-to-business commercial transaction in which the consumer is not involved. Unlike the consumer and the dealer, the finance company has no physical interaction with, or direct information about, the vehicle and the finance company relies on the information provided by the dealer.

The CFPB states that on some occasions finance companies may learn of a misrepresentation regarding the vehicle options from the consumers themselves in an initial onboarding call. If that is the case, it only proves that the consumer was not deceived because they were able to correctly identify the options present on the vehicle. In any event, the CFPB's assumption that a misrepresentation to the finance company must mean that the consumer was deceived is simply incorrect and does not reflect the reality of the vehicle purchase transaction. Again, the sole purpose of the dealer misrepresentation about the options on the vehicle is to deceive the finance company about the risk of the underlying financing transaction and to induce the finance company into approving the application and/or offering more favorable terms for the business-to-business transaction for the purchase of the retail installment sale contract. What the CFPB also fails to note is that where such fraud *is* identified, finance companies will often reject the deal, reprice the deal, or seek to recover the powerbooked amount from the dealer. It should also be noted that for many finance companies, in particular for those financing cars which are not manufactured by an affiliate, there are very few tools available to identify overstatements of collateral options, or they would already be utilized. As described above, powerbooking increases both the frequency and amount of loss to finance companies, so it is in their interest to utilize tools where available to prevent the same

In the Supervisory Highlights, the CFPB concludes that it is an unfair or abusive practice for the aggrieved finance company not to refund interest paid on the inflated value of the vehicle when a finance company discovers the fraud, but the value of the vehicle to the consumer is not inflated – it is negotiated by the consumer and unaffected by subsequent powerbooking. The CFPB's conclusion conflates the two separate transactions (one consumer, one commercial) described above involved in the purchase and financing of the vehicle.

Powerbooking creates no consumer injury in the first transaction and the CFPB does not have authority over the second business-to-business transaction. The dealer and the finance source agree on terms under which the finance source will purchase the retail installment sale contract from the dealer. Any misrepresentation made by the dealer to the finance source about the options on the vehicle when the terms of the business-to-business transaction are determined has no impact on the consumer's understanding of the options on the vehicle or the price they negotiated. The amount that the customer agrees to pay for the vehicle is not affected by any subsequent misconduct directed at the finance source. Neither the Total Sale Price nor the Amount Financed are inflated on the retail installment sale contract and therefore, the consumer suffers no injury – compensable or otherwise -- in a powerbooking event. In fact, because the finance source has no first-hand knowledge of the vehicle, "powerbooking" *solely* harms the finance company – the only injured party to the transaction.

AFSA shares and appreciates the CFPB's interest in reducing fraud. However, we want to make it clear that your concerns with respect to powerbooking as a source of consumer harm are misplaced. The consumer is not the injured party, and the finance source has neither caused nor supported any consumer harm. It is the finance source that is injured by the powerbooking dealer's misrepresentations. Consequently, this misconduct has no place in the Supervisory Highlights report or the CFPB's enforcement docket.

The Supervisory Highlights states that "auto lenders and servicers" should review the CFPB's findings and implement changes to avoid the violations the report describes. However, as discussed earlier, the CFPB does not provide sufficient facts or analysis in the case of "powerbooking" to identify actual – and compensable -- consumer harm such that finance sources and servicers can take meaningful action. In fact, it appears there is a fundamental misunderstanding of how powerbooking works and why dealers engage in it (i.e., to sell riskier retail installment sale contracts and/or benefit consumers by increasing the odds of credit approval and offering them better financing rates than honest competitors can). Further, there also appears to be a misunderstanding regarding which party in the indirect financing model (the finance source) is harmed by the practice.

AFSA respectfully requests that, absent further factual information identifying the nature of any actual consumer harm arising from a fraud perpetrated by dealers on finance sources, the CFPB withdraw those portions of the Supervisory Highlight Report asserting such harm. Our member companies are happy to meet with the CFPB to further discuss powerbooking.

Sincerely,

Celia Winslow
Senior Vice President
American Financial Services Association

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