

**EMBARGOED UNTIL 5:00 p.m. EDT:**

**Billing Code: 4810-AM-P**

**BUREAU OF CONSUMER FINANCIAL PROTECTION**

**12 CFR Parts 1001 and 1090**

**[Docket No. CFPB-2014-0024]**

**RIN: 3170-AA46**

**Defining Larger Participants of the Automobile Financing Market and Defining Certain Automobile Leasing Activity as a Financial Product or Service**

**AGENCY:** Bureau of Consumer Financial Protection.

**ACTION:** Proposed rule with request for public comment.

**SUMMARY:** The Bureau of Consumer Financial Protection (Bureau or CFPB) proposes to amend the regulation defining larger participants of certain consumer financial product and service markets by adding a new section to define larger participants of a market for automobile financing. The new section would define a market that includes grants of credit for the purchase of an automobile, refinancings of such credit obligations, and purchases or acquisitions of such credit obligations (including refinancings). It would also include automobile leases and purchases or acquisitions of such automobile lease agreements. The Bureau is proposing this rule pursuant to its authority, under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), to supervise certain nonbank covered persons for compliance with Federal consumer financial law and for other purposes. The Bureau has the authority to supervise nonbank covered persons of all sizes in the residential mortgage, private education lending, and payday lending markets. In addition, the Bureau has the authority to supervise nonbank “larger participant[s]” of markets for other consumer financial products or services, as

the Bureau defines by rule. The proposal (Proposed Rule) would identify a market for automobile financing and define as larger participants of this market certain nonbank covered persons that would be subject to the Bureau's supervisory authority. The Proposed Rule would also define certain automobile leases as a "financial product or service" under section 1002(15)(A)(xi)(II) of the Dodd-Frank Act. Finally, the Proposed Rule would make certain technical corrections to existing larger-participant rules.

**DATES:** Comments must be received on or before **[INSERT DATE 60 DAYS AFTER FEDERAL REGISTER PUBLICATION]**.

**ADDRESSES:** You may submit comments, identified by Docket No. CFPB-2014-0024 or RIN 3170-AA46, by any of the following methods:

- *Electronic:* <http://www.regulations.gov>. Follow the instructions for submitting comments.
- *Mail:* Monica Jackson, Office of the Executive Secretary, Consumer Financial Protection Bureau, 1700 G Street, NW, Washington, DC 20552.
- *Hand Delivery/Courier:* Monica Jackson, Office of the Executive Secretary, Consumer Financial Protection Bureau, 1275 First Street, NE, Washington, DC 20002.

**INSTRUCTIONS:** All submissions should include the agency name and docket number or Regulatory Information Number (RIN) for this rulemaking. Because paper mail in the Washington, DC area and at the Bureau is subject to delay, commenters are encouraged to submit comments electronically. In general, all comments received will be posted without change to <http://www.regulations.gov>. In addition, comments will be available for public inspection and copying at 1275 First Street, NE, Washington, DC 20002, on official business

days between the hours of 10 a.m. and 5 p.m. Eastern Time. You can make an appointment to inspect the documents by telephoning (202) 435-7275.

All comments, including attachments and other supporting materials, will become part of the public record and subject to public disclosure. Sensitive personal information, such as account numbers or Social Security numbers, should not be included. Comments will not be edited to remove any identifying or contact information.

**FOR FURTHER INFORMATION CONTACT:** Jolina Cuaresma, Counsel, Andrea Pruitt Edmonds and Amanda Quester, Senior Counsels, Office of Regulations, at (202) 435-7700.

**SUPPLEMENTARY INFORMATION:**

**I. Overview**

Section 1024 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), codified at 12 U.S.C. 5514,<sup>1</sup> gives the Bureau supervisory authority over all nonbank covered persons<sup>2</sup> offering or providing three enumerated types of consumer financial products or services: (1) origination, brokerage, or servicing of consumer loans secured by real estate, and related mortgage loan modification or foreclosure relief services; (2) private education loans; and (3) payday loans.<sup>3</sup> The Bureau also has supervisory authority over “larger

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<sup>1</sup> Public Law 111-203, section 1024, 124 Stat. 1376, 1987 (2010) (codified at 12 U.S.C. 5514).

<sup>2</sup> The provisions of 12 U.S.C. 5514 apply to certain categories of nondepository (nonbank) covered persons, described in subsection (a)(1), and expressly exclude from coverage persons described in 12 U.S.C. 5515(a) or 5516(a). “Covered persons” include: “(A) any person that engages in offering or providing a consumer financial product or service; and (B) any affiliate of a person described [in (A)] if such affiliate acts as a service provider to such person.” 12 U.S.C. 5481(6).

<sup>3</sup> 12 U.S.C. 5514(a)(1)(A), (D), (E). The Bureau also has the authority to supervise any nonbank covered person that it “has reasonable cause to determine, by order, after notice to the covered person and a reasonable opportunity . . . to respond . . . is engaging, or has engaged, in conduct that poses risks to consumers with regard to the offering or provision of consumer financial products or services.” 12 U.S.C. 5514(a)(1)(C); *see also* 12 CFR part 1091 (prescribing procedures for making determinations under 12 U.S.C. 5514(a)(1)(C)). In addition, the Bureau has supervisory authority over very large depository institutions and credit unions and their affiliates. 12 U.S.C.

participant[s] of a market for other consumer financial products or services,” as the Bureau defines by rule.<sup>4</sup>

This Proposed Rule, if adopted, would (1) define certain nonbank covered persons as larger participants of a market for automobile financing that would include grants of credit for the purchase of an automobile, refinancings of such credit obligations and any subsequent refinancings thereof, purchases or acquisitions of such credit obligations (including refinancings), automobile leases, and purchases or acquisitions of automobile lease agreements; (2) define, pursuant to section 1002(15)(A)(xi)(II) of the Dodd-Frank Act, the term “financial product or service” to include certain types of automobile leases that banks are authorized to offer and that the Bureau finds have or likely will have a material impact on consumers; and (3) make certain technical corrections to revise a term used in subpart A of 12 CFR part 1090 and to clarify the affiliate aggregation requirements in two earlier larger-participant rules.

This Proposed Rule would be the fifth in a series of rulemakings to define larger participants of markets for other consumer financial products or services for purposes of section 1024(a)(1)(B) of the Dodd-Frank Act.<sup>5</sup> The Proposed Rule would establish the Bureau’s supervisory authority over certain nonbank covered persons participating in a market for automobile financing. The Proposed Rule would describe this market for consumer financial

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5515(a). Furthermore, the Bureau has certain authorities relating to the supervision of other depository institutions and credit unions. 12 U.S.C. 5516(c)(1), (e). One of the Bureau’s mandates under the Dodd-Frank Act is to ensure that “Federal consumer financial law is enforced consistently without regard to the status of a person as a depository institution, in order to promote fair competition.” 12 U.S.C. 5511(b)(4).

<sup>4</sup> 12 U.S.C. 5514(a)(1)(B), (a)(2); *see also* 12 U.S.C. 5481(5) (defining “consumer financial product or service”).

<sup>5</sup> The first three rules defined larger participants of markets for consumer reporting, 77 FR 42874 (July 20, 2012) (Consumer Reporting Rule), consumer debt collection, 77 FR 65775 (Oct. 31, 2012) (Consumer Debt Collection Rule), and student loan servicing, 78 FR 73383 (Dec. 6, 2013) (Student Loan Servicing Rule). The Bureau also recently released a fourth rule, which defines larger participants of a market for international money transfers and is available at [http://files.consumerfinance.gov/f/201409\\_cfpb\\_final-rule\\_larger-participant-rule-international-money-transfer-market.pdf](http://files.consumerfinance.gov/f/201409_cfpb_final-rule_larger-participant-rule-international-money-transfer-market.pdf) (International Money Transfer Rule).

products or services, which the Proposed Rule labels “automobile financing.” The proposed definition would not encompass all activities that could be considered auto financing. Any reference herein to “the automobile financing market” means only the particular market for automobile financing identified by the Proposed Rule.

The Bureau is authorized to supervise nonbank covered persons subject to section 1024 of the Dodd-Frank Act for purposes of: (1) assessing compliance with Federal consumer financial law; (2) obtaining information about such persons’ activities and compliance systems or procedures; and (3) detecting and assessing risks to consumers and consumer financial markets.<sup>6</sup> The Bureau conducts examinations, of various scopes, of supervised entities. In addition, the Bureau may, as appropriate, request information from supervised entities without conducting examinations.<sup>7</sup>

The Bureau prioritizes supervisory activity among nonbank covered persons on the basis of risk, taking into account, among other factors, the size of each entity, the volume of its transactions involving consumer financial products or services, the size and risk presented by the market in which it is a participant, the extent of relevant State oversight, and any field and market information that the Bureau has on the entity. Such field and market information might include, for example, information from complaints and any other information the Bureau has about risks to consumers posed by a particular entity.

The specifics of how an examination takes place vary by market and entity. However, the examination process generally proceeds as follows. Bureau examiners contact the entity for

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<sup>6</sup> 12 U.S.C. 5514(b)(1).

<sup>7</sup> See 12 U.S.C. 5514(b) (authorizing the Bureau both to conduct examinations and to require reports from entities subject to supervision).

an initial conference with management and often request records and other information. Bureau examiners will ordinarily also review the components of the supervised entity's compliance management system. Based on these discussions and a preliminary review of the information received, examiners determine the scope of an on-site examination and then coordinate with the entity to initiate the on-site portion of the examination. While on-site, examiners spend a period of time discussing with management the entity's policies, processes, and procedures; reviewing documents and records; testing transactions and accounts for compliance; and evaluating the entity's compliance management system. Examinations may involve issuing confidential examination reports, supervisory letters, and compliance ratings. In addition to the process described above, the Bureau may also conduct off-site examinations.

The Bureau has published a general examination manual describing the Bureau's supervisory approach and procedures.<sup>8</sup> As explained in the manual, the Bureau will structure examinations to address various factors related to a supervised entity's compliance with Federal consumer financial law and other relevant considerations.

This Proposed Rule would establish a category of nonbank covered persons that is subject to the Bureau's supervisory authority under section 1024 by defining "larger participants" of a market for automobile financing.<sup>9</sup> The aspect of the Proposed Rule defining larger participants of a market for automobile financing pertains only to that purpose and would not impose new substantive consumer protection requirements. Nonbank covered persons

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<sup>8</sup> CFPB, CFPB Supervision and Examination Manual (Oct. 1, 2012), *available at* <http://www.consumerfinance.gov/guidance/supervision/manual/>.

<sup>9</sup> The Bureau's supervisory authority also extends to service providers of those covered persons that are subject to supervision under 12 U.S.C. 5514(a)(1). 12 U.S.C. 5514(e); *see also* 12 U.S.C. 5481(26) (defining "service provider").

generally are subject to the Bureau’s regulatory and enforcement authority, and any applicable Federal consumer financial law, regardless of whether they are subject to the Bureau’s supervisory authority.

The Bureau proposes to add § 1001.1 and § 1001.2(a) in part 1001 to title 12 of the Code of Federal Regulations. Proposed § 1001.1 would state the authority and purpose of part 1001, which is to implement the Bureau’s authority, granted by section 1002(15)(A)(xi) of the Dodd-Frank Act, to define the term “financial product or service” to include financial products or services in addition to those defined in sections 1002(15)(A)(i)-(x). Proposed § 1001.2(a) would define the term “financial product or service” under that same authority to include certain automobile leases.

## **II. Summary of Proposed Rule**

The Bureau is authorized to define larger participants in markets for consumer financial products or services. Subpart A of the Bureau’s existing larger-participant rule, 12 CFR part 1090, prescribes various procedures, definitions, standards, and protocols that apply with respect to all markets in which the Bureau defines larger participants.<sup>10</sup> Those generally applicable provisions would also apply to the automobile financing market described by this Proposed Rule. The definitions in § 1090.101 should be used, unless otherwise specified, when interpreting terms in this Proposed Rule.

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<sup>10</sup> 12 CFR 1090.100-.103.

The Bureau includes relevant market descriptions and larger-participant tests, as it develops them, in subpart B.<sup>11</sup> Accordingly, the Proposed Rule defining larger participants of the automobile financing market would become § 1090.108 in subpart B.

The Proposed Rule would define a market for automobile financing that would cover specific activities and would set forth a test to determine whether a nonbank covered person is a larger participant of that market. Nonbanks that are the subject of this Proposed Rule provide automobile financing by engaging in one or more of the following activities: granting credit for the purpose of purchasing an automobile; refinancing existing credit obligations or previously refinanced credit obligations that had been made for the purchase of an automobile; purchasing or acquiring such credit obligations (including refinancings); providing automobile leases; and purchasing or acquiring automobile lease agreements.

The Bureau is not proposing to include automobile title lending or the securitization of automobile loans and leases within the meaning of the term “automobile financing” in this Proposed Rule, although as discussed below the Bureau is seeking comment on this approach. Moreover, the Proposed Rule excludes certain auto dealers.<sup>12</sup> The Proposed Rule also would not apply to depository institutions and credit unions that engage in automobile financing, including those already subject to the Bureau’s supervisory authority.

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<sup>11</sup> 77 FR 42874, 42875 (Consumer Reporting Rule), 12 CFR 1090.104; 77 FR 65775, 65777 (Consumer Debt Collection Rule), 12 CFR 1090.105; 78 FR 73383, 73384 (Student Loan Servicing Rule), 12 CFR 1090.106. As noted above, the Bureau also recently released the International Money Transfer Rule, which is available at [http://files.consumerfinance.gov/f/201409\\_cfpb\\_final-rule\\_larger-participant-rule-international-money-transfer-market.pdf](http://files.consumerfinance.gov/f/201409_cfpb_final-rule_larger-participant-rule-international-money-transfer-market.pdf).

<sup>12</sup> Under section 1029 of the Dodd-Frank Act, the Bureau may not exercise its authority over certain auto dealers, as outlined in that section. As explained below, the proposed larger-participant rule would also exclude certain dealers that extend retail credit or leases without routinely assigning them to unaffiliated third parties, even though such dealers are not subject to the statutory exclusion.



The Proposed Rule would define “automobile” to mean any self-propelled vehicle primarily used for personal, family, or household purposes for on-road transportation.<sup>13</sup> The Proposed Rule would define “annual originations” as grants of credit for the purchase of an automobile, refinancings of such credit obligations and any subsequent refinancings thereof, and purchases or acquisitions of such credit obligations (including refinancings). It would also include “automobile leases” and purchases or acquisitions of automobile lease agreements. Under the Proposed Rule, the term “automobile lease” would mean leases that fall within the meaning of section 1002(15)(A)(ii) of the Dodd-Frank Act or meet the requirements of new proposed § 1001.2(a), which is discussed below.

The Proposed Rule would set forth a test to determine whether a nonbank covered person is a larger participant of the automobile financing market. A nonbank covered person would be a larger participant if it has at least 10,000 aggregate annual originations. As prescribed by existing § 1090.102, any nonbank covered person that qualifies as a larger participant would remain a larger participant until two years after the first day of the tax year in which the person last met the applicable test.<sup>14</sup>

Pursuant to existing § 1090.103, a person would be able to dispute whether it qualifies as a larger participant in the automobile financing market. The Bureau would notify an entity when the Bureau intended to undertake supervisory activity; the entity would then have an opportunity to submit documentary evidence and written arguments in support of its claim that it was not a

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<sup>13</sup> Any reference to the term “automobile” means only the particular vehicles identified by the Proposed Rule. The term “auto” as used in this Proposed Rule is intended to include a broader category of vehicles. Similarly, the term “auto financing” is used generically and more broadly than the proposed defined term “automobile financing.”

