

Adverse Action Notices

November 14, 2007

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NADA MANAGEMENT GUIDE

Route to:

☐ _____

☐ _____

File under Legal, L.49

The image shows a credit application form titled "CREDIT APPLICATION" with a large, bold, black "DENIED" stamp across the center. A metal stamping machine is positioned over the form. The form contains various fields and checkboxes, including "IMPORTANT: Read these Directions before completing this Application", "If you are applying for individual credit in your own name, based on your own income or assets, complete Sections A, C, D, and E, omitting Section B", "If you are applying for individual credit, but are relying on income from alimony, child support, or separate maintenance or on income or assets of another person as the basis for repayment of the credit requested, complete all Sections to the extent possible, providing information in B about the person on whose alimony, support, or maintenance payments or income or assets you are relying", "Payment Date Desired", "Proceeds of Credit To be Used For", and "Birthdate".

A Dealer Guide to ...

ADVERSE ACTION NOTICES

- Who Needs to Send an Adverse Action Notice?
- When Does a Participating Creditor Need to Send an Adverse Action Notice?
- What Is the Time Period for Sending an Adverse Action Notice?
- What Should the Notice Include and How Should It be Sent?
- What Rules Apply to Incomplete Credit Applications?

- What Records Should You Keep?
- What Procedures Should You Have in Place to Comply?
- Unique Considerations for Business Credit

Appendices

- ✓ Adverse Action Flow Chart
- ✓ Sample Simplified Adverse Action Notice
- ✓ Other Sample Adverse Action Notices

The logo for the NADA Management Series features a circular seal with "NADA" in the center, surrounded by "OFFICIAL" and "ACCREDITED". To the right of the seal is a large, stylized "M" with the words "MANAGEMENT SERIES" below it.

We'll cover...

- How we got here
- Adverse Action notices – who, what, when, how
- Will the bank's notice suffice?
- What about incomplete credit applications?
- What about withdrawn credit applications?
- Record retention
- Requirements for business credit applicants
- Creating a F&I process for compliance

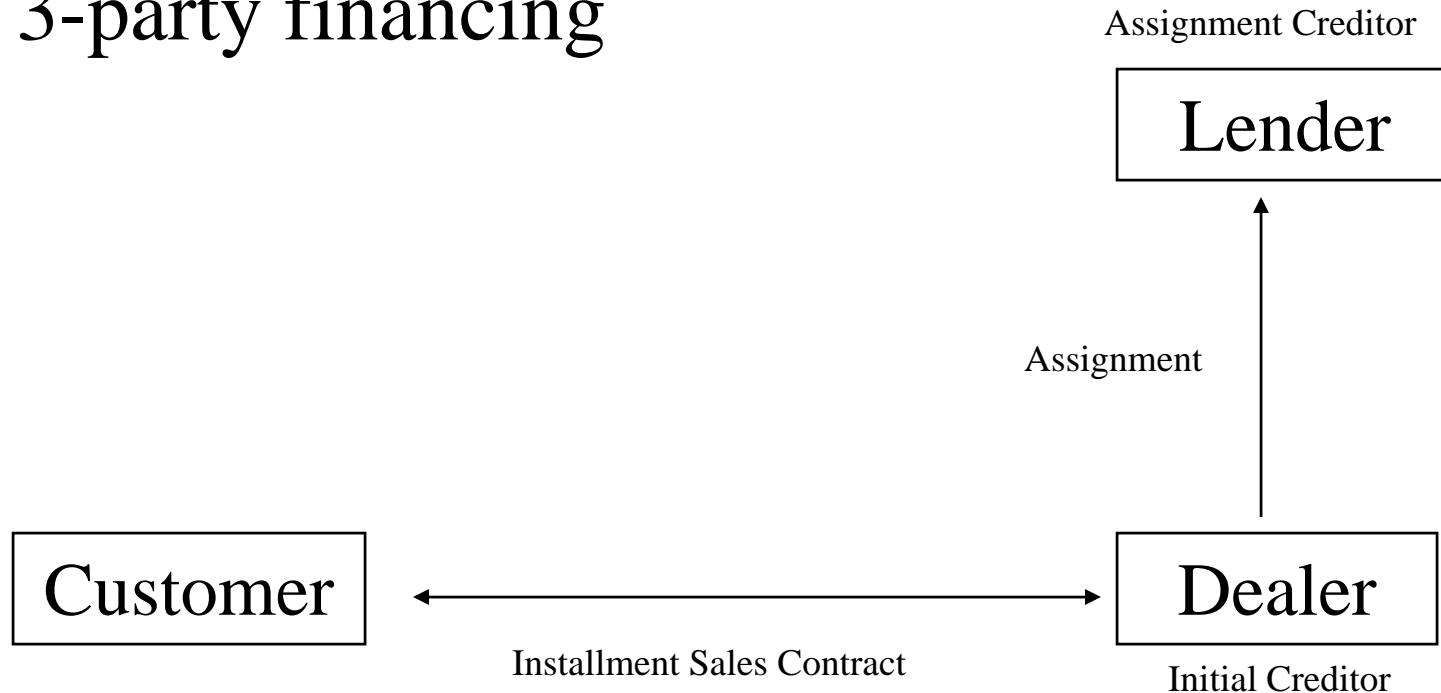
We're here because...

