

HOT TOPIC:

FIRST CFPB ENFORCEMENT ACTION AGAINST AN ADD-ON PRODUCT SERVICE PROVIDER

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The Consumer Financial Protection Bureau (CFPB) recently filed its first enforcement action against an add-on product service provider for deceptive marketing. The bank issuing the underlying loan was also fined under a separate enforcement action for nearly identical alleged violations. The case provides insight into practices that add-on product service providers should avoid, and some mitigating practices they should follow.

Background

A bank issued vehicle retail installment loans to servicemembers through a program developed and run by a nonbank partner. Optional add-on products were offered in connection with the loan, including guaranteed asset protection (GAP) insurance and vehicle service contracts (VSC), and many servicemembers financed the cost of these products with the retail installment loan. The loans were required to be repaid through a military allotment (a form of direct payment from a servicemembers pay), and a monthly fee was charged to a third party for processing the payment. The nonbank service provider received a portion of the monthly processing fee.

Alleged Violations

Deceptive Marketing

The add-on products were marketed through outbound telemarketing, a website, brochures, and individual car dealers. Specific statements regarding the add-on products' costs and benefits were allegedly deceptive:

- **Deceptive Cost Descriptions.** The VSC brochure stated the product would add "just a few dollars to your monthly payment" when the average monthly cost of a financed VSC was actually \$40. Telemarketers also made off-script statements that the GAP product would add "just a few cents to your car payment" or cost "only a few pennies a day," when the average monthly cost of a financed GAP product was actually \$12.55 (over 40 cents per day).
- **Inadequate Disclosure of Exclusions.**
 - The VSC brochure prominently identified covered parts but did not list excluded parts and only included a six-point font directive to review the VSC agreement for a full description of exclusions.
 - The VSC brochure and agreement contained

subheadings identifying covered parts, but failed to identify excluded parts within those subheadings. For example, “Brakes” were described as being covered in the brochure, but the agreement excluded brake pads and rotors.

- In some cases, the items described as covered in the brochure were not covered under the agreement. For example, the brochure stated transmissions and suspensions were covered, but did not actually cover manual clutches or shock absorbers.
- The telemarketing script stated that the VSC “cover[ed] mechanical breakdowns” without prominently disclosing that major parts were excluded.

Both the bank and the add-on product service provider were cited for these violations.

Inaccurate Finance Charge, APR, & Payment Schedule Disclosures

The consent order with the bank (but not the add-on product service provider) contained allegations that the finance charge, annual percentage rate (APR), payment schedule, and total payment amounts on the loan were not properly calculated and disclosed. Failing to include the “effectively required” allotment processing fee and collecting payments twice per month but only crediting the loan account once per month both contributed to the inaccurate disclosures.

Service Provider Liability

The add-on product provider was deemed a “service provider” subject to the CFPB’s enforcement authority because it participated in “designing, operating, or maintaining” the vehicle retail installment sales loans, which are consumer financial products or services, and because it was responsible for marketing the loans and add-on products.

New Disclosure Requirements

The enforcement action requires the add-on product service provider to “*clearly and prominently*” disclose the following when selling add-on products:

1. The total cash price;
2. That the product is optional;
3. That the product does not have to be financed and that a difference in cost exists when the product is paid for in cash versus financing;
4. That the product can be cancelled; and
5. The existence and nature of exclusions.

The bank is also required to ensure that misrepresentations regarding the material terms of the add-on products do not occur when they are sold by others, such as automobile dealers. Material terms include the monthly and total price, scope of coverage, and exclusions.

The standard for providing disclosures clearly and prominently varies based on the channel in which the disclosures are given.

- ***Textual disclosures*** should be of a type, size, and location to be noticeable, read, and comprehended, and appear in a print that contrasts with the background;
- ***Oral disclosures*** should be in a volume and cadence to be heard and comprehended;
- ***Video disclosures*** should follow the requirements for textual and oral disclosures, as they apply, and should appear on the screen for a sufficient duration to permit reading and comprehension;
- ***Online disclosures*** should follow the requirements for textual, oral, and video disclosures, as they apply, and the user must be required to view the disclosure; and

- *In all cases* the disclosures should be given before the consumer is required to pay, be in easily understandable language, and not be inconsistent with any other communication.

Lenders and other service providers selling add-on products should ensure their practices meet the specific disclosures outlined above.

Oversight of Others Selling Add-on Products

Both the add-on product service provider and bank are required to adopt procedures that ensure automobile dealers selling the vehicle retail installment loans and add-on products do not misrepresent the add-on products' costs, coverages, exclusions, or other material terms. However, these restrictions only apply when the bank or service provider is "offering or providing an add-on product in connection with" a vehicle retail installment loan, which is narrowly defined to include only scenarios

where an optional product is selected, recommended, or required to be marketed by the bank *and is financed with the loan*.

Review and Retain Marketing Materials

While the bank had a right to review add-on product marketing materials created by the service provider, it should have (but did not) regularly "validate statements made in the [marketing] materials." Moreover, copies of all scripts, training materials, advertisements, websites, and other marketing materials related to the vehicle retail installment loans and add-on products must be retained for at least five years.

Restitution of \$6.5 Million

The add-on product provider was ordered to pay \$3.3 million in restitution and the bank was ordered to pay \$3.2 million in restitution.

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