



# CAR DEALER

The Auto Dealer's Management Briefing

**INSIDER**

## ATTENTION DEALERS – ADVERSE ACTION LETTERS: NOT JUST FOR LENDERS

By Alex Kurkin

**Here's another case of car dealers being lumped together with financial institution in the regulatory scheme. This time it's about sending so-called "adverse action" letters to consumers who have been turned down for financing.**

When considering F&I issues, dealers may think, "why should I care? I am not the lender."

Simple analysis requires only that you look at your LAW contract. It identifies the dealer as "Creditor-Seller". When the dealer originates the loan transaction, the dealer is the "lender". The fact that the dealer may later assign the contract to a "lender" does not diminish the dealer's original "lender" status.

At the expense of oversimplifying the situation, the adverse action notification obligation applies to all lenders. Under the Fair Credit Reporting Act ("FCRA"), whenever a negative decision is made about a consumer's credit application based on information regarding the consumer's credit worthiness, generally obtained from a credit-reporting agency (or some other third party), the consumer is entitled to a notification pursuant to the FCRA. In the industry, these notifications are commonly referred to as the "turn down letter" that the "banks" send out. Dealers have been aware of the adverse action

notification requirement and have historically decided to not send adverse action notifications, but rather, have opted to burden the banks with that obligation.

More specifically, in those situations where the dealer knows that a consumer will not qualify for the credit sought, rather than turn down the consumer and give the consumer an adverse action letter, dealers send that application to a bank so that the bank will decline the credit and issue the adverse action letter. This procedure has generally been without incident – until now.

Recently, a federal court found that a dealer violated the FCRA when it failed to give a consumer an adverse action letter notwithstanding the fact that the lender, to whom the dealer sent the credit application, sent the consumer an adverse action letter. In this case, the court's rationale was based, in part, on the fact that the dealer was participating in the APR negotiation by proposing terms greater than the buy rate.

So what does all this mean? If the situation involves some promotional APR and there is no rate spread and the bank rejects the consumer, a strong argument could be made that the rationale of this new case does not apply. However, in most situations the dealer is participating in the APR, is the benefactor of some rate spread and would more squarely fit within the analysis of this Federal court decision. As a result, dealers should get into the practice of issuing their own adverse action letters. Does this mean that the consumer will get two adverse action letters, one from the bank and one from the dealer? Yes. Isn't that duplicative and unnecessary? Maybe. Did the federal court care? No.

This then begs the question, "What happens if I don't?" The answer is less certain.

- First, since the ink on this court's decision is still wet, it remains to be seen how the creative plaintiffs' trial bar will use this decision.
- Second, without regard to that creativity, examine the damage provisions in the FCRA. Section 616 governs willful non-compliance. The definition of "willful" is debatable, but generally applies to a fact pattern where someone is aware of an obligation and intentionally ignores it. It is also generally a question of fact (that would be resolved by a jury if it were a jury trial). In the event of a willful non-compliance, the consumer is entitled to recover actual damages of not less than \$100.00 and not greater than \$1,000.00. Again, while unclear, the section appears to create a minimum damage award of \$100.00 per person. While not a lot, we anticipate that this type of claim will likely be asserted as a class action. Naturally, attorneys' fees and punitive damages are also recoverable under this section.

- Section 617 governs negligent non-compliance and appears to cover situations that are deemed to be less than "willful". Unlike Section 616, Section 617 does not have a minimum amount that can be recovered, but rather, permits the recovery of actual damages and attorneys' fees. How a consumer can suffer actual damages by receiving an adverse action letter from the "bank" and the not the dealer is yet unclear, but such technicalities have yet to deter plaintiff's attorneys. Again, this would require proof of damages and lends itself less to class action relief.

While this issue will generate lots of discussion amongst dealers, compliance is simple. The dealer need only fill out and send a form letter. Dealers should immediately consider taking on this responsibility, as it is no longer something that only the banks have to do.