- Federal Statutes and Regulations
 - Two applicable statutes require notices of Adverse Action
 - Equal Credit Opportunity Act (ECOA)
 - Fair Credit Reporting Act (FCRA)
 - For purposes of our discussion – except as noted later - we will treat the notice provisions as congruent
 - ECOA notices are the primary mover
 - FCRA notices piggyback
 - Regulation B – Equal Credit Opportunity and staff interpretations
- In a nutshell

Dealer creditors who participate in making credit decisions and who are unable to place financing must provide notices of Adverse Action

We're here because...

3-party financing



We're here because...

Confusing patchwork of federal case law addressing requirement of dealership to issue Adverse Action notice

- . Outside the Eighth Circuit
 - . Treadway V. Gateway Chevrolet (Illinois 2004) Didn't forward credit app anywhere
 - . Castro v. Union Nissan, Inc. (Illinois 2002) Mixed messages – Dealer repossessed because lender didn't buy paper – adverse. Not adverse if repossessed because missed payment.
 - . Padin v. Oyster Point Dodge (Virginia 2005) Marked up interest rate
 - . Rayburn v. Car Credit Center (Illinois 2000) Required additional cash deposit.
 - . Rodriguez v. Lynch Ford (Illinois 2004) Dealer required cosigner
 - . NADA materials – Merely taking a credit app, forwarding it, and then signing installment sales contracts may be enough.
- . Within the Eighth Circuit, the outcome of the cases has been generally favorable, but the law still cloudy
 - . Bayard v. Behlmann Automotive (Missouri 2003) Applied for 0%. GMAC failed to send notice. Therefore dealer should have. Dicta that one would have been enough.
 - . Madrical v. Kline Oldsmobile (Minnesota 2004) No Adverse Action required because offered favorable financing. Left open the question of whether dealer was a participating creditor.

We're here because...

- The role of F&I professionals has expanded
 - Far more likely to obtain consumer credit reports and shop financing
 - Far more likely – especially in subprime – to evaluate credit applications and make credit decisions
- Visibility of dealership F&I practices may have put us on the radar screen

We're here because...

NADA – to their credit – set the standard by
issuing the Adverse Action Management Guide

We're here because...

- Civil liability – Equal Credit Opportunity Act
 - Actual damages
 - Punitive damages
 - Individual action – up to \$10,000
 - Class action – up to lessor of \$500,000 or 1% net worth
 - Cost and attorney's fees
- Civil liability – Fair Credit Reporting Act
 - Actual damages
 - Punitive and statutory damages for “willful noncompliance”
 - Costs and attorney's fees
 - Note: 2003 federal FACTA law arguably removed civil liability for Adverse Action notice violations under the Fair Credit Reporting Act.

Who must give notice?