<sup>14</sup> 12 CFR 1090.102.

larger participant.<sup>15</sup> Section 1090.103(d) provides that the Bureau may require submission of certain records, documents, and other information for purposes of assessing whether a person is a larger participant of a covered market;<sup>16</sup> this authority would be available to the Bureau to facilitate its identification of larger participants of the automobile financing market, just as in other markets.

As noted above, the Bureau is proposing to include automobile leases in the criterion it would use to define larger participants in the market for automobile financing. Certain consumer leases are identified as a financial product or service under section 1002(15)(A)(ii) and, thus, the Bureau would have authority over such leases and those leases would count toward the threshold for the larger-participant test in this Proposed Rule. While most consumer leases fall within section 1002(15)(A)(ii), some likely will not because section 1002(15)(A)(ii) requires that leases be, among other things, the functional equivalent of purchase finance arrangements.<sup>17</sup> As discussed further below, the Bureau believes that the purpose of the Proposed Rule and the Bureau's overall mission would be best served by covering automobile leasing more broadly. Accordingly, the Bureau also proposes in § 1001.2(a) to define the term "financial product or service" under its authority granted by section 1002(15)(A)(xi)(II) of the Dodd-Frank Act to include automobile leases that do not fall under the definition in section 1002(15)(A)(ii).

Finally, the Proposed Rule would amend the Bureau's existing larger-participant rule. Specifically, the Bureau is proposing to make a technical correction to existing § 1090.101, by

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<sup>15</sup> 12 CFR 1090.103(a).

<sup>16</sup> 12 CFR 1090.103(d).

<sup>17</sup> As discussed in greater detail below, section 1002(15)(A)(ii) also requires that leases be non-operating and have an initial term of at least 90 days. The Bureau believes that automobile leases in the current consumer leasing market meet these two criteria.

inserting the word “financial” before the term “product or service” in the definition of “nonbank covered person.” The Proposed Rule would also amend paragraph (iii)(D) of the definition of “annual receipts” in existing § 1090.104(a) and § 1090.105(a), which governs how the affiliate aggregation rules apply to formerly affiliated companies for purposes of the consumer reporting and consumer debt collection larger-participant rules. The proposal would clarify that if a company ceases to be an affiliated company of a nonbank covered person during the relevant measurement period, its annual receipts must be aggregated for the entire period of measurement.

### **III. Legal Authority and Procedural Matters**

#### *A. Rulemaking Authority*

The Bureau is issuing this Proposed Rule pursuant to its authority under the Dodd-Frank Act: (1) sections 1024(a)(1)(B) and (a)(2), which authorize the Bureau to supervise nonbanks that are larger participants of markets for consumer financial products or services, as defined by rule;<sup>18</sup> (2) section 1024(b)(7), which, among other things, authorizes the Bureau to prescribe rules to facilitate the supervision of covered persons under section 1024;<sup>19</sup> (3) section 1022(b)(1), which grants the Bureau the authority to prescribe rules as may be necessary or appropriate to enable the Bureau to administer and carry out the purposes and objectives of Federal consumer financial law, and to prevent evasions of such law;<sup>20</sup> and (4) section 1002(15)(A)(xi), which authorizes the Bureau to prescribe rules to define “other financial product[s] or service[s],” if the Bureau finds that such financial products or services are: (i)

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<sup>18</sup> 12 U.S.C. 5514(a)(1)(B), (a)(2).

<sup>19</sup> 12 U.S.C. 5514(b)(7).

<sup>20</sup> 12 U.S.C. 5512(b)(1).

entered into or conducted as a subterfuge or with a purpose to evade any Federal consumer financial law; or (ii) permissible for a bank or a financial holding company to offer or provide under any applicable Federal law or regulation, and have, or likely will have, a material impact on consumers.<sup>21</sup>

#### *B. Proposed Effective Date of Final Rule*

The Administrative Procedure Act generally requires that rules be published not less than 30 days before their effective dates.<sup>22</sup> The Bureau is proposing that the final rule arising from this Proposed Rule would be effective 60 days after publication.

### **IV. Section-By-Section Analysis**

#### *A. 12 CFR Part 1001—Financial Product or Service*

##### *Section 1001.1 Authority and Purpose*

Proposed § 1001.1 states the authority and purpose for new part 1001. It explains that under section 1002(15)(A)(xi) of the Dodd-Frank Act, the Bureau is authorized to define certain financial products or services for purposes of title X of the Dodd-Frank Act, in addition to those defined in sections 1002(15)(A)(i)-(x). As proposed § 1001.1 explains, the purpose of part 1001 is to implement that authority.

##### *Section 1001.2 Definitions*

###### *2(a)*

Proposed § 1001.2(a) would define the term “financial product or service” under section 1002(15)(A)(xi)(II) of the Dodd-Frank Act, to include certain automobile leases that (1) meet the

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<sup>21</sup> 12 U.S.C. 5481(15)(A)(xi).

<sup>22</sup> 5 U.S.C. 553(d).

requirements of section 108 of the Competitive Equality Banking Act of 1987 (CEBA),<sup>23</sup> as implemented by 12 CFR part 23, and are thus permissible for banks to offer or provide; and (2) are not currently defined as a financial product or service under section 1002(15)(A)(ii) of the Dodd-Frank Act. Under section 1002(15)(A)(xi)(II), for purposes of title X of the Act, the Bureau may define as a covered financial product or service, by regulation: “such other financial product or service . . . if the Bureau finds that such financial product or service is— . . . (II) permissible for a bank or for a financial holding company to offer or to provide under any provision of a Federal law or regulation applicable to a bank or a financial holding company, and has, or likely will have, a material impact on consumers.” The Bureau is proposing § 1001.2(a) pursuant to this authority.

Depository institutions have long engaged in auto leasing activities, and nonbank entities are a major player in the leasing sector.<sup>24</sup> It is an important and growing part of the auto financing market for consumers. While the auto financing market is largely comprised of purchase loans, in recent years consumers have begun to migrate more towards leasing agreements.<sup>25</sup> As of the first quarter of 2014, leases comprise approximately 30 percent of new vehicle automotive financing transactions, which is up from about 20 percent five years ago.<sup>26</sup> Furthermore, of all new and used auto financing transactions recorded in the first quarter of

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<sup>23</sup> CEBA, Public Law 100-86, 101 Stat. 519 (1987) (codified at 12 U.S.C. 24(Tenth)).

<sup>24</sup> DBRS, *Methodology: Rating U.S. Auto Lease Securitizations* 4 (Jan. 2010), available at <http://www.dbrs.com/research/231458>.

<sup>25</sup> Melinda Zabritski, *Experian Automotive, State of the Automotive Finance Market First Quarter 2014* (June 5, 2014), available at [http://www.experian.com/assets/automotive/brochures/experian-auto-2014-q1-credit-webinar-presentation-6-5-2014.pdf?WT.srch=Auto\\_Q12014FinanceTrends\\_PDF](http://www.experian.com/assets/automotive/brochures/experian-auto-2014-q1-credit-webinar-presentation-6-5-2014.pdf?WT.srch=Auto_Q12014FinanceTrends_PDF).

<sup>26</sup> *See id.* at 21.

2014, approximately 14 percent occurred through leasing arrangements, while the remainder used purchase financing.<sup>27</sup>

The Bureau is proposing to include automobile leasing in the consumer financial product or service market for automobile financing for purposes of a rule defining larger participants in that market. Section 1002(15)(A)(ii) defines the term “financial product or service” to include certain leases that, among other things, are the functional equivalent of purchase finance arrangements.<sup>28</sup> As discussed below, the Bureau believes that most consumer automobile leases meet this requirement; however, some may not. The Dodd-Frank Act accounts for the possibility that the enumerated list of financial products and services in sections 1002(15)(A)(i)-(x) may not completely capture the markets for financial products or services available to consumers. Specifically, section 1002(15)(A)(xi)(II) grants the Bureau the authority to define additional financial products or services by regulation as described above. Pursuant to this authority, the Bureau is proposing § 1001.2(a) to define automobile leases that (1) meet the requirements of section 108 of CEBA, as implemented by 12 CFR part 23, and are thus permissible for banks to offer or provide; and (2) are not currently defined as a financial product or service under section 1002(15)(A)(ii) of the Dodd-Frank Act.

Section 1002(15)(A)(ii) defines the term “financial product or service,” in relevant part, as: “extending or brokering leases of personal . . . property that are the functional equivalent of purchase finance arrangements, if—(I) the lease is on a non-operating basis; [and] (II) the initial

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<sup>27</sup> *See id.* at 20.

<sup>28</sup> Section 1002(15)(A)(ii) also requires that leases be non-operating and have an initial term of at least 90 days. The Bureau believes that automobile leases in the current consumer leasing market meet these two criteria.

term of the lease is at least 90 days.”<sup>29</sup> For ease of reference, the Bureau refers to these types of leasing arrangements herein as “category (ii)” leases. As explained below, in the Bureau’s view, the features of a category (ii) lease are found in most consumer automobile leases.

The Bureau believes the phrase “functional equivalent of purchase finance arrangements”—which is not defined in the Dodd-Frank Act<sup>30</sup>—is reasonably interpreted to encompass most automobile leases. Under section 1021 of the Dodd-Frank Act, the Bureau is charged with “implement[ing], and, where applicable, enforc[ing] Federal consumer financial law consistently for the purpose of ensuring that all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive.”<sup>31</sup> In light of this purpose and mandate, the Bureau believes the term “functional equivalent of purchase finance arrangements” is best interpreted from the perspective of the consumer.

For consumers, leasing a vehicle requires an application process and an ongoing contractual obligation that are both financial in nature and similar to entering into a financial arrangement to purchase a vehicle. Like a consumer seeking to qualify for a loan to purchase a vehicle, a consumer seeking to lease a vehicle must provide basic financial information such as income and credit history.<sup>32</sup> Though a consumer who leases an automobile need not finance the entire cost of the vehicle, the consumer still undertakes a major financial obligation in the form

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<sup>29</sup> Section 1002(5) of the Dodd-Frank Act defines “Consumer financial product or service” as “any financial product or service that is described in one or more categories under—(A) paragraph (15) and is offered or provided for use by consumers primarily for personal, family, or household purposes; or (B) clause (i), (iii), (ix), or (x) of paragraph (15)(A), and is delivered, offered, or provided in connection with a consumer financial product or service referred to in subparagraph (A).”

<sup>30</sup> The Bureau is not aware of any Federal or State statute or regulation that defines the term.

<sup>31</sup> 12 U.S.C. 5511(a).

<sup>32</sup> See Fed. Trade Comm’n, *Consumer Information: Understanding Vehicle Financing* (Jan. 2014), available at <http://www.consumer.ftc.gov/articles/0056-understanding-vehicle-financing>.

of a commitment to make a stream of payments over a significant period of time.<sup>33</sup> The consumer must consider how much cash to use, if any, for a down payment, the preferred lease term, and the affordability of monthly payments and other costs including maintenance, insurance, and state registration fees.

Auto leasing also shares many other features with auto lending. A consumer must demonstrate an ability to pay the monthly payments in order to qualify for a lease and a consumer's creditworthiness impacts the terms of the lease. An auto finance company may furnish information about a lessee, such as payment history, to credit bureaus in the same manner that the company does for a borrower. Also, similar to a consumer who finances an auto with a loan, a consumer who leases an auto bears the responsibility for the vehicle's upkeep and must maintain, repair, and service the vehicle during the lease term.<sup>34</sup> The consumer must also insure the vehicle and bears the risk should the vehicle become damaged or totaled.<sup>35</sup> Similarly, if a consumer fails to make loan or lease payments, the vehicle must be returned to the auto finance company, and fees or penalties may apply.<sup>36</sup> Most importantly, regardless of whether consumers seek to purchase or lease a vehicle, they must negotiate the price and terms. For all the foregoing reasons, automobile leases carry similar obligations and risks that vehicle loans present to consumers. In addition, in an auto leasing arrangement, the consumer can typically purchase the vehicle at the end of the lease term for a pre-determined amount, which is generally based on the

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<sup>33</sup> Like consumers who borrow money to purchase a vehicle, consumers who lease are contractually obligated to make monthly lease payments during the lease term. *See* Fed. Res. Sys., *Key to Vehicle Leasing Consumer Guide* (Mar. 13, 2013), available at <http://www.federalreserve.gov/pubs/leasing/>.

<sup>34</sup> *See id.*

<sup>35</sup> *See id.*

<sup>36</sup> *See id.* Also, if a consumer terminates a lease early, early termination fees may apply.



residual value of the vehicle.<sup>37</sup> Accordingly, from the perspective of a consumer, leasing presents an alternative method to a loan for acquiring a vehicle through a series of installment payments, and is therefore reasonably understood to be the functional equivalent of purchase finance arrangements.

Moreover, autos are important to the financial well-being of consumers regardless of whether the consumer obtains the use of a vehicle through a lease or a loan. Consumers rely on autos for their transportation needs, including to and from the workplace. From a consumer's standpoint, whether a vehicle is leased or financed through a loan, any consumer financial law violation that impedes access to a vehicle or otherwise creates problems related to the loan or leasing arrangement can have a critical impact on the consumer. Thus, as interpreted by the Bureau, most automobile leases are the functional equivalent of purchase finance arrangements.

The Bureau believes that typical auto leases also meet the remaining two requirements of section 1002(15)(A)(ii) of the Dodd-Frank Act. First, auto leases are generally “non-operating.” Consistent with the definition in Regulation Y, which governs bank holding companies and changes in bank control, the Bureau interprets “non-operating” to mean that the lease provider is not, directly or indirectly, engaged in operating, servicing, maintaining, or repairing the leased property during the lease term.<sup>38</sup> Under most auto leases, the consumer, rather than the lessor, is

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<sup>37</sup> CFPB, *Ask CFPB: What is residual value?* (June 24, 2012), available at <http://www.consumerfinance.gov/askcfpb/737/what-residual-value.html>. The residual value is the projected market value of the vehicle at the end of the lease, which is usually the amount the consumer would have to pay to purchase the vehicle at the end of the lease term. Additionally, the consumer may be responsible for any applicable taxes or fees.

<sup>38</sup> 12 CFR 225.28(b)(3)(i) n.6 (“The requirement that the lease be on a nonoperating basis means that the bank holding company may not, directly or indirectly, engage in operating, servicing, maintaining, or repairing leased property during the lease term. For purposes of the leasing of automobiles, the requirement that the lease be on a nonoperating basis means that the bank holding company may not, directly or indirectly: (1) Provide servicing, repair, or maintenance of the leased vehicle during the lease term; (2) purchase parts and accessories in bulk or for

responsible for ensuring the care and maintenance of the vehicle.<sup>39</sup> Second, most leases have terms well beyond 90 days. Lease terms for autos typically range from 12 to 60 months, with the majority of leases ranging from 24 to 48 months.<sup>40</sup> Thus, the Bureau believes that most automobile leases readily fall under section 1002(15)(A)(ii) as financial products or services.

