

# Automotive News

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## Keep margins consistent amid regulatory risk

Retailers should keep F&I dealer reserve consistent and document the reason for any downward deviations.

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AUTOMOTIVE NEWS ILLUSTRATION

Retailers should keep F&I dealer reserve consistent and document the reason for any downward deviations.

DENVER — The auto F&I segment might face additional scrutiny over differences in the retail margins dealerships charge white people compared with other racial and ethnic groups, compliance experts continue to warn.

As a result, discretionary dealership additions to both interest rates and the price of finance and insurance products could be in the crosshairs of the Consumer Financial Protection Bureau and Federal Trade Commission.

Compliance advisers encourage retailers to protect themselves by adopting strategies proposed by the National Automobile Dealers Association: Keep F&I retail margins consistent and document the reason for any downward deviations.

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As an FTC commissioner, Rohit Chopra, now head of the CFPB, called dealership reserve over the buy rate “an undisclosed kickback.”

### ‘Auto market abuses’

Two of the nation's most powerful regulators challenged dealer reserve above lender buy rates at the time of the [FTC's 2020 settlement with Bronx Honda](#).

The sentiments from FTC Commissioners [Rohit Chopra](#) — now the head of the CFPB — and [Rebecca Slaughter](#) should be grounds for concern, according to Randy Henrick, Ignite Consulting Partners franchise dealer

group leader, and Terry O'Loughlin, Reynolds & Reynolds Document Solutions compliance director.

"They slammed the car business," Henrick told the Ethical F&I Managers Conference here in September.

Slaughter and Chopra advocated for greater FTC oversight related to auto lending. Chopra characterized dealership reserves over the buy rate as "an undisclosed kickback that dealers earn for convincing prospective car buyers to agree to a higher interest rate than they actually qualify for with a lender."

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#### OPERATE SAFELY

The National Automobile Dealers Association, National Association of Minority Automobile Dealers and American International Automobile Dealers Association have collaborated on model policies retailers could use to protect against allegations of discriminatory F&I dealer reserve. The organizations released the Fair Credit Compliance Policy & Program, which addresses interest rates and dealer reserve, in 2014 and followed up with the Model Dealership Voluntary Protection Products Policy in 2019.

Key elements of both strategies include:

- Set a standard margin or price. It is acceptable to set one standard price for a single voluntary protection product and a separate price for an F&I product bundle.

- Document each time a deviation occurs and the circumstances behind it.

- Do not deviate from the standard pricing except in predefined conditions. These include:

- Dealer reserve: Following a cap established by an individual provider; offering manufacturer subvention or an employee incentive program to qualifying customers; moving a vehicle that meets predetermined inventory reduction criteria

- Voluntary protection products: Following a cap established by law or an individual provider; offering an employee incentive program to qualifying customers

- For both: Accommodating customer's stated monthly payment constraint; meeting a competitor's offer stated by the customer or beating it by a preset amount; honoring a promotion offered to all customers on the same terms

Slaughter called auto financing "profoundly broken" and supported regulation of dealers' discretionary ability to mark up loans. She encouraged customers to seek direct financing or, if using a dealer, declare, "I will agree only to the lowest buy rate that has been offered and not a penny more."

The CFPB doesn't have jurisdiction over auto dealerships. But Chopra said the FTC — which does — should take action on "auto market abuses."

Slaughter agreed the FTC should "commence rulemaking proceedings to tackle both the unfair and deceptive consumer abuses as well as the discrimination too often seen at auto dealerships."

Regulators might not need proof of intentional discrimination to find that it's occurring. Instead, they can use the concept of "disparate impact" to take action: Transactions involving minority borrowers are compared with transactions involving white borrowers to see whether a practice — even a seemingly neutral one — is producing [statistically significant differences](#).

For example, in 2016 the CFPB alleged Toyota Motor Credit Corp. allowed its dealers to charge Black people 0.27 percentage point and Asian/Pacific Islander borrowers 0.18 point more than white people in discretionary retail margin.

The CFPB pointed out such retail margins were not related to the borrower's creditworthiness. The captive finance company settled with the agency without admitting wrongdoing.

Fifth Third Bank National Sales Manager Terry Gilmore recounted to the Ethical F&I Managers Conference audience how the CFPB and Office of the Comptroller of the Currency had frequently examined his bank in the past over disparate impact issues.

He said regulators had expressed plans for greater attention again.

"When they do those kind of audits, they take note of the offending dealers," Henrick told the conference.

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Randy Henrick of Ignite Consulting Partners pointed to NADA's Model Dealership Voluntary Protection Products Policy.

Names of potential dealership targets could be passed to the FTC and state attorneys general, he said.

"That's a big way that regulators get cases," he said. "They get them from consumer complaints, and they get them from other regulators."

And even if the CFPB can't regulate auto dealerships directly, it could pressure them through its regulation of their indirect lender partners.

"It has the same effect," Henrick told *Automotive News* in November. He said he had anecdotally heard of the agency looking at large banks recently.

Mark Edelman, chairman of the McGlinchey Stafford consumer financial services practice, told the 2021 Auto Finance Summit in Las Vegas in October that while the CFPB might

observe dealership disparate impact during bank examinations, the FTC was likely to be more active on pursuing it.

### **'Best defense'**

[NADA in 2014](#) offered dealerships a strategy to avoid disparate impact allegations: Pick a standard retail margin and stick to it. Deviate downward only in certain situations, such as price-matching a competitor's rate, and document the reason for the change. NADA based this Fair Credit Compliance Policy & Program upon terms outlined in 2007 Department of Justice consent orders with dealerships. It also offers a template for documenting deviations.

Edelman: FTC more likely to pursue

"That's gonna be your best defense," Henrick said as he outlined the NADA document.

He advised habitually placing the deviation form in every deal jacket, even in transactions where it wasn't needed, to avoid omitting the documentation in a situation where it was necessary.

He and O'Loughlin advised dealerships to approach discretionary margins on F&I products the same way: standardized pricing with specific and documented deviation criteria. [NADA promoted such a pricing approach in a 2019 model F&I products policy.](#)

KPA F&I East Central District Manager Ryan Daly asked the Ethical F&I Managers Conference audience how many of them had a standard margin on F&I products.

"Not a lot," he observed of the response.

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### **Flats**

Henrick said he had also encountered a sentiment among dealers that they wouldn't object to simply switching to "flats" — fixed payments from lenders in compensation for arranging the loans.

"It surprised me a little bit," Henrick said.

But dealers feel they can still make a profit and see flats as the direction of the industry, he said. Retailers aren't displaying a "universal opposition to flats," he said.

Inline Play

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