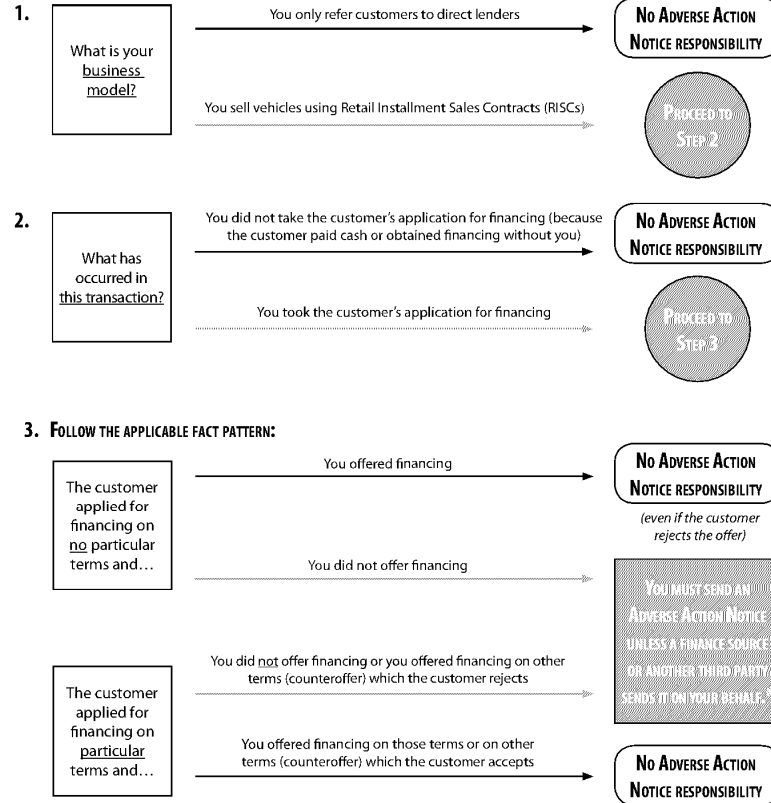
- “Participating creditors” must give notices
 - Regulation B: “a person who, in the ordinary course of business, regularly participates in a credit decision, including setting the terms of the credit...”
- “Referral creditors” need not give notices
 - Regulation B: “a person who, in the ordinary course of business, regularly refers applicants or prospective applicants to creditors, or selects or offers to select creditors to whom a request for credit may be made.”
 - Federal Reserve Board Official Staff Interpretation to Regulation B: “...includes persons such as real estate brokers, automobile dealers, home builders, and home-improvement contractors who do not participate in credit decisions but who only accept applications and refer applicants to creditors, or select or offer to select creditors to whom credit requests can be made.”
- Neither may discriminate or discourage applications on a prohibited basis

What is Adverse Action?

- Credit application and turndown
- Rejected counteroffer (more later)
- When does an inquiry turn into a credit application? When you ask for information to evaluate the credit worthiness of the customer. Examples of inquiries that are not applications (from official staff interpretations)
 - A consumer calls to ask about loan terms and an employee explains the creditor's basic loan terms, such as interest rates, loan-to-value ratio, and debt-to-income ratio
 - A consumer calls to ask about interest rates for car loans, and, in order to quote the appropriate rate, the loan officer asks for the make and sales price of the car and the amount of the downpayment, then gives the consumer the rate
 - A consumer asks about terms for a loan to purchase a home and tells the loan officer her income and intended downpayment, but the loan officer only explains the creditor's loan-to-value ratio policy and other basic lending policies, without telling the consumer whether she qualifies for the loan
 - A consumer calls to ask about terms for a loan to purchase vacant land and states his income and the sales price of the property to be financed, and asks whether he qualifies for a loan; the employee responds by describing the general lending policies, explaining that he would need to look at all of the consumer's qualifications before making a decision, and offering to send an application form to the consumer

NADA Flow Chart:

APPENDIX A—FLOW CHART —DO YOU NEED TO ISSUE AN ADVERSE ACTION NOTICE?



*An Adverse Action Notice sent on your behalf must include, among other things, your name and address and either your specific reasons for the action taken or a disclosure of the customer's right to a statement of your specific reasons if requested within 60 days. (See Section V.)