However, as discussed above, the requirement that category (ii) leases be the functional equivalent of purchase finance arrangements means that coverage of leases under section 1002(15)(A)(ii) will necessarily depend on a number of factors and circumstances that may vary between particular leases and institutions. Given the potential variance in the terms of lease agreements, the Bureau is concerned that not all automobile leases that materially impact consumers will necessarily qualify for coverage under section 1002(15)(A)(ii) and that market participants may have a difficult time discerning which leases meet the definition and which do not. Such a result would make the automobile financing larger-participant rule difficult to administer with respect to leasing and would not provide optimal protection to consumers. To further the mandate of protecting consumers and for ease of administering the automobile financing larger-participant rule, the Bureau is proposing to exercise its authority under section 1002(15)(A)(xi)(II) of the Dodd-Frank Act to define certain automobile leases not covered under section 1002(15)(A)(ii) as financial products or services within the meaning of section 1002(15)(A) of the Dodd-Frank Act.

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an individual vehicle after the lessee has taken delivery of the vehicle; (3) provide the loan of an automobile during servicing of the leased vehicle; (4) purchase insurance for the lessee; or (5) provide for the renewal of the vehicle's license merely as a service to the lessee where the lessee could renew the license without authorization from the lessor.").

<sup>39</sup> See *supra* note 33.

<sup>40</sup> See Zabritski, *supra* note 25, at 25; see also *supra* note 33.

Under section 1002(15)(A)(xi)(II), for purposes of title X of the Dodd-Frank Act, the Bureau may define as a covered financial product or service, by regulation: “such other financial product or service . . . if the Bureau finds that such financial product or service is— . . . (II) permissible for a bank or for a financial holding company to offer or to provide under any provision of a Federal law or regulation applicable to a bank or a financial holding company, and has, or will have, a material impact on consumers.” In this proposal, the Bureau would define the term “financial product or service” under section 1002(15)(A)(xi)(ii) to include certain automobile leases that: (1) meet the requirements of section 108 of CEBA, as implemented by 12 CFR part 23, and therefore are permissible for banks to offer or provide; and (2) are not the functional equivalent of purchase finance arrangements under section 1002(15)(A)(ii) of the Dodd-Frank Act.

Banks and financial holding companies are broadly authorized to engage in automobile leasing. With respect to national banks, CEBA amended the National Bank Act, to add, among other things, 12 U.S.C. 24(Tenth), which authorizes national banks to “invest in tangible personal property, including, without limitation, vehicles, manufactured homes, machinery, equipment, or furniture, for lease financing transactions on a net lease basis.”<sup>41</sup> Neither CEBA nor its implementing regulations require that such leases be the functional equivalent of loans,

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<sup>41</sup> Under the implementing regulations, net lease is defined as “a lease under which the national bank will not, directly or indirectly, provide or be obligated to provide for:

- (1) Servicing, repair, or maintenance of the leased property during the lease term;
- (2) Parts or accessories for the leased property;
- (3) Loan of replacement or substitute property while the leased property is being serviced;
- (4) Payment of insurance for the lessee, except where the lessee has failed in its contractual obligation to purchase or maintain required insurance; or
- (5) Renewal of any license or registration for the property unless renewal by the bank is necessary to protect its interest as owner or financier of the property.”

12 CFR 23.2(f).

credit, or purchase finance arrangements.<sup>42</sup> Similarly, under Regulation Y, bank and financial holding companies may engage in leasing of personal property irrespective of whether the leases are the functional equivalent of loans, credit, or purchase finance arrangements.<sup>43</sup>

Additionally, the Bureau believes that, whether or not a particular automobile lease qualifies as a category (ii) lease, all consumer automobile leasing, including leasing covered by the proposed definition, has a material impact on consumers. As discussed below, access to a vehicle is critical for consumers. Auto leasing is a significant financial obligation, and consumers are increasingly turning to leasing as a means to obtain a vehicle. The impact of automobile leasing on consumers and their financial well-being does not turn on whether a lease is the functional equivalent of a purchase finance arrangement.

Accordingly, as authorized under section 1002(15)(A)(xi)(II) of the Dodd-Frank Act, the Bureau is proposing to define the term “financial product or service” to include extending or brokering leases for automobiles, where the lease: (1) qualifies as a full-payout<sup>44</sup> lease and a net lease, as provided by 12 CFR 23.3(a), and has an initial term of not less than 90 days, as provided by 12 CFR 23.11; and (2) is not a financial product or service under section 1002(15)(A)(ii).<sup>45</sup> The proposed definition meets the requirements of section 1002(15)(A)(xi)(II). As discussed above, banks and financial holding companies are permitted

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<sup>42</sup> See 12 U.S.C. 24(Tenth); 12 CFR 23.2, 23.3.

<sup>43</sup> 12 CFR 225.28(b)(3). Bank holding companies are limited to leases that are non-operating, as described above, and have a term of at least 90 days. *Id.*

<sup>44</sup> Under the implementing regulations, “full-payout lease” is defined as “a lease in which the national bank reasonably expects to realize the return of its full investment in the leased property, plus the estimated cost of financing the property over the term of the lease, from:

- (1) Rentals;
- (2) Estimated tax benefits; and
- (3) The estimated residual value of the property at the expiration of the lease term.”

12 CFR 23.2(e).

<sup>45</sup> For purposes of this definition, “automobile” would be defined as proposed in 12 CFR 1090.108(a).

to engage in automobile leasing described under this definition, and such automobile leasing has a material impact on consumers.

This proposed definition would ensure that such leases are subject to the same range of protections applicable to “financial product[s] or service[s]” under the Dodd-Frank Act. For example, it would ensure that the offering or providing of the defined leases is subject to the prohibition against unfair, deceptive, or abusive acts or practices in section 1031 of the Dodd-Frank Act.<sup>46</sup> Because leases that are not the functional equivalent of purchase finance arrangements can raise the same consumer protection concerns as category (ii) leases, the Bureau believes that it is appropriate to subject these additional leases to the Dodd-Frank Act provisions that apply to “financial product[s] or service[s].” Comprehensive coverage of automobile leasing will also make the Proposed Rule defining larger participants of the automobile financing market more accurately reflect the structure of that market and easier to administer by eliminating uncertainty about which types of leasing activities are counted.

The Bureau invites comments on its analysis regarding the leasing market and this proposed definition, and requests data on automobile leases generally.

*B. 12 CFR Part 1090—Defining Larger Participants of Certain Consumer Financial Product and Service Markets*

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<sup>46</sup> The proposed definition would also expand the scope of certain other Bureau authorities under title X of the Dodd-Frank Act. Perhaps most significantly, the proposed definition would expand the Bureau’s rulemaking authority under section 1032 of the Dodd-Frank Act, which authorizes the Bureau to prescribe rules to ensure that the features of any consumer financial product or service are fully, accurately, and effectively disclosed to consumers in a manner that permits consumers to understand the costs, benefits, and risks associated with the product or service. In addition, the proposed definition would expand the scope of the Bureau’s authority under section 1022(c) of the Dodd-Frank Act to “monitor for risks to consumers in the offering or provision of consumer financial products or services, including developments in markets for such products or services,” and the scope of the Bureau’s authority under section 1033 of the Dodd-Frank Act to prescribe rules for covered persons with respect to consumer rights to access information concerning consumer financial products or services that the consumer received from such person.

### *Section 1090.101 Definitions*

The Bureau proposes to make a technical correction to the definition of “nonbank covered person” in § 1090.101 by substituting the term “consumer financial product or service” for “consumer product or service” where it appears. With this substitution, the definition would read:

*Nonbank covered person* means, except for persons described in 12 U.S.C. 5515(a) and 5516(a):

- (1) Any person that engages in offering or providing a consumer financial product or service;
- and
- (2) Any affiliate of a person that engages in offering or providing a consumer financial product or service if such affiliate acts as a service provider to such person.

### *Section 1090.104 Consumer Reporting Market*

#### *104(a) Market-related definitions*

*104(a), paragraph (iii)(D) of the definition of “Annual receipts”—“Annual receipts of affiliated companies”*

The Bureau proposes to make a technical correction to paragraph (iii)(D) of the definition of “annual receipts” in § 1090.104(a), which governs how the affiliate aggregation rules apply to formerly affiliated companies for purposes of the Consumer Reporting Rule. For the reasons explained below, the correction would clarify that if a company is an affiliated company of the nonbank covered person during the relevant measurement period but ceases to be an affiliated company during the same period, the annual receipts of the nonbank covered person and the formerly affiliated company must be aggregated for the entire period of measurement. As noted

below, the Bureau is proposing to make the same change to paragraph (iii)(D) of the definition of “annual receipts” in § 1090.105(a) in the Consumer Debt Collection Rule.

Under section 1024(a)(3)(B) of the Dodd-Frank Act, the activities of affiliated companies are to be aggregated for purposes of computing activity levels for the larger-participant rules. In the Consumer Reporting and Consumer Debt Collection Rules, the Bureau has implemented the aggregation called for by section 1024(a)(3)(B) by prescribing the addition of all the receipts of a nonbank covered person and its affiliated companies to produce the nonbank covered person’s annual receipts.<sup>47</sup> The Bureau has prescribed similar calculations for account volume in the Student Loan Servicing Rule and for aggregate annual international money transfers in the International Money Transfer Rule.<sup>48</sup>

The affiliate aggregation provisions of each of the larger-participant rules address circumstances where a company becomes affiliated with a nonbank covered person or ceases to be affiliated with the nonbank covered person during the relevant measurement period.<sup>49</sup> For simplicity and completeness of coverage, the Bureau believes it is appropriate in both circumstances to aggregate the activity of the company with that of the nonbank covered person for the entire period of measurement, even though the company was an affiliated company of the nonbank covered person for only part of the measurement period.

This is the approach used in the Student Loan Servicing Rule’s definition of “account volume” and the International Money Transfer Rule’s definition of “aggregate annual

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<sup>47</sup> 12 CFR 1090.104(a), 1090.105(a).

<sup>48</sup> 12 CFR 1090.106(a), 1090.107(a).

<sup>49</sup> This aspect is addressed in paragraphs (iii)(B) and (iii)(D) of the definition of “annual receipts” in § 1090.104(a), paragraphs (iii)(B) and (iii)(D) of the definition of “annual receipts” in § 1090.105(a), paragraphs (iii)(B) and (iii)(C) of the definition of “account volume” in § 1090.106(a), and paragraph (iii)(B) of the definition of “aggregate annual international money transfers” in § 1090.107(a).

international money transfers.”<sup>50</sup> It is also the approach that the Bureau intended to adopt in the Consumer Reporting and Consumer Debt Collection Rules. However, the language addressing aggregation of formerly-affiliated companies in the definition of “annual receipts” in those rules is unclear.<sup>51</sup> To clarify the operation of those paragraphs, the Bureau proposes to replace the final sentence of paragraph (iii)(D) of § 1090.104(a)’s definition of “annual receipts” with: “The annual receipts of a nonbank covered person and its formerly affiliated company are aggregated for the entire period of measurement if the affiliation ceased during the applicable period of measurement as set forth in paragraph (ii) of this definition.”

*Section 1090.105—Consumer Debt Collection Market*

*105(a) Market-related definitions*

*105(a), paragraph (iii)(D) of the definition of “Annual receipts” – “Annual receipts of affiliated companies”*

For the same reasons described above with respect to § 1090.104(a), the Bureau proposes to replace the final sentence of paragraph (iii)(D) of § 1090.105(a)’s definition of “annual receipts” with: “The annual receipts of a nonbank covered person and its formerly affiliated

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<sup>50</sup> Paragraph (iii)(C) of the definition of “account volume” in § 1090.106(a) provides: “If two affiliated companies cease to be affiliated companies, the number of accounts of each continues to be included in the other’s account volume until the succeeding December 31.” Paragraph (iii)(B) of the definition of “aggregate annual international money transfers” in § 1090.107(a) provides:

The annual international money transfers of a nonbank covered person must be aggregated with the annual international money transfers of any person that was an affiliated company of the nonbank covered person at any time during the preceding calendar year. The annual international money transfers of the nonbank covered person and its affiliated companies are aggregated for the entire preceding calendar year, even if the affiliation did not exist for the entire calendar year.

<sup>51</sup> Paragraph (iii) of the definition of “annual receipts” in both § 1090.104(a) and § 1090.105(a) provides:

The annual receipts of a formerly affiliated company are not included if affiliation ceased before the applicable period of measurement as set forth in paragraph (ii) of this definition. This exclusion of annual receipts of formerly affiliated companies applies during the entire period of measurement, rather than only for the period after which affiliation ceased.



company are aggregated for the entire period of measurement if the affiliation ceased during the applicable period of measurement as set forth in paragraph (ii) of this definition.”

*Section 1090.108—Automobile Financing Market*

The Bureau is proposing § 1090.108 to define larger participants of the automobile financing market because of the important role that automobiles and related financing play in consumers’ lives. Autos have become indispensable for most working individuals, with nearly 90 percent of the workforce commuting to work by car, and most driving alone.<sup>52</sup> Consumers’ reliance on vehicles is underscored by recent studies on repayment patterns, which show that consumers pay their auto loans before other secured and unsecured debt.<sup>53</sup> Auto loans are the third largest category of outstanding household debt, behind mortgage and student loans. In the first quarter of 2014, consumers in the United States had 87.4 million outstanding auto loans valued at nearly \$900 billion.<sup>54</sup>

As stated above, the Bureau is proposing to define a market for automobile financing that would include grants of credit for the purchase of an automobile, refinancings of such credit obligations and any subsequent refinancings thereof, and purchases or acquisitions of such credit obligations (including refinancings). It would also include automobile leases and purchases or acquisitions of automobile lease agreements. While a significant number of consumers obtain

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<sup>52</sup> See Brian McKenzie & Melanie Rapino, U.S. Census Bureau, *Commuting in the United States: 2009* (2011), <http://www.census.gov/prod/2011pubs/acs-15.pdf>.

<sup>53</sup> See TransUnion, *New Developments around the Consumer Payment Hierarchy* (2014), [http://media.marketwire.com/attachments/201403/233081\\_PaymentHierarchyInfographic2014FINAL.jpg](http://media.marketwire.com/attachments/201403/233081_PaymentHierarchyInfographic2014FINAL.jpg) (Full report available at <http://www.transunioninsights.com/studies/behaviorstudy>).

<sup>54</sup> Fed. Res. Bank of N.Y., *Quarterly Report on Household Debt and Credit* (May 2014), [http://www.newyorkfed.org/householdcredit/2014-q1/data/pdf/HHDC\\_2014Q1.pdf](http://www.newyorkfed.org/householdcredit/2014-q1/data/pdf/HHDC_2014Q1.pdf). According to the New York Federal Reserve, “auto loans” are “loans taken out to purchase a car, including Auto Bank loans provided by banking institutions (banks, credit unions, savings and loan associations), and Auto Finance loans, provided by automobile dealers and automobile financing companies.”

credit to purchase their automobile,<sup>55</sup> in recent years, consumers have begun to migrate more towards leasing agreements. Leasing is growing quickly as a proportion of new vehicle financing.<sup>56</sup>

Under the proposed automobile financing market, nonbank participants include: (1) specialty finance companies, (2) “captive” nonbanks (commonly referred to as “captives”), and (3) Buy Here Pay Here (BHPH) finance companies.<sup>57</sup> Specialty financing companies serve consumers in specialized markets. Many of these companies focus on providing financing to subprime borrowers who tend to have past credit problems, lower income, or limited credit histories, which prevent them from being able to obtain financing elsewhere.