The foregoing chart is offered for informational purposes only and is not intended as legal advice. The full range of adverse action notice considerations is too extensive to fully summarize on one page. Contact your attorney concerning your adverse action notice compliance responsibilities.

Will the bank's notice suffice?

- Regulation B Staff Commentary: “If one notification is provided on behalf of multiple creditors, the notice must contain the name and address of each creditor. The notice must either disclose the applicant's right to specific reasons ... or give the primary reasons each creditor relied upon in taking the adverse action – clearly indicating which reasons relate to which creditor.” (emphasis supplied)
- Even if your lenders are willing to put the dealership's name and address on their form, your reason's for turndown are different than theirs
- Also, if you send to multiple lenders, each individual lender won't know that financing wasn't placed

Notice description

What the notice must say

Four elements required by ECOA

1. Statement that Adverse Action taken
2. Dealership name and address
3. Boilerplate EEOC notice
4. Specific reasons for denial **or** statement that can request within 60 days

Five extra elements if action influenced by credit report

1. Statement that credit report influenced decision
2. Contact information for credit reporting agency
3. Statement that credit reporting agency didn't make credit decision
4. Statement of right to obtain free copy of credit report
5. Statement of right to dispute accuracy of report

Two extra elements if action influenced by information from 3rd party

1. Statement that information from 3rd party influenced decision
2. Statement that consumer can obtain nature of information

These notices may be combined!

NADA model combined notice form:

Dealership Letterhead

(Insert dealership name, address, and phone number)

[Applicant's Name]

[Date]

[Applicant's Street Address]

[Applicant's City, State and Zip Code]

Dear _____:

Thank you for submitting your recent application to us for vehicle financing. After carefully reviewing your application, we are sorry to advise you that we cannot extend vehicle financing to you at this time.

If you would like a statement of specific reasons why your application was denied, please contact our Finance Director at the address and/or telephone number listed above within 60 days of the date of this letter, and we will provide you with a statement of reasons within 30 days after receiving your request. If we provide reasons to you orally, you have the right to request that we confirm them in writing within 30 days of our receipt of your written request for confirmation.

DEALER OBTAINED A CREDIT REPORT: ☐ YES ☐ NO

If we checked YES, that means we obtained information from a consumer reporting agency as part of our consideration of your application. The box checked below shows the name, address, and (toll-free) telephone number for the consumer reporting agency that provided a report to us. The reporting agency played no part in our decision and is unable to supply specific reasons why we have denied credit to you. You have a right under the Fair Credit Reporting Act to know the information contained in your credit file at the consumer reporting agency. You also have a right to a free copy of your report from the reporting agency, if you request it no later than 60 days after you receive this notice. In addition, if you find that any information contained in the report you received is inaccurate or incomplete, you have the right to dispute the matter with the reporting agency. You can find out about the information contained in your file (if one was used) by contacting:

☐ Experian

P.O. Box 2104

Allen, TX 75013

(888) 397-3742

www.experian.com

☐ TransUnion

P.O. Box 2000

Chester, PA 19022

(800) 888-4213

www.transunion.com

☐ Equifax

P.O. Box 740241

Atlanta, GA 30374

(800) 685-1111

www.equifax.com

DEALER OBTAINED INFORMATION FROM THIRD PARTY ABOUT CREDITWORTHINESS: ☐ YES ☐ NO

If we checked YES, that means we obtained information from a third party other than a credit reporting agency, such as your employer, landlord, or other credit reference you provided. Our credit decision was based in whole or in part on information obtained from the third party. Under the Fair Credit Reporting Act, you have the right to make a written request, no later than 60 days after you receive this notice, for disclosure of the nature of this information.

DEALER SUBMITTED YOUR APPLICATION TO FINANCE SOURCE(S): ☐ YES ☐ NO

If we checked YES, that means we submitted your application to a bank or other creditor(s). You should understand that as a dealer, we generally sell cars on credit only if a third party like a bank or finance company will agree to buy the contract from us on terms that are financially acceptable to us. Regrettably, we could not do that in this instance.