Generally, captives are subsidiary finance companies owned by auto manufacturers. They provide consumers with financing for the primary purpose of facilitating their parent companies’ and associated franchised dealers’ auto sales.

BHPH finance companies are similar to captives in that they are associated with certain BHPH dealers,<sup>58</sup> which traditionally focus on subprime and deep subprime borrowers. While BHPH dealers are mostly independently-owned entities that serve as the primary lender and receive payments directly from consumers, some larger BHPH dealers will sell or assign their contracts to specific BHPH finance companies once the contract has been consummated with the

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<sup>55</sup> In addition to financing the initial acquisition of an automobile, some consumers refinance their existing automobile loans. Consumers typically refinance their automobile loans to lower their loan interest rates to achieve lower monthly payments. The level of refinancing depends on trends in interest rate levels over the term for most auto loans, which ranges from three to seven years.

<sup>56</sup> As stated above, at the end of the first quarter of 2014, leases comprised approximately 30 percent of new vehicle automotive financing transactions, which is up from about 20 percent five years ago. *See* Zabritski, *supra* note 25.

<sup>57</sup> Although dealers may also engage in some automobile financing activities, they are not included for purposes of this discussion of market participants.

<sup>58</sup> Unlike captives, however, not all BHPH finance companies are associated with specific automobile dealers. The Bureau is aware of BHPH finance companies that provide financing to independently-owned BHPH dealer franchises.

consumer. However, these BHPH finance companies do not focus on a particular auto manufacturer unlike captives whose primary purpose is to extend credit to consumers who want to purchase or lease a specific manufacturer's vehicles.<sup>59</sup>

According to the Bureau's estimates based on Experian Automotive's AutoCount® database,<sup>60</sup> the proposed automobile financing market includes over five hundred nonbank automobile lenders<sup>61</sup> and is fairly concentrated. As measured by the number of transactions identified in the AutoCount Lender Report<sup>SM</sup>, fewer than 40 entities comprise over 90 percent of the auto loan and lease transactions in the nonbank market.<sup>62</sup> The top tier of this market is dominated by large captives. The other large companies in the nonbank automobile financing market are either specialty finance companies or BHPH finance companies. The lower tiers of the nonbank market are comprised generally of smaller regional specialty finance companies.

Auto credit is provided both through direct and indirect channels creating different dynamics for consumers and industry participants. In the direct lending channel, a consumer seeks credit directly from the financing source, whereas in the indirect lending channel, the dealer typically facilitates a loan from a third-party finance source.<sup>63</sup> Depository institutions and

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<sup>59</sup> The BHPH segment of the market primarily serves deep subprime borrowers. BHPH automobile dealers generally are indifferent to the consumers' automobile choice. Typically, only after the dealer assesses consumers' creditworthiness and determines their maximum monthly payment does the dealer present automobile options.

<sup>60</sup> Experian Automotive's AutoCount database is a vehicle database that collects monthly transaction data from State Departments of Motor Vehicles (DMVs). *See also infra* note 79 and accompanying text.

<sup>61</sup> To reach this estimate, the Bureau considered data from Experian Automotive's AutoCount database for calendar year 2013, with several adjustments. First, transactions with no lender listed were excluded from the sample. Second, entities with fewer than 360 loans and leases on an annual basis were excluded from the sample. Third, entities that were identified by Experian Automotive as "Other" in the lender type category were also excluded from the sample. Fourth, the Bureau excluded entities that already fall within the Bureau's supervisory authority or that it identified as BHPH dealers and title lenders. In some cases, entities were also consolidated due to known affiliations.

<sup>62</sup> These estimates were derived using the same methodology described in *supra* note 61.

<sup>63</sup> Such sources include depository institutions, nonbank affiliates of a depository institution, independent nonbanks, and captives.

credit unions have an advantage in the direct lending space because these entities often have a pre-existing relationship with consumers. Captives and other specialty finance companies are more active in the indirect channel. Most consumers who finance the purchase of an automobile—roughly 80 percent—use the indirect channel and look to automobile dealers to facilitate their purchase loans.<sup>64</sup>

With indirect lending, dealers rather than consumers typically select the lender who will provide the financing. Upon completion of the vehicle selection process, the dealer usually collects basic information regarding the applicant and uses an automated system to forward that information to prospective indirect automobile lenders. After evaluating the applicant, indirect auto lenders may provide the dealer with purchase eligibility criteria or stipulations including, but not limited to, a risk-based “buy rate” that establishes a minimum interest rate at which the lender is willing to purchase a retail installment sales contract executed between the consumer and the dealer for the purchase of the vehicle.<sup>65</sup>

A franchised dealer often can choose from a selection of funding sources.<sup>66</sup> However, a franchised dealer that is affiliated with a manufacturer can be incentivized to use a captive through mechanisms such as promotional discounts or limited-time financing offers that can be used to attract consumers. An independent auto dealer, which is not associated with a specific

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<sup>64</sup> See Delvin Davis, Ctr. For Responsible Lending, *The State of Lending in America & Its Impact on U.S. Households* (Dec. 2012), available at <http://www.responsiblelending.org/state-of-lending/reports/4-Auto-Loans.pdf>.

<sup>65</sup> The Bureau is aware that an indirect auto lender may also have a policy that allows the dealer to mark up the interest rate above the indirect auto lender’s buy rate. In the event that the dealer charges the consumer an interest rate that is higher than the lender’s buy rate, the lender may pay the dealer what is typically referred to as “reserve” (or “participation”), compensation based upon the difference in interest revenues between the buy rate and the actual note rate charged to the consumer in the retail installment contract executed with the dealer. Dealer reserve is one method lenders use to compensate dealers for the value they add by originating loans and finding financing sources. The exact computation of compensation based on dealer markup varies across lenders and may vary between programs at the same lender.

<sup>66</sup> See *supra* note 63 and accompanying text.

manufacturer or brand, typically does not have access to captive finance sources but will have access to other indirect sources, including depository institutions engaged in indirect lending as well as specialty finance companies.

With the relevant eligibility criteria and stipulations, the dealer then selects the indirect lender that will finance the loan to the consumer and extends the loan through a retail installment sales contract that the indirect lender purchases or acquires. The dealer is typically compensated for arranging indirect financing. For indirect automobile loans, the indirect automobile lender typically becomes responsible for servicing the loan and consumers will then make loan payments to the lender.

Similarly, leases may be obtained through direct or indirect channels, although most are through indirect channels. To purchase an automobile lease from a dealer, finance sources express their interest by providing the dealer with the relevant terms of a lease similar to those considered for a loan. These terms can include a “money factor,” which establishes how much a consumer will be paying in finance charges, and the length or term of the lease.<sup>67</sup> However in a lease, a finance source will also quote a residual value, which is one of the elements comprising both the consumer’s monthly payments and the consumer’s pre-determined purchase option cost at the end of the lease term. As a practical matter, few auto dealers enter into a financing or leasing arrangement with a consumer unless there is an indirect lender or lessor who will purchase the retail installment sales contract or leasing contract.<sup>68</sup>

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<sup>67</sup> Fed. Reserve Sys., *Glossary, Keys to Vehicle Leasing* (Mar. 13, 2013), available at <http://www.federalreserve.gov/pubs/leasing/glossary.htm>.

<sup>68</sup> This does not apply to those auto dealers, such as BHPH dealers, who serve as the primary lender.

Refinancing of an existing credit obligation can enable a consumer to reduce his or her monthly auto payment. The refinancing market is highly dependent on interest rates and, thus, activity typically increases as rates decrease relative to the initial rate at origination. However, the average auto loan term for a new vehicle is relatively short at around 66 months,<sup>69</sup> and market rates during the loan repayment period typically do not differ much from the rates at origination. These dynamics explain why the Bureau believes that overall refinancing volumes comprise only a small niche of the broader auto financing market. Unfortunately, there is limited data available pertaining to refinancing volume because, among other things, publicly traded market participants generally tend to consolidate refinancing activity within origination activity for financial reporting purposes.

*Section 1090.108(a)—Market-Related Definitions*

Unless otherwise specified, the definitions in § 1090.101 should be used when interpreting terms in this Proposed Rule. The Proposed Rule would define additional terms relevant to the proposed automobile financing market. These terms include “aggregate annual originations,” which the Proposed Rule would use as the criterion for assessing larger-participant status; “automobile”; “automobile financing”; “automobile lease”; and “refinancings.”

The Bureau seeks comment on each of the definitions set forth in the Proposed Rule and any suggested additions, clarifications, modifications, or alternatives.

*Aggregate annual originations.* The Bureau is proposing to use aggregate annual originations as the criterion to assess whether a nonbank covered person is a larger participant of the automobile financing market. Proposed § 1090.108(a) would define the term “aggregate

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<sup>69</sup> Zabritski, *supra* note 25, at 39.

annual originations” as the sum of the number of annual originations of a nonbank covered person and the number of annual originations of each of the nonbank covered person’s affiliated companies, as calculated according to instructions set forth in the proposed regulation and as discussed below.

*Annual originations.* Proposed § 1090.108(a) would define the term “annual originations” to mean the sum of the following transactions for the preceding calendar year: grants of credit for the purchase of an automobile, refinancings of such credit obligations and any subsequent refinancings thereof, and purchases or acquisitions of such credit obligations (including refinancings). It would also include automobile leases and purchases or acquisitions of automobile lease agreements. Only originations involving automobiles primarily used for personal, family or household purposes would be counted as annual originations for purposes of this larger-participant rule.

The Bureau proposes to exclude from annual originations any investments in asset-backed securities. Automobile asset-backed securities are investment vehicles in which the principal and interest payments from automobile loans serve as collateral for bonds sold to investors and do not generally alter the contractual obligation between the consumer and the entity that granted the credit or services the loan. Accordingly, the Bureau does not believe such transactions should be considered as annual originations under the Proposed Rule. The Bureau solicits comment as to whether this proposed exclusion for asset-backed securities is appropriate and whether the Bureau should define the term “asset-backed securities” in proposed § 1090.108(a).

The Bureau is also considering whether to include other types of automobile-secured loans. These could include, for example, automobile title loans, in which a lender extends credit

to a consumer that is secured by the title to an automobile that the consumer owns. The Bureau is proposing to define a market for automobile financing that does not include automobile title loans because the Bureau believes that this financial product or service is substantially different from automobile financing activities. For example, auto title loans are generally provided by companies that do not compete with lenders that finance the acquisition of a vehicle. Loans provided by auto title lenders typically are not used for the activities identified in the criterion to measure market activity, such as the grant of credit to purchase an automobile or to refinance an existing credit obligation. Further, auto title loans are generally significantly shorter in term and smaller in size than loans used to purchase an automobile or to refinance an existing automobile loan. The Bureau thus believes that auto title loans might be better analyzed separately from the automobile financing market as part of a future larger-participant rulemaking.<sup>70</sup> However, the Bureau solicits feedback on whether it should define the market for automobile financing and annual originations to include other types of loans secured by automobiles and, if so, whether it is appropriate to use the same criterion and threshold for such loans as proposed here or whether an alternative criterion and threshold would be preferable. The Bureau also solicits comments on data sources that the Bureau might use in analyzing other automobile-secured loans like automobile title loans that are not used to purchase the vehicle.

*Aggregating the annual originations of affiliated companies.* Under the Dodd-Frank Act, the activities of affiliated companies are to be aggregated for purposes of computing activity levels for rules—like this Proposed Rule—to determine larger participants in particular markets

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<sup>70</sup> As noted above, this larger-participant rule is only one in a series of rulemakings.



for consumer products or services under section 1024(a)(1).<sup>71</sup> Therefore, the Proposed Rule would define the “aggregate annual originations” for each nonbank covered person as the sum of the number of annual originations of the covered entity and the number of annual originations of all its affiliated companies. For purposes of computing the covered person’s aggregate annual originations, the annual originations of each affiliated company would first be calculated separately and then aggregated with the originations of the covered entity.

Paragraph (ii) of the proposed definition of “aggregate annual originations” would set forth the method of aggregating the annual originations of a nonbank covered person and its affiliated companies when affiliation has started or ended within the preceding calendar year. It would provide that the annual originations of a nonbank covered person must be aggregated with the annual originations of any person that was an affiliated company of the nonbank covered person at any time during the preceding calendar year. The annual originations of a nonbank covered person and its affiliated companies would be aggregated for the entire preceding calendar year, even if the affiliation did not exist for the entire calendar year. This provision would not apply, however, if the affiliated company is a dealer that is excluded by proposed § 1090.108(c), which is discussed below.

*Automobile.* Proposed § 1090.108(a) would define “automobile” to mean any self-propelled vehicle primarily used for personal, family, or household purposes for on-road transportation. The proposed definition would apply to both new and used vehicles. The

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<sup>71</sup> 12 U.S.C. 5514(a)(3)(B) (“For purposes of computing activity levels under [12 U.S.C. 5514(a)(1)] or rules issued thereunder, activities of affiliated companies (other than insured depository institutions or insured credit unions) shall be aggregated.”).

proposed definition would not include motor homes, recreational vehicles (RVs), golf carts, and motor scooters.

The proposed definition of “automobile” was informed by the definition of “motor vehicle” in section 1029(f) of the Dodd-Frank Act,<sup>72</sup> but includes modifications to limit its application to vehicles primarily used for personal, family, or household purposes for on-road transportation. The definition of “motor vehicle” found in the Dodd-Frank Act encompasses a wide range of vehicles, and the Bureau believes that using such a broad definition in this larger-participant rulemaking would make the Proposed Rule difficult to administer. Consistent with the definition of “motor vehicles,” the proposed definition of “automobile” would cover vehicles such as cars, sports utility vehicles, light-duty trucks, and motorcycles. However, because the proposed definition is limited to vehicles primarily used for personal, family, or household purposes, heavy-duty trucks, buses, or ambulances are excluded as they are designed for and primarily used for commercial purposes.

Certain types of motor vehicles, such as motor homes, recreational vehicles (RVs), golf carts and motor scooters, are in markets that differ from those of the vehicles captured in the proposed definition of “automobile.” Although the Bureau does not have sufficient data on these other market segments, the Bureau does not believe that financing for the types of motor vehicles that are excluded from its proposed definition of “automobile” is done on the same scale as financing of vehicles used by consumers as transportation to work or to carry out their errands

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<sup>72</sup> Under section 1029(f)(1) of the Dodd-Frank Act, the term “motor vehicle” means: (A) any self-propelled vehicle designed for transporting persons or property on a street, highway, or other road; (B) recreational boats and marine equipment; (C) motorcycles; (D) motor homes, recreational vehicle trailers, and slide-in campers as those terms are defined in section 571.3 and 575.103(d) of title 49, Code of Federal Regulations, or any successor thereto; and (E) other vehicles that are titled and sold through dealers. 12 U.S.C. 5519(f)(1).

and other daily activities. Thus, the Bureau believes that the vehicles excluded from the definition likely warrant different larger-participant criteria and thresholds if they were included in the market defined for this Proposed Rule. However, the Bureau seeks comment and additional market data related to these assumptions. The Bureau also seeks comment on its proposed definition of “automobile,” specifically whether the proposed definition should address other vehicles or types of vehicles, and whether motorcycles should be a separately defined term.<sup>73</sup>

*Automobile financing.* Proposed § 1090.108(a) would define the term “automobile financing” to mean providing the transactions enumerated under the definition of the term “annual originations” as defined in proposed § 1090.108(a). Thus, under the Proposed Rule, “automobile financing” would mean granting credit for the purpose of purchasing an automobile; refinancing existing credit obligations or previously refinanced credit obligations that had been made for the purchase of an automobile; purchasing or acquiring such credit obligations (including refinancings); providing automobile leases; and purchasing or acquiring automobile lease agreements. The Bureau believes this proposed definition reflects the number of consumer loans and leases made or facilitated (through purchases of the loans and leases) regarding one of the most important nonfinancial assets to American households.

*Automobile lease.* Proposed § 1090.108(a) would define the term “automobile lease” to mean a lease for the use of an automobile, as that term is defined in this Proposed Rule, that is a financial product or service under either section 1002(15)(A)(ii) of the Dodd-Frank act or

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<sup>73</sup> The Bureau notes that this larger-participant rule is only one in a series of rulemakings and the Bureau could address the financing of other vehicles or categories of vehicles not covered under this Proposed Rule in a separate rulemaking should it determine it appropriate to do so.

proposed § 1001.2(a). A lease for the use of an automobile is a financial product or service under section 1002(15)(A)(ii) if it: (1) is the functional equivalent of a purchase finance arrangement; (2) is on a non-operating basis; and (3) has an initial term of at least 90 days.<sup>74</sup> As explained above, the Bureau believes that most automobile leases meet these requirements. The Bureau also believes that those automobile leases that are not the functional equivalent of purchase finance arrangements, and therefore do not fall under section 1002(15)(A)(ii), would nevertheless likely be covered by the proposed new category of “financial product or service” under proposed § 1001.2(a). Proposed § 1001.2(a) is guided by the requirements in 12 CFR 23.2(d)(1), which implement the product-related requirements for leases under CEBA. An automobile lease would be a financial product or service under proposed § 1001.2(a) as long as (1) the lease qualifies as a full-payout lease and a net lease, as required under 12 CFR 23.3(a); (2) the lease has an initial term of at least 90 days, as required under 12 CFR 23.11; and (3) the lease does not meet the requirements for a financial product or service under section 1002(15)(A)(ii).

*Refinancing.* The Bureau proposes to define the term “refinancing” for purposes of this rule by reference to § 1026.20(a) of Regulation Z.<sup>75</sup> Section 1026.20(a) defines “refinancing” for closed-end credit transactions, including those related to the purchase of automobiles. If a transaction is determined to be a “refinancing” under § 1026.20(a), a “new transaction” has occurred and the creditor must provide the consumer with disclosures, among other things. Under Regulation Z, a refinancing occurs only when an existing obligation is satisfied and

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<sup>74</sup> 12 U.S.C. 5481(15)(A)(ii).

<sup>75</sup> 12 CFR 1026.20.

replaced by the original creditor or a holder or servicer of the original obligation, and a new obligation is undertaken by the same consumer. It is noted that if a *new* creditor refinances an existing credit obligation, it is considered a new transaction rather than a refinancing for purposes of Regulation Z without reference to whether satisfaction and replacement occurs.<sup>76</sup> Under § 1026.20(a), whether satisfaction and replacement has occurred is determined based on the parties' contract and applicable state law. Section 1026.20(a) also provides certain exceptions to the requirement for satisfaction and replacement.

The definition of “refinancing” in proposed § 1090.108(a) mirrors the Regulation Z definition except that the nonbank covered person is not required to be the original creditor or a holder or servicer of the original obligation to fall under the definition.<sup>77</sup> Thus, as applied to this proposal, a nonbank covered person would be required to include in its aggregate annual originations any grant of credit for the purchase of an automobile that satisfies and replaces an existing credit obligation, even if the nonbank covered person is not the original creditor, holder or servicer of the existing credit obligation. The Bureau believes it is appropriate to include refinancing activity conducted by third parties as part of the automobile financing market.<sup>78</sup> As in Regulation Z, proposed § 1090.108(a) would require that to be a refinancing, both the existing and the new grant of credit must involve the same borrower.

As an alternative, the Bureau is considering whether it would be preferable to propose a new definition of “refinancing” for purposes of the Proposed Rule. Auto finance companies that grant credit secured by a vehicle are already subject to § 1026.20(a). The Bureau believes that

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<sup>76</sup> 12 CFR 1026.20, comment 20(a)-5.

<sup>77</sup> *See id.*

<sup>78</sup> By contrast, under Regulation Z, such transactions are omitted from the definition of “refinancing” but are nevertheless subject to disclosure and other requirements as a new transaction. *Id.*

using the Regulation Z definition would avoid adding regulatory complexity that could arise through the creation of a new definition for purposes of this larger-participant rulemaking, but invites comments on this approach and whether the Regulation Z definition of “refinancing” with the modification described above is appropriate for purposes of the Proposed Rule.

Finally, as discussed above, the Bureau does not have a reliable data source pertaining to refinancings in the automobile market. Although the Bureau is aware that refinancings occur, particularly when interest rates are declining, there is no standard reporting available that describes what percentage of the total market for automobile financing is comprised of refinancings and what part of the automobile refinancing market is provided by entities that would be subject to the Proposed Rule. Thus, to better understand this segment of the market, the Bureau seeks data on refinancing activity in the market and the market participants that engage in refinancing. The Bureau also seeks comment on its proposal to include refinancings in the proposed definition of “annual originations” and in the market definition of “automobile financing.”

*Section 1090.108(b)—Test to Define Larger Participants*

*Criterion.* The Bureau has broad discretion in choosing a criterion for assessing whether a nonbank covered person is a larger participant of a market. For any specific market, there might be several criteria, used alone or in combination, that could be viewed as reasonable alternatives. For the automobile financing market, the Bureau is considering a number of criteria, including aggregate annual originations, dollar volume of originations, and dollar volume of outstanding loans. The Bureau invites comment on these three possible criteria as well as suggestions for other criteria that commenters believe might be superior.

Among these options, the Bureau proposes to use aggregate annual originations as the criterion that establishes which entities are larger participants of the automobile financing market. A discussion of the definition of “aggregate annual originations” is set forth above. The Bureau expects that aggregate annual originations will be an appropriate criterion, because, among other things, it is a meaningful measure of a nonbank covered person’s level of participation in the automobile financing market and of its impact on consumers. The annual number of originations by a particular nonbank entity reflects the number of loans and leases it makes or facilitates (through purchases of the loans and leases) regarding one of the most important nonfinancial assets to American households. Further, because the term “aggregate annual originations” would be defined, in part, in terms of how many loans or leases an entity granted or purchased, the aggregate annual originations criterion would generally correlate to the size of the entity’s loan and lease portfolios.

The Bureau anticipates that nonbank covered persons could calculate aggregate annual originations without difficulty, should the occasion arise to do so. As a general matter, most market participants generally know the number of loans and leases they extend because they handle the servicing for these accounts. Further, they know the number of loans they make or purchase because they need to execute liens against the automobile titles. Also, nonbank covered persons in the automobile financing market will readily be able to ascertain aggregate annual originations because they are presumably expecting a payment for each loan and lease.

The Bureau has data on a significant portion of annual originations, as defined in this Proposed Rule, from Experian Automotive’s AutoCount database. AutoCount is a vehicle database that collects monthly transaction data from State Departments of Motor Vehicles (DMVs). In 46 states, DMV title and registration information includes the finance source on

record.<sup>79</sup> These finance sources are listed either individually or categorized into lender type. The Bureau proposes to use the AutoCount Lender Report as its data source for this rulemaking because it is based on title and registration information filed with State DMVs and, thus, is likely to be objective. It is also national in scope. The report covers almost the entire United States and includes transactions that in many ways approximate the Bureau’s proposed definition of “annual originations.” The Bureau recognizes, however, that estimates of “annual originations” based on the AutoCount data may be either over- or under inclusive due to differences between what is included in the AutoCount data and in the Bureau’s proposed definitions. For example, the term “annual originations,” as defined in the Proposed Rule, includes transactions not tracked in the AutoCount report. Specifically, the Proposed Rule defines “annual originations” to include the sum of a nonbank covered person’s loans, leases, refinancings, and the purchase and acquisition of credit obligations (including refinancings) and leases. In contrast, the AutoCount data are less inclusive and track only loans and leases for which a title and registration is filed with the state DMV. Thus, unlike the Proposed Rule, the AutoCount report does not include refinancings and may not include all purchases and acquisitions of credit obligations and leases. Similar to the Proposed Rule, AutoCount excludes vehicles that are designed for and used primarily for commercial purposes. However, the exact scope of which commercial transactions are excluded in AutoCount may be different than in the Proposed Rule. The Bureau invites comments on this data source as well as suggestions for other data sources that commenters believe might augment the Bureau’s understanding and analysis of the market.

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<sup>79</sup> The AutoCount data cover transactions in every state, excluding Oklahoma, Wyoming, Rhode Island and Delaware.



*Threshold.* Under the Proposed Rule, a nonbank covered person would be a larger participant of the automobile financing market if the person has at least 10,000 aggregate annual originations. The Bureau estimates that the proposed threshold would bring within the Bureau's supervisory authority about 38 entities, roughly 7 percent of all nonbank covered persons in the automobile financing market.<sup>80</sup> Based on the number of covered transactions, the Bureau estimates that these 38 entities are responsible for approximately 91 percent of the activity in the nonbank automobile financing market.<sup>81</sup>

The Bureau anticipates that the proposed aggregate annual originations threshold of 10,000 would allow the Bureau to supervise market participants that represent a substantial portion of the automobile financing market and that have a significant impact on consumers. In 2013, the 38 entities that the Bureau estimates would be larger participants under the proposed threshold provided loans and leases to approximately 6.8 million consumers.<sup>82</sup> At the same time, this threshold would likely subject to the Bureau's supervisory authority only entities that can reasonably be considered larger participants of the market.

The Bureau is also considering a lower or higher threshold. For example, an aggregate annual originations threshold of 5,000 might allow the Bureau to supervise approximately 55 entities, representing nearly 93 percent of activity in this market.<sup>83</sup> While lowering the threshold would substantially increase the number of entities subject to supervision, the lower threshold would result in only a marginal increase in market coverage. The additional entities that would be included using this lower threshold are only a fraction of the size of the smallest entities that

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<sup>80</sup> Experian Automotive's AutoCount as adjusted by the CFPB, *see supra* note 61.

<sup>81</sup> *Id.*

<sup>82</sup> *Id.* The Bureau assumes that an average consumer only enters into one auto loan or lease in a given year.

<sup>83</sup> *Id.*

meet the proposed threshold and are mostly regional finance companies. In comparison, the Bureau estimates that an aggregate annual originations threshold of 50,000 would allow the Bureau to supervise the 17 very largest participants in the market, representing approximately 86 percent of market activity.<sup>84</sup> However, at this higher threshold the Bureau would not be able to supervise as varied a mix of nonbank larger participants that have a substantial impact on the full spectrum of consumers in the market.

The Bureau seeks comment, including suggestions of alternatives on the proposed threshold for defining larger participants of the automobile financing market.

*Section 1090.108(c)—Exclusion*

Proposed § 1090.108(c)(1) would provide that those motor vehicle dealers that are excluded from the Bureau’s authority by section 1029 of the Dodd-Frank Act do not qualify as larger participants under this section.<sup>85</sup> Proposed § 1090.108(c)(2) would also exclude additional motor vehicle dealers that are not subject to the statutory exclusion – specifically, those motor vehicle dealers that are identified in section 1029(b)(2) of the Dodd-Frank Act and are predominantly engaged in the sale and servicing of motor vehicles, the leasing and servicing of motor vehicles, or both. This would exclude from the proposed larger-participant rule certain dealers that extend retail credit or leases to consumers without routinely assigning them to unaffiliated third parties. Although section 1029(b)(2) provides the Bureau with rulemaking and other authority over such dealers, the Bureau has chosen to exclude them from the market defined in this Proposed Rule. These entities use a different business model, as described above,

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<sup>84</sup> *Id.*

<sup>85</sup> 12 U.S.C. 5519.

are typically much smaller in asset size and activity level than other entities that the Bureau proposes to include, and therefore form part of a separate and distinct market.<sup>86</sup> However, nonbank covered persons that meet the definition of “motor vehicle dealer” under section 1029(f)(2), but are not predominantly engaged in the sale and servicing of motor vehicles, the leasing and servicing of motor vehicles, or both would not be excluded from the proposed larger-participant rule.

## **V. Request for Comments**

The Bureau invites comment on all aspects of this notice of proposed rulemaking and on the specific issues on which comment is solicited elsewhere herein, including on any appropriate modifications or exceptions to the Proposed Rule.

## **VI. Section 1022(b)(2)(A) of the Dodd-Frank Act**

### *A. Overview*

The Bureau is considering potential benefits, costs, and impacts of the Proposed Rule.<sup>87</sup> The Bureau requests comment on the preliminary analysis presented below as well as submissions of additional data that could inform the Bureau’s analysis of the costs, benefits, and impacts of the Proposed Rule. In developing the Proposed Rule, the Bureau has consulted with

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<sup>86</sup> As the Bureau has explained, this larger-participant rulemaking is only one in a series of rulemakings, and the Bureau could address motor vehicle dealers identified in section 1029(b)(2) in a separate larger-participant rulemaking with a criterion and threshold that is better tailored to their business model and activity levels, should it determine that it is appropriate to do so.

<sup>87</sup> Specifically, 12 U.S.C. 5512(b)(2)(A) calls for the Bureau to consider the potential benefits and costs of a regulation to consumers and covered persons, including the potential reduction of access by consumers to consumer financial products or services, the impact on depository institutions and credit unions with \$10 billion or less in total assets as described in 12 U.S.C. 5516, and the impact on consumers in rural areas. In addition, 12 U.S.C. 5512(b)(2)(B) directs the Bureau to consult, before and during the rulemaking, with appropriate prudential regulators or other Federal agencies, regarding consistency with objectives those agencies administer. The manner and extent to which the provisions of 12 U.S.C. 5512(b)(2) apply to a rulemaking of this kind that does not establish standards of conduct are unclear. Nevertheless, to inform this rulemaking more fully, the Bureau performed the analysis and consultations described in those provisions of the Dodd-Frank Act.

or offered to consult with the Federal Trade Commission, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the National Credit Union Administration regarding, among other things, consistency with any prudential, market, or systemic objectives administered by such agencies.

The Proposed Rule would define a category of nonbanks that would be subject to the Bureau's nonbank supervision program pursuant to section 1024(a)(1)(B). The proposed category would include "larger participants" of a market for "automobile financing" described in the Proposed Rule. Participation in this market would be measured on the basis of aggregate annual originations. If a nonbank covered person, together with its affiliated companies, has aggregate annual originations (measured for the preceding calendar year) of at least 10,000, it would be a larger participant in the market for automobile financing. As prescribed by existing § 1090.102, any nonbank covered person that qualifies as a larger participant would remain a larger participant until two years after the first day of the tax year in which the person last met the larger-participant test.<sup>88</sup> The Proposed Rule would also include in the definition of "financial product[s] or service[s]" a new category of automobile leases, as defined by the Proposed Rule, under authority granted to the Bureau by section 1002(15)(A)(xi)(II) of the Dodd-Frank Act.<sup>89</sup>

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<sup>88</sup> 12 CFR 1090.102.