If we checked NO, that means we made the decision on your application without submitting it to another creditor.

If you have any questions regarding this notice, please contact our Finance Director at the number listed above.

Sincerely,

DEALER

Notice: The federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The federal agency that administers compliance with this law concerning this creditor is the Federal Trade Commission at Federal Trade Commission, Equal Credit Opportunity, Washington, DC 20580.

Published by the National Automobile Dealers Association

8400 Westpark Drive, McLean, VA 22102

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How is the notice delivered?

Notice must be in writing and may be delivered

- . In person
- . Regular mail
- . Fax
- . Electronically – must comply with federal E-Sign Act which in general provides for electronic delivery if
 - . Consumer has affirmatively consented and not withdrawn consent
 - . Consumer, prior to consenting, is provided with a clear and conspicuous statement informing the consumer
 - . Right or option of the consumer to have the record provided or made available on paper or in nonelectronic form
 - . Right of the consumer to withdraw the consent
 - . Right to have the record provided or made available in an electronic form and of any conditions or consequences
 - . Describing the procedures the consumer must use to withdraw consent
 - . Must be retrievable

When must notices be sent?

In general, you must act on a credit application within 30 days in one of these ways

- Offer credit that fulfills application
- Send a written Adverse Action notice
- If the customer applied for specific credit terms that you can't offer, make a written "counteroffer"
(Details next slides)
- If you have an incomplete application, send a written notice of incompleteness.
(Details next slides)

Meeting the 30 day rule: counteroffers

If the customer asked for specific terms which can't be met, you may "counteroffer." Include trying to salvage a spot delivery that can't be sold.

- . More money down, cosigner, etc. Distinguish "stipulations"
- . You can call the customer...but
- . To meet the 30 day rule, must act in writing
 - . You can combine a counteroffer and a notice of adverse action in a single writing
 - . The official staff commentary suggests the Appendix C – Sample D notice with the specific reasons
 - . However a written counteroffer along with the NADA combined notice should be sufficient
 - . Advantage of the combination: You don't have to send another adverse action notice if customer doesn't accept counteroffer
 - . You can send a written counteroffer alone without an adverse action notice. If you use this approach and the customer doesn't accept, you must send an adverse action notice within 90 days of the counteroffer

Meeting the 30 day rule: incomplete applications

- If you receive an incomplete application, you can meet the 30 day rule by sending a notice to customer asking for what you need and giving a set time to comply (Appendix C-Sample F)
- The date to supply needed information must be “reasonable”
- Most stipulation requests would probably be considered as attempts to complete a credit application
- If the customer fails to respond to the written request, no further action is required on your part
- Permissible to request orally or in person, however if don’t respond, you must act in writing within 30 days of original application
- If the customer does respond thereby “completing” the application, I see that the 30 days starts over. If it’s all oral, you would want to document the date completed in your file

Withdrawn credit applications

According to Official Staff Interpretation

“When an applicant expressly withdraws a credit application, the creditor is not required to comply with the notification requirements.”

NADA model follow-up

- Dealers who use the NADA model combination Adverse Action notice that gives the customer 60 days to request information will need to be prepared for occasional follow-up requests (scenarios on pages 7 and 8 of NADA material)
 - Application sent to lender
 - Application not sent to lender
- No particular form to for the follow-up disclosure details. Can even be oral unless applicant requests follow-up in writing
- Must be done in 30 days

Recordkeeping

- Equal Credit Opportunity Act – 25 months
 - Credit application
 - Information to evaluate - including any credit report
 - Notices to customer
 - Written statement by customer alleging violation
 - Specific reasons for denial
 - Documentation of oral disclosures
 - May be retained electronically if prompt and accurate retrieval system
 - Commercial – generally 12 months
- Fair Credit Reporting Act
 - No specific requirements – NADA recommends 5 years

Commercial Transactions

- Equal Credit Opportunity Act applies
- Adverse Action notices required by participating creditors
- Can give a notice at time of application that fulfills responsibility
- 12 months recordkeeping

- Follow-up Form
- Questions