<sup>89</sup> The Proposed Rule also clarifies how to address aggregation of formerly-affiliated companies for purposes of assessing larger-participant status under the existing Consumer Reporting and Consumer Debt Collection Rules, by making changes to the definition of "annual receipts" in those rules. As explained above, the proposed changes to the affiliate aggregation provisions clarify the Bureau's methodology for affiliate aggregation. The proposed changes would provide marginal benefits for market participants in the consumer reporting and consumer debt collection markets by making those rules clearer and easier to understand. They may, however, result in an additional cost to market participants that are seeking to assess whether they are larger participants, but only if they would not have collected information relevant to thresholds from formerly affiliated companies for the entire preceding calendar year when the affiliation ended during the preceding calendar year. The Bureau does not know the extent to which participants seeking to self-assess currently collect information relevant to thresholds from formerly affiliated companies. However, if the proposed clarification is finalized, participants seeking to self-assess

## *B. Potential Benefits and Costs to Consumers and Covered Persons*

This analysis considers the benefits, costs, and impacts of the key provisions of the Proposed Rule against a baseline that includes the Bureau's existing rules defining larger participants in certain markets.<sup>90</sup> At present, there is no Federal program for supervision of nonbank covered persons in the automobile financing market with respect to Federal consumer financial law. The Proposed Rule extends the Bureau's supervisory authority over larger participants of the defined automobile financing market. This includes the authority to supervise for compliance with the Equal Credit Opportunity Act (ECOA), the Truth in Lending Act (TILA), and the Consumer Leasing Act, as well as other Federal consumer financial laws, to the extent applicable.

The Bureau notes at the outset that limited data are available with which to quantify the potential benefits, costs, and impacts of the Proposed Rule. As described above, the Bureau has utilized Experian AutoCount database for quantitative information on the number of market participants and their number and dollar volume of originations. However, the Bureau lacks detailed information about their rate of compliance with Federal consumer financial law and about the range of, and costs of, compliance mechanisms used by market participants.

In light of these data limitations, this analysis generally provides a qualitative discussion of the benefits, costs, and impacts of the Proposed Rule. General economic principles, together

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could arrange to obtain the necessary threshold information in advance of ending the affiliation, and such arrangements would tend to mitigate the costs of obtaining this information. Further, as noted above, participants in these markets are not required to engage in such self-assessments. Thus, both the benefits and costs of these amendments would not be significant.

<sup>90</sup> The Bureau has discretion in any rulemaking to choose an appropriate scope of analysis with respect to potential benefits and costs and an appropriate baseline. The Bureau, as a matter of discretion, has chosen to describe a broader range of potential effects to inform the rulemaking more fully.

with the AutoCount data, provide insight into these benefits, costs, and impacts. Where possible, the Bureau has made quantitative estimates based on these principles and data as well as its experience of undertaking similar supervisory activities with respect to depository institutions and credit unions.

The discussion below describes four categories of potential benefits and costs. First, the Proposed Rule, if adopted, would authorize the Bureau to supervise certain nonbank entities in the automobile financing market. These larger participants in the market might respond to the possibility of supervision by changing their systems and conduct, and those changes might result in costs, benefits, or other impacts. Second, if the Bureau undertakes supervisory activity at specific larger participants, those companies would incur costs from responding to supervisory activity, and the results of the individual supervisory activities might also produce benefits and costs.<sup>91</sup> Third, entities might incur certain costs as a result of their efforts to assess whether they would qualify as larger participants under the Proposed Rule. Fourth, including certain automobile leases in the Dodd-Frank Act definition of “financial product or service” would subject those leases to the prohibition on unfair, deceptive, or abusive acts or practices (UDAAP) under section 1031 of the Dodd-Frank Act and to Bureau authority to prescribe certain rules applicable to a covered person or service provider under section 1031(b) of the Dodd-Frank Act. The proposed definition would also expand the Bureau’s supervisory authority, as described

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<sup>91</sup> Pursuant to 12 U.S.C. 5514(e), the Bureau also has supervisory authority over service providers to nonbank covered persons encompassed by 12 U.S.C. 5514(a)(1), which includes larger participants. The Bureau does not have data on the number or characteristics of service providers to the larger participants of the automobile financing market. The discussion herein of potential costs, benefits, and impacts that may result from the Proposed Rule generally applies to service providers to larger participants.

below, and these changes might also produce benefits and costs, although the Bureau does not expect these effects to be significant.

In considering the costs and benefits of the Proposed Rule, it is important to note that various products or services are included in the proposed automobile financing market. Direct lending, where the consumer applies for credit directly to the financial institution, makes up a relatively small portion of the total auto loan and sales volume. Direct lending is currently dominated by traditional depository institutions and credit unions already regulated by the Bureau and other governmental agencies. Indirect lending, where a dealer—rather than the consumer—finds a lender willing to provide credit to the consumer, comprises a significant portion of the automobile financing market. In addition, some consumers refinance the credit obligation for their automobile after taking out the initial loan. Finally, leasing is the other primary way in which consumers can finance the use of a vehicle; under this arrangement a financial institution holds the title to the vehicle that the consumer leases under a payment plan that typically ends with an option to purchase the vehicle.<sup>92</sup>

#### *1. Benefits and Costs of Responses to the Possibility of Supervision*

The Proposed Rule would subject larger participants of the automobile financing market to the possibility of Bureau supervision. That the Bureau would be authorized to undertake supervisory activities with respect to a nonbank covered person who qualified as a larger participant would not necessarily mean the Bureau would in fact undertake such activities with respect to that covered entity in the near future. Rather, supervision of any particular larger

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<sup>92</sup> According to Experian Automotive, of all new and used auto financing transactions recorded in the first quarter of 2014, approximately 14 percent occurred through leasing arrangements, while the remainder used purchase financing. See Zabritski, *supra* note 25.

participant as a result of this rulemaking would be probabilistic in nature. For example, the Bureau would examine certain larger participants on a periodic or occasional basis. The Bureau's decisions about supervision would be informed, as applicable, by the factors set forth in section 1024(b)(2), relating to the size and volume of individual participants, the risks their consumer financial products and services pose to consumers, the extent of State consumer protection oversight, and other factors that the Bureau may determine are relevant. Each entity that believed it qualified as a larger participant would know that it might be supervised and might gauge, given its circumstances, the likelihood that the Bureau would initiate an examination or other supervisory activity.

The prospect of potential supervisory activity could create an incentive for larger participants to allocate additional resources and attention to compliance with Federal consumer financial law, potentially leading to an increase in the level of compliance. These entities might anticipate that by doing so (and thereby decreasing risks to consumers) they could decrease the likelihood of their actually being subjected to supervision as the Bureau evaluated the factors outlined above. In addition, an actual examination would likely reveal any past or present noncompliance, which the Bureau could seek to correct through supervisory activity or, in some cases, enforcement actions. Larger participants might therefore judge that the prospect of supervision increased the potential consequences of noncompliance with Federal consumer financial law, and they might seek to decrease that risk by curing or mitigating any noncompliance. Larger participants might thus be able to catch and address compliance problems at an earlier point when the costs of correcting them would be lower.

The Bureau believes it is likely that many market participants would increase compliance in response to the Bureau's supervisory activities authorized by the Proposed Rule. However,



because the Proposed Rule itself would not require any nonbank covered person in the automobile financing market to alter its conduct, any estimate of the amount of increased compliance would require both an estimate of current compliance levels and a prediction of market participants' behavior in response to a final rule. The data the Bureau currently has do not support a specific quantitative estimate or prediction. But, to the extent that nonbank entities allocate resources to increase their compliance in response to the Proposed Rule, that response would result in both benefits and costs to consumers and covered persons.<sup>93</sup>

*a. Benefits from Increased Compliance*

Increased compliance with Federal consumer financial law by larger participants in the market for automobile financing would be beneficial to consumers who either finance the purchase of or lease automobiles, or refinance their credit obligation related to the purchase of their automobile. The number of individuals who could potentially be affected is significant. As noted above, data from the first quarter of 2014 show auto lenders holding more than 87.4 million outstanding automobile loans, totaling almost \$900 billion.<sup>94</sup> The market is even larger when taking into account the automobile leasing market, which comprised an additional 14 percent of the automobile financing market in the first quarter of 2014.<sup>95</sup> Increasing the rate of compliance with Federal consumer financial law would benefit consumers and the consumer financial market by providing more of the protections mandated by law.

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<sup>93</sup> Another approach to considering the benefits, costs, and impacts of the Proposed Rule would be to focus almost entirely on the supervision-related costs for larger participants and omit a broader consideration of the benefits and costs of increased compliance. As noted above, the Bureau has, as a matter of discretion, chosen to describe a broader range of potential effects to inform the rulemaking more fully.

<sup>94</sup> *Supra* note 54.

<sup>95</sup> *See* Zabritski, *supra* note 25, at 20.

Several Federal consumer financial laws offer protections to consumers in regards to automobile financing as defined in the Proposed Rule, including, to the extent applicable, TILA and Regulation Z, the Fair Credit Reporting Act and Regulation V, the Consumer Leasing Act and Regulation M, ECOA and Regulation B, and the Gramm-Leach-Bliley Act and Regulation P.<sup>96</sup> More broadly, the Bureau would examine whether larger participants of the automobile financing market engage in UDAAPs.<sup>97</sup> Conduct that does not violate an express prohibition of another Federal consumer financial law may nonetheless constitute a UDAAP.<sup>98</sup> To the extent that any larger participant or service provider is currently engaged in any UDAAP in connection with any transaction for or the offering of a consumer financial product or service, the cessation of the unlawful act or practice would benefit consumers. As the Bureau may review a larger participant's conduct in relation to any consumer financial product or service during an examination, larger participants might improve policies and procedures globally in response to possible supervision in order to avoid engaging in UDAAPs.

The possibility of supervision also may help make incentives to comply with Federal consumer financial law more consistent between the likely larger participants and depository institutions and credit unions, which are already subject to Federal supervision with respect to Federal consumer financial law. Introducing the possibility of Federal supervision could encourage entities that would likely qualify as larger participants to devote additional resources

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<sup>96</sup> The Bureau recognizes that the nature of a larger participant's responsibility for compliance with these laws may vary depending on the activity the larger participant engages in. For example, under TILA, a larger participant that purchases a credit obligation for the purchase of an automobile is likely an assignee, not a "creditor" under TILA, and as such is generally liable only for a violation of TILA that is "apparent on the face of the disclosure statement." 15 U.S.C. 1641(a).

<sup>97</sup> 12 U.S.C. 5531.

<sup>98</sup> The CFPB Supervision and Examination Manual provides further guidance on how the UDAAP prohibition applies to supervised entities. CFPB, *CFPB Supervision and Examination Manual – Version 2.0* (Oct. 2012), available at <http://www.consumerfinance.gov/guidance/supervision/manual>.

to compliance. It could also help ensure that the benefits of Federal oversight reach consumers who do not have ready access to automobile financing through depository institutions and credit unions.

*b. Costs of Increased Compliance*

The Bureau recognizes that increasing compliance involves costs. These costs may be fixed or ongoing. Nonbank entities in the automobile financing market might need to hire or train additional personnel to effectuate any changes in their practices that would be necessary to produce the increased compliance. They might need to invest in changes to their systems to carry out their revised procedures. In addition, they might need to develop or enhance compliance management systems, to ensure awareness of any gaps in compliance. Such changes would also require investment and might entail increased operating costs.

Economic theory predicts that fixed costs will be absorbed by providers, here the entities that may qualify as larger participants. However, consumers may be adversely affected by increases in these costs to the extent these cost increases cause current providers of automobile financing to decrease volume, deter providers from increasing volume, or deter entry by new providers in the future.<sup>99</sup> This could result in consumers having more restricted choices than they would otherwise. In certain situations, a decrease in the number of market participants could better enable those remaining providers to exercise market power, resulting in higher prices for consumers or decreased product or service quality, or both.

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<sup>99</sup> Alexei Alexandrov & Xiaoling Ang, *Identifying a Suitable Control Group Based on Microeconomic Theory: The Case of Escrows in the Subprime Market* (July 3, 2014) (finding consumers not adversely affected by policy changes that implement a fixed cost), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2462128](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2462128).

An entity that incurs ongoing costs in support of increasing compliance might try to recoup these costs by attempting to pass those costs directly through to consumers; for example, in the case of the indirect channel, this could occur through lowering fees or other forms of compensation paid to dealers and other entities. Whether and to what extent either change would occur depends on the relative elasticities of supply and demand in the automobile financing market. These elasticities can vary across products or services that would be covered by the Proposed Rule and may be influenced by the presence of substitute products or services as well as the availability of information, which would influence the perceived availability of substitute products or services. For example, larger participants of the automobile financing market may be in competition with depository institutions or credit unions (or affiliates thereof) that are already subject to supervision by the Bureau and/or Federal prudential regulators with respect to Federal consumer financial law. To the extent the Proposed Rule would result in an increase in the costs faced by larger participants, that increase would be a competitive benefit to banks and credit unions with sufficient liquidity to expand their financing operations. Competition from banks and credit unions might reduce the ability of larger participants to pass through cost increases to consumers, dealers, or other entities as they may instead seek alternate sources of financing. Moreover, consumers might respond to such a cost increase by reducing the amounts they are willing to pay in other aspects of the automobile purchase transaction, while dealers could respond to decreased levels of financing revenues shared with them by larger participants by either attempting to increase revenues derived from other areas of the automobile purchase transaction, such as the stated price of the vehicle or costs of accessories, or bearing the loss of revenue.

In considering any potential price effect of the Proposed Rule, it is important to take into account the fact that nonbank covered persons below the larger participant threshold would not be subject to supervision as a result of this rule. The costs of these nonbank covered persons would therefore be unaffected by the definition of larger participants in the Proposed Rule and so their pricing should also not be affected. To the extent that nonbank larger participants raise their prices in response to this rule, nonbank entities that are not larger participants, along with banks and credit unions that already compete in the market while bearing the cost of supervision, could potentially offer more attractive transaction terms relative to larger participants and thus deter larger participants from increasing prices. While a shift in transactions from larger participants toward nonbank entities that are not larger participants would mitigate some of the benefits to consumers of supervision of larger participants, the prospect of this shift might also reduce the likelihood that larger participants would choose to increase their prices in response to the Proposed Rule.

## *2. Benefits and Costs of Individual Supervisory Activities*

In addition to the responses of market participants anticipating supervision, the possible consequences of the Proposed Rule would include the responses to and effects of individual examinations or other supervisory activities that the Bureau might conduct in the automobile financing market.

### *a. Benefits of Supervisory Activities*

Supervisory activity could provide several types of benefits. For example, as a result of supervisory activity, the Bureau and an entity might uncover deficiencies in the entity's policies and procedures. The Bureau's examination manual calls for the Bureau generally to prepare a report of each examination, to assess the strength of the entity's compliance mechanisms, and to

assess the risks the entity poses to consumers, among other things. The Bureau would share examination findings with the examined entity because one purpose of supervision is to inform the entity of problems detected by examiners. Thus, for example, an examination might find evidence of widespread noncompliance with Federal consumer financial law, or it might identify specific areas where an entity has inadvertently failed to comply. These examples are only illustrative of the kinds of information an examination might uncover.

Detecting and informing entities about such problems should be beneficial to consumers. When the Bureau notifies an entity about risks associated with an aspect of its activities, the entity is expected to adjust its practices to reduce those risks. That response may result in increased compliance with Federal consumer financial law, with benefits like those described above. Or it may avert a violation that would have occurred had Bureau supervision not detected the risk promptly. The Bureau may also inform entities about risks posed to consumers that fall short of violating the law. Action to reduce those risks would also be a benefit to consumers.

Given the obligations nonbank covered persons in the automobile financing market have under Federal consumer financial law and the existence of efforts to enforce such law, the results of supervision also may benefit entities under supervision by detecting compliance problems early. When an entity's noncompliance results in litigation or an enforcement action, the entity must face both the costs of defending its actions and the penalties for noncompliance, including potential liability for damages to private plaintiffs. The entity must also adjust its systems to ensure future compliance. Changing practices that have been in place for long periods of time can be expected to be relatively difficult because the practices may be severe enough to represent a serious failing of an entity's systems. Supervision may detect flaws at a point when correcting them would be relatively inexpensive. Catching problems early can, in some situations, forestall

costly litigation. To the extent early correction limits the amount of consumer harm caused by a violation, it can help limit the cost of redress. In short, supervision might benefit larger participants by, in the aggregate, reducing the need for other more expensive activities to achieve compliance.<sup>100</sup>

*b. Costs of Supervisory Activities*

The potential costs of actual supervisory activities would arise in two categories. The first would involve any costs to larger participants of increasing compliance in response to the Bureau's findings during supervisory activity and to supervisory actions. These costs would be similar in nature to the possible compliance costs, described above, that larger participants in general might incur in anticipation of possible supervisory actions. This analysis will not repeat that discussion. The second category would be the cost of supporting supervisory activity.

Supervisory activity may involve requests for information or records, on-site or off-site examinations, or some combination of these activities. For example, in an on-site examination, Bureau examiners generally contact the entity for an initial conference with management. That initial contact is often accompanied by a request for information or records. Based on the discussion with management and an initial review of the information received, examiners determine the scope of the on-site exam. While on-site, examiners spend some time in further conversation with management about the entity's policies, procedures, and processes. The

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<sup>100</sup> Further potential benefits to consumers, covered persons, or both might arise from the Bureau's gathering of information during supervisory activities. The goals of supervision include informing the Bureau about activities of market participants and assessing risks to consumers and to markets for consumer financial products and services. The Bureau may use this information to improve regulation of consumer financial products and services and to improve enforcement of Federal consumer financial law, in order to better serve its mission of ensuring consumers' access to fair, transparent, and competitive markets for such products and services. Benefits of this type would depend on what the Bureau learns during supervision and how it uses that knowledge. For example, because the Bureau would examine a number of covered persons in the automobile financing market, the Bureau would build an understanding of how effective compliance systems and processes function in that market.

examiners also review documents, records, and accounts to assess the entity's compliance and evaluate the entity's compliance management system. As with the Bureau's other examinations, examinations of nonbank larger participants of the automobile financing market could involve issuing confidential examination reports and compliance ratings. The Bureau's examination manual describes the supervision process and indicates what materials and information an entity could expect examiners to request and review, both before they arrive and during their time on-site.

The primary cost an entity would face in connection with an examination would be the cost of employees' time to collect and provide the necessary information. If the Proposed Rule is adopted, the frequency and duration of examinations of any particular entity would depend on a number of factors, including the size of the entity, the compliance or other risks identified, whether the entity has been examined previously, and the demands on the Bureau's supervisory resources imposed by other entities and markets. Nevertheless, some rough estimates may be useful to provide a sense of the magnitude of potential staff costs that entities might incur.

The cost of supporting supervisory activity may be calibrated using prior Bureau experience in supervision. The Bureau considers its auto financing examinations at depository institutions and credit unions as a reasonable proxy for the duration and labor intensity of potential nonbank larger participant examinations. This belief arises from the similar role these institutions play in the market for automobile financing, where they frequently coexist as direct competitors to one another.



The average duration of the on-site portion of Bureau bank auto financing examinations is approximately 9 weeks.<sup>101</sup> Assuming that each exam requires 2 weeks of preparation time by a larger participant's staff prior to the exam as well as on-site assistance by staff throughout the duration of the exam, the Bureau assumes that the typical examination in this nonbank market would require 11 weeks of staff time. The Bureau has not suggested that counsel or any particular staffing level is required during an examination. However, for purposes of this analysis, the Bureau assumes, conservatively, that an entity might dedicate the equivalent of one full-time compliance officer and one-tenth of a full-time attorney to the exam. The average hourly wage of a compliance officer in a nonbank entity that operates in activities related to installment lending is \$33.97, and the average hourly wage of a lawyer in the same industry is \$83.88.<sup>102</sup> Assuming that wages account for 67.5 percent of total compensation, the total labor cost of an examination would be about \$27,611.<sup>103</sup> The Bureau estimates that the cost for an entity with 10,000 aggregate annual originations per year, with an average amount financed of

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<sup>101</sup> This estimate was derived using confidential supervisory Bureau data on the duration of on-site auto financing examinations at depository institutions and credit unions. For purposes of this calculation, the Bureau counted its auto financing examinations for which the on-site portion had been completed, while excluding the shortest and longest examinations to minimize the influence of outliers. Additionally, the Bureau counted only the on-site portion of an examination, which included time during the on-site period of the examination that examiners spent off-site for holiday or other travel considerations. However, the Bureau did not count time spent scoping an examination before the on-site portion of the examination or summarizing findings or preparing reports of examination afterwards.

<sup>102</sup> Bureau of Labor Statistics (BLS), *Occupational Employment Statistics*, available at <http://data.bls.gov/oes/>. (BLS data for "Nondepository Credit Intermediation" (North American Industry Classification System (NAICS) code 522200)). Dividing the hourly wage of a full-time compliance officer by 67.5 percent yields a total mean hourly cost (including total costs, such as salary, benefits, and taxes) rounded to the nearest dollar of \$50 per hour.

<sup>103</sup> BLS, *Employer Costs for Employee Compensation Database*, Series ID CMU2025220000000D, available at [http://data.bls.gov/timeseries/CMU2025220000000D?data\\_tool=XGtable](http://data.bls.gov/timeseries/CMU2025220000000D?data_tool=XGtable) (providing wage and salary percent of total compensation in the credit intermediation and related activities private industry for the second quarter of 2013). All figures assume 40 hours of work per week.

\$21,750 per loan origination,<sup>104</sup> would be approximately 0.013 percent of total revenue from originations for that year. This is a conservative estimate in several respects because it reflects revenue only from this line of business and uses an average amount financed in combination with the minimum number of transactions that a larger participant would provide.

The Bureau declines to predict, at this point, precisely how many examinations in the automobile financing market it would undertake in a given year. If the Proposed Rule is adopted, the Bureau would be able to undertake supervisory activity in the identified market; however, neither the Dodd-Frank Act nor the Proposed Rule specifies a particular level or frequency of examinations. Given the Bureau's finite supervisory resources, and the range of industries over which it has supervisory responsibility for consumer financial protection, when and how often a given larger participant would be supervised is uncertain. The frequency of examinations would depend on a number of factors, including the Bureau's understanding of the conduct of market participants and the specific risks they pose to consumers; the responses of larger participants to prior examinations; and the demands that other markets make on the Bureau's supervisory resources. These factors can be expected to change over time, and the Bureau's understanding of these factors may change as it gathers more information about the market through its supervision and by other means.

### *3. Costs of Assessing Larger-Participant Status*

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<sup>104</sup> The estimated average amount financed uses 2013 origination data from AutoCount for entities with 360 or greater loans and leases on an annual basis. The dollar value listed is based solely on loans, as the Bureau was unable to obtain data on the average amount financed in lease transactions. That said, the Bureau believes it is unlikely that the estimated revenue from leasing transactions, including both the stream of payments over the course of the lease as well as the option value of purchase or resale price of the vehicle at the end of the lease, would differ in a way that materially impacts the relationship between the cost of supervision and revenues.

The larger-participant rule does not require nonbank entities to assess whether they are larger participants. However, the Bureau acknowledges that in some cases they might decide to incur costs in assessing whether they qualify as larger participants and potentially disputing their status.

Larger-participant status depends on a nonbank's aggregate annual originations, as defined in the Proposed Rule. An estimate of this number should be readily extractible from company records, as market participants likely evaluate the components of aggregate annual originations as part of their regular business practices. In addition, information on originations can be derived from title records that market participants maintain and publicly record.

To the extent that some nonbank covered persons in the automobile financing market do not already know whether their aggregate annual originations exceed the threshold, such entities might, in response to the Proposed Rule, develop new systems to count their aggregate annual originations in accordance with the definition in the Proposed Rule. The data the Bureau currently has do not support a detailed estimate of how many nonbank entities would engage in such development or how much they might spend. Regardless, nonbank entities would be unlikely to spend significantly more on specialized systems to count aggregate annual originations than it would cost them to be supervised by the Bureau as larger participants. It bears emphasizing that even if expenditures on an accounting system successfully proved that a nonbank covered person in the automobile financing market was not a larger participant, it would not necessarily follow that this entity could not be supervised. The Bureau can supervise a nonbank entity whose conduct the Bureau determines, pursuant to section 1024(a)(1)(C), poses risks to consumers. Thus, a nonbank entity choosing to spend significant amounts on an accounting system directed toward the larger-participant test could not be sure it would not be

subject to Bureau supervision notwithstanding those expenses. The Bureau therefore believes it is unlikely that any but a very few nonbank entities would undertake such expenditures.

4. *Benefits and Costs of Adding Certain Automobile Leases to the Definition of “Financial Product or Service”*

Finally, the Bureau is proposing to define the term “financial product or service” to include automobile leases that (1) meet the requirements of section 108 of CEBA, as implemented by 12 CFR part 23, and are thus, permissible for banks to offer or provide; and (2) are not currently defined as a financial product or service under section 1002(15)(A)(ii) of the Dodd-Frank Act. As explained below, the Bureau believes that the benefits, costs, and impacts to consumers and covered persons of the proposed definition would likely be small. First, the proposed definition would not extensively alter the substantive obligations of covered persons. Second, the proposed definition would not substantially expand the market participants brought under supervision as a result of the Proposed Rule, or for entities already subject to supervision, the scope of supervisory examinations. The Bureau lacks data about the range of, and costs of, compliance mechanisms used by banks or nonbank entities in the automobile financing market. In light of these data limitations, the Bureau’s analysis generally provides a qualitative discussion of the benefits, costs, and impacts of the proposed definition.

a. *Benefits of the Proposed Definition*

Benefits of the proposed definition would stem from enhanced consumer protections relating to automobile leases that would fall under the definition. As financial products or services under the Dodd-Frank Act, such leases would become subject to the UDAAP prohibition under section 1031 of the Dodd-Frank Act. These leases are already subject to a similar prohibition against unfair or deceptive acts or practices (UDAP) in or affecting

commerce under section 5 of the Federal Trade Commission Act (FTC Act).<sup>105</sup> The prohibitions set forth in section 5 of the FTC Act and section 1031 of the Dodd-Frank Act, however, are not precisely co-extensive. Most notably, section 5 of the FTC Act does not include a prohibition on abusive acts or practices similar to that under section 1031 of the Dodd-Frank Act. Accordingly, consumers would benefit from the expanded scope of consumer protection under section 1031 of the Dodd-Frank Act in connection with transactions involving these leases.

The proposed definition also has the potential to expand supervisory activities in two distinct ways. First, the proposed definition, as incorporated into the larger participant rule proposal, could bring certain nonbank entities under Bureau supervision by expanding the activities counted in determining whether participants of the automobile financing market qualify as larger participants and are thus subject to supervision under the Proposed Rule. To the extent that nonbank entities in the automobile financing market would be brought under supervision as a result of the proposed definition, both consumers and covered persons would benefit. The nature of these benefits, including from both the possibility of supervision and actual individual supervisory activities, are discussed above.

Second, the proposed definition could affect the scope of supervision for other nonbank entities and certain banks and credit unions.<sup>106</sup> For nonbank entities in the automobile financing market that would be subject to supervision as a larger participant even absent the proposed

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<sup>105</sup> 15 U.S.C. 45. This prohibition is enforced by the Federal Trade Commission with respect to nonbanks under section 5 and by the prudential regulators with respect to banks under section 8 of the Federal Deposit Insurance Act, 12 U.S.C. 1818.

<sup>106</sup> With respect to nonbanks, the Bureau currently supervises mortgage companies, payday lenders, and private student lenders, as well as larger participants of the consumer reporting, consumer debt collection, and student loan servicing markets, and will soon have authority to supervise larger participants of the international money transfer market. The Bureau is not aware of any significant automobile leasing activity by these entities. Thus, the Bureau believes that the proposed definition in itself would have at most a marginal impact on the scope of examinations for these entities.

definition, the proposed definition would not expand the leasing activities of such entities subject to supervision. However, the proposed definition would expand the scope of supervision for leasing covered by the proposed definition to include compliance with section 1031 of the Dodd-Frank Act.

With respect to banks and credit unions, the Bureau has supervisory authority over large banks with total assets of more than \$10 billion (and their affiliates) for compliance with Federal consumer financial laws, and the prudential regulators exercise primary supervisory authority over other banks with total assets of \$10 billion or less for compliance with Federal consumer financial laws. As noted above, although the proposed definition would not expand the leasing activities of banks subject to supervision, for leasing covered under the proposed definition, it would expand the scope of that supervision to include compliance with section 1031 of the Dodd-Frank Act. Again, the benefits to consumers of that expanded supervision authority would be similar to the general benefits of supervision discussed above.

Although the Bureau has identified the above potential consumer benefits from the expanded supervision authority that could result from the proposed definition, the Bureau believes such benefits would be limited in extent. Most significantly, as discussed above, the Bureau believes that most automobile leases currently qualify as a financial product or service under section 1002(15)(A)(ii) of the Dodd-Frank Act. Thus, the Bureau believes that few, if any, nonbank participants in the automobile financing market will be subject to the Bureau's supervision under the Proposed Rule as a result of the proposed definition. Further, for bank and nonbank entities that would be subject to supervision even absent the proposed definition, the Bureau believes that the proposed definition would expand only the scope of supervision of the leasing activities of such entities. Notably, even absent the proposed definition, all leasing

activities of such entities would be subject to supervision by the Bureau or the prudential regulators for compliance with the “enumerated consumer laws” as defined in section 1002(12) of the Dodd-Frank Act, including the Consumer Leasing Act.<sup>107</sup> And under the existing regulatory framework, the prudential regulators are authorized to supervise banks for compliance with section 5 of the FTC Act. Thus, for entities that would be subject to supervision even absent the proposed definition, the expanded supervision resulting from the proposed definition would be focused on the entity’s compliance with section 1031 of the Dodd-Frank Act in connection with the activities covered by the proposed definition.

Finally, under section 1031(b) of the Dodd-Frank Act, the Bureau has authority to prescribe rules applicable to a covered person or service provider identifying as unlawful unfair, deceptive, or abusive acts or practices in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service. Thus, if the proposed definition is finalized, the Bureau could promulgate such rules in connection with transactions for the leases that would fall under the proposed definition. The Bureau would consider the benefits, costs, and impacts of any such rulemaking as part of its analysis under section 1022 for that rulemaking. The Bureau notes that any such rulemaking would likely aim to provide consumers and covered persons with additional clarity in regard to identifying unfair, deceptive or abusive acts or practices. It is not possible, however, to identify

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<sup>107</sup> With respect to the enumerated consumer laws, the scope of the Bureau’s authority is defined by the scope of those laws, not by the activities listed under section 1002(15)(A) of the Dodd-Frank Act.

with any greater specificity here the potential benefits to consumers or covered persons from the proposed definition as a result of an unspecified future rulemaking.<sup>108</sup>

*b. Costs of the Proposed Definition*

The proposed definition would impose compliance costs on covered persons by subjecting leasing activities that fall under the proposed definition to the UDAAP prohibitions in section 1031 of the Dodd-Frank Act. Those entities would incur some cost of compliance because, as laid out above, the prohibitions under section 1031 of the Dodd-Frank Act and section 5 of the FTC Act are not co-extensive: in particular, section 5 of the FTC Act does not include a prohibition on abusive acts or practices similar to that under section 1031 of the Dodd-Frank Act. However, given the fact that, as interpreted by the Bureau, section 1002(15)(A)(ii) covers most automobile leases and the substantial overlap of the prohibited conduct under section 1031 of the Dodd-Frank Act and section 5 of the FTC Act, in the Bureau's judgment, the compliance costs to covered persons of this new prohibition would be limited in extent.

Regarding supervision, the proposed definition, as incorporated into the larger participant rule proposal, could also bring certain nonbank entities under Bureau supervision and would

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<sup>108</sup> The proposed definition would also benefit consumers by expanding the scope of certain other Bureau authorities under title X of the Dodd-Frank Act. Perhaps most significantly, the proposed definition would expand the Bureau's rulemaking authority under section 1032 of the Dodd-Frank Act, which authorizes the Bureau to prescribe rules to ensure that the features of any consumer financial product or service are fully, accurately, and effectively disclosed to consumers in a manner that permits consumers to understand the costs, benefits, and risks associated with the product or service. In addition, the proposed definition would expand the scope of the Bureau's authority under section 1022(c) of the Dodd-Frank Act to "monitor for risks to consumers in the offering or provision of consumer financial products or services, including developments in markets for such products or services," and the scope of the Bureau's authority under section 1033 of the Dodd-Frank Act to prescribe rules for covered persons with respect to consumer rights to access information concerning consumer financial products or services that the consumer received from such person. As with respect to section 1031(b) of the Dodd-Frank Act, it is not possible for the Bureau to identify with specificity here the benefits to consumers that might result from the Bureau's potential future exercise of these authorities. The Bureau, however, notes that it would consider the benefits, costs, and impacts of any rulemakings under sections 1032 or 1033 of the Dodd-Frank Act as part of the section 1022 analysis for such rulemakings.



affect the scope of supervision for other nonbank entities, banks, and credit unions. With respect to nonbanks, the proposed definition would, as discussed above, expand the activities counted in determining whether participants of the automobile financing market qualify as larger participants and are thus subject to supervision under the Proposed Rule. To the extent that larger participants in the automobile financing market are brought under supervision as a result of the proposed definition, such entities would incur costs. The nature of these costs, including from the possibility of supervision as well as from actual individual supervisory activities, are discussed above. For participants of the automobile financing market that would be subject to supervision under the proposed larger-participant rule even absent the proposed definition, the proposed definition would impose costs by expanding the leasing activities of such entities subject to supervision for compliance with section 1031 of the Dodd-Frank Act. With respect to banks and credit unions, by expanding the leasing activities subject to the section 1031 UDAAP prohibition, as discussed above, the proposed definition would correspondingly expand the activities subject to supervision by either the Bureau or the prudential regulators, as applicable, for compliance with that prohibition.

For both banks and nonbanks, the Bureau believes that the increased costs of supervision identified above would be small. As discussed above, the Bureau believes that most auto leases currently qualify as a financial product or service under section 1002(15)(A)(ii) of the Dodd-Frank Act. Thus, the Bureau believes that few, if any, nonbank participants in the automobile financing market will be brought under Bureau supervision under the Proposed Rule as a result of the proposed definition. Similarly, for banks and nonbank entities that would be subject to supervision even absent the proposed definition, the Bureau believes that the proposed definition would only subject the leasing activities of such entities to slightly expanded supervision.

Notably, even absent the proposed definition, all leasing activities of such entities would be subject to supervision by the Bureau or the prudential regulators for compliance with the enumerated consumer laws, including the Consumer Leasing Act.<sup>109</sup> And under the existing regulatory framework, the prudential regulators are authorized to supervise banks for compliance with section 5 of the FTC Act. Thus, for entities that would be subject to supervision even absent the Proposed Rule, the scope of expanded supervision for the limited activities that would fall under the proposed definition would be further limited to compliance with section 1031 of the Dodd-Frank Act. The Bureau believes that the additional cost to entities already subject to supervision of being supervised for compliance with section 1031 of the Dodd-Frank Act would be minimal.

Finally, under section 1031(b) of the Dodd-Frank Act, the Bureau has authority to prescribe rules applicable to a covered person or service provider identifying as unlawful unfair, deceptive, or abusive acts or practices in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service. Thus, if the proposed definition is finalized, the Bureau could promulgate such rules in connection with transactions for the leases that would fall under the proposed definition. Such a rule may impose costs on covered persons or service providers. It is not possible to identify with any greater specificity here the potential costs to covered persons or service providers of any such hypothetical future rulemaking. The Bureau notes, however, that it would consider the

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<sup>109</sup> With respect to the enumerated consumer laws, the scope of the Bureau's authority is defined by the scope of those laws, not by the activities listed under section 1002(15)(A) of the Dodd-Frank Act.

benefits, costs, and impacts of any such rulemaking as part of its analysis under section 1022 for that rulemaking.<sup>110</sup>

#### 5. *Consideration of Alternatives*

The Bureau is considering different thresholds for larger-participant status in the market for automobile financing. One alternative the Bureau is considering is a larger threshold of, for example, 50,000 aggregate annual originations. Under such an alternative, the benefits of supervision to both consumers and covered persons would likely be substantially reduced because some firms impacting a large portion of consumers in important market segments, such as captive, subprime, and BHPH lending, would be omitted. On the other hand, the overall potential costs across all nonbank covered persons would of course be reduced if fewer firms were defined as larger participants and thus fewer were subject to the Bureau's supervision authority on that basis. Similarly, the Bureau is also considering lower thresholds, such as 5,000 aggregate annual originations, but believes this would only marginally increase the proportion of market activity that the Bureau could supervise while potentially exposing a greater number of nonbank covered persons to the costs listed above. However, the total direct costs for actual

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<sup>110</sup> The proposed definition would also impose costs on covered persons by expanding the scope of certain other Bureau authorities under title X of the Dodd-Frank Act. Specifically, the proposed definition would expand the Bureau's rulemaking authority under section 1032 of the Dodd-Frank Act, which authorizes the Bureau to prescribe rules to ensure that the features of any consumer financial product or service are fully, accurately, and effectively disclosed to consumers in a manner that permits consumers to understand the costs, benefits, and risks associated with the product or service. In addition, the proposed definition would expand the scope of the Bureau's authority under section 1022(c) of the Dodd-Frank Act to "monitor for risks to consumers in the offering or provision of consumer financial products or services, including developments in markets for such products or services," and the scope of the Bureau's authority under section 1033 of the Dodd-Frank Act, to prescribe rules for covered persons with respect to consumer rights to access information concerning consumer financial products or services that the consumer received from such person. As with respect to section 1031(b) of the Dodd-Frank Act, it is not possible for the Bureau to identify with specificity here the costs to covered persons that may result from the Bureau's potential future exercise of these authorities. The Bureau, however, notes that it would consider the benefits, costs, and impacts of any rulemakings under sections 1032 or 1033 of the Dodd-Frank Act as part of the section 1022 analysis for such rulemakings.

supervisory activity might not change substantially because the Bureau conducts exams on a risk basis and would not necessarily examine more or fewer entities if the rule's coverage were broader or narrower.

The Bureau is also considering various other criteria for assessing larger-participant status, including dollar volume of originations and total unpaid principal balances. Calculating either of these metrics might be more involved than calculating the number of originations for a given nonbank entity. If so, then a given entity might face greater costs for evaluating or disputing whether it qualified as a larger participant should the occasion to do so arise.

Additionally, as some nonbank entities might, for example, specialize in sectors featuring higher average loan amounts or different prepayment and default rates than others, using aggregate annual originations more directly captures the number of consumers impacted by the Proposed Rule. For each criterion, the Bureau expects that it could choose a suitable threshold for which the set of larger participants, among those entities participating in the market today, would be similar to those expected to qualify under the Proposed Rule. Consequently, the costs, benefits, and impacts of this Proposed Rule should not depend on which criterion the Bureau uses.

### *C. Potential Specific Impacts of the Proposed Rule*

#### *1. Depository Institutions and Credit Unions With \$10 Billion or Less in Total Assets, As Described in Section 1026 of the Dodd-Frank Act*

No depository institutions or credit unions of any size would become larger participants in the market for automobile leases under the Proposed Rule. Further, as explained above, the proposed change in the definition of financial product or service would not in itself have any significant effect on depository institutions and credit unions with \$10 billion or less in total assets. Nevertheless, the Proposed Rule might, as discussed above, have some impact on

depository institutions or credit unions that provide financing for automobile transactions. The Proposed Rule might therefore alter market dynamics in a market in which some depository institutions and credit unions with less than \$10 billion in assets may be active. For example, if nonbanks' price of credit for loan acquisitions or leases were to increase, or similarly were the compensation for selling those same products to decrease due to increased costs related to supervision, then depository institutions or credit unions of any size might benefit by the relative change in competitors' costs.

*2. Impact of the Provisions on Consumer Access to Credit and on Consumers in Rural Areas*

Because the rule applies uniformly to automobile financing transactions of both rural and non-rural consumers, the rule should not have a unique impact on rural consumers. The Bureau is not aware of any evidence suggesting that rural consumers have been disproportionately harmed by nonbank entities' failure to comply with Federal consumer financial law. The Bureau would welcome any comments that may provide information related to how automobile financing transactions affect rural consumers.

## **VII. Regulatory Flexibility Act**

The Regulatory Flexibility Act (RFA), as amended by the Small Business Regulatory Enforcement Fairness Act of 1996,<sup>111</sup> requires each agency to consider the potential impact of its regulations on small entities, including small businesses, small governmental units, and small not-for-profit organizations.<sup>112</sup> The RFA defines a "small business" as a business that meets the

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<sup>111</sup> The RFA, Public Law 96-354, 94 Stat. 1164 (1980) (codified as amended at 5 U.S.C. 601-12).

<sup>112</sup> The term "'small organization' means any not-for-profit enterprise which is independently owned and operated and is not dominant in its field, unless an agency establishes [an alternative definition after notice and comment]."

size standard developed by the Small Business Administration (SBA) pursuant to the Small Business Act.<sup>113</sup>

The RFA generally requires an agency to conduct an initial regulatory flexibility analysis (IRFA) of any proposed rule subject to notice-and-comment rulemaking requirements, unless the agency certifies that the proposed rule would not have a significant economic impact on a substantial number of small entities.<sup>114</sup> The Bureau also is subject to certain additional procedures under the RFA involving the convening of a panel to consult with small entity representatives prior to proposing a rule for which an IRFA is required.<sup>115</sup>

The undersigned certifies that the Proposed Rule, if adopted, would not have a significant economic impact on a substantial number of small entities and that an IRFA is therefore not required.

The Proposed Rule would define a class of nonbank covered persons as larger participants of the automobile financing market and thereby would authorize the Bureau to undertake supervisory activities with respect to those nonbank covered persons. The Proposed Rule would also define the term “financial product[s] or service[s]” to include automobile leases that (1) meet the requirements of section 108 of CEBA, as implemented by 12 CFR part 23, and are thus permissible for banks to offer or provide; and (2) are not currently defined as a financial

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5 U.S.C. 601(4). The term “‘small governmental jurisdiction’ means governments of cities, counties, towns, townships, villages, school districts, or special districts, with a population of less than fifty thousand, unless an agency establishes [an alternative definition after notice and comment].” *Id.* at 601(5). The Bureau is not currently aware of any small governmental units or small not-for-profit organizations to which the Proposed Rule would apply.

<sup>113</sup> 5 U.S.C. 601(3). The Bureau may establish an alternative definition after consultation with SBA and an opportunity for public comment. *Id.*

<sup>114</sup> 5 U.S.C. 605(b).

<sup>115</sup> 5 U.S.C. 609.

product or service under section 1002(15)(A)(ii) of the Dodd-Frank Act. The Proposed Rule would not affect a substantial number of small businesses.

Regarding insured depositories and credit unions, these entities are small businesses only if their assets are below \$550 million. The proposed definition of larger participants of the automobile financing market applies only to nonbank entities, so it would have no impact on depository institutions or credit unions of any size. The proposed definition of the term financial product or service to include certain automobile leases would have little impact on compliance and supervision costs for insured depositories and credit unions. The leasing activities covered under the proposed definition would become subject to the UDAAP prohibition under section 1031 of the Dodd-Frank Act. Although the two are not co-extensive, as discussed above, a similar prohibition on UDAP in or affecting commerce under section 5 of the FTC Act already applies to these activities. Similarly, small banks are already subject to supervision for compliance with section 5 of the FTC Act, as well as with the enumerated consumer laws. In addition, most small banks have a very low share of leases relative to loans, and most of this leasing activity already qualifies as a financial product or service under section 1002(15)(A)(ii) of the Dodd-Frank Act. Accordingly, the Bureau estimates that very few to no small banks would experience a significant impact due to the proposed change to the definition of a financial product or service.

Regarding nonbank entities, the Proposed Rule adopts a threshold for larger-participant status of at least 10,000 aggregate annual originations.<sup>116</sup> Under the size standard for the most

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<sup>116</sup> As noted above, if a nonbank covered person meets the larger-participant test, it would remain a larger participant until two years from the first day of the tax year in which it last met the larger-participant test.

relevant SBA classification, *i.e.*, NAICS code 522220, an entity engaged in automobile financing is a small business if its annual receipts are below \$38.5 million.<sup>117</sup> The Bureau used AutoCount data for 2013 combined with public financial statements, securitization filings, and additional market research to estimate annual receipts for each of the potential larger participants.<sup>118</sup> Based on this review, it appears that few, if any, of the approximately 38 potential larger participants identified by the Bureau’s analysis meet the small business threshold classification.<sup>119</sup> The Bureau therefore estimates that no or very few small businesses would be classified as larger participants of the automobile financing market under the Proposed Rule.<sup>120</sup>

Finally, the proposed definition of the term financial product or service to include certain

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<sup>117</sup> 13 CFR 121.201 (NAICS code 522220) (as amended by 79 FR 33647, 33655 (June 12, 2014)). The Bureau believes that larger participants in the proposed nonbank automobile financing market are likely to be classified under NAICS code 522220, sales financing. NAICS lists “automobile financing” and “automobile finance leasing companies” as index entries corresponding to this code. See U.S. Census Bureau, North American Industry Classification System, *2012 NAICS Definition 522220 Sales Financing*, available at <http://www.census.gov/cgi-bin/sssd/naics/naicsrch>.

<sup>118</sup> To generate these estimates, the Bureau first calculated an estimate of the average stream of interest income the 38 potential larger participants would receive over a 12-month period for all loans originated in 2013, as well as the income each entity would receive during the same period for loans made in previous years if the number of originations were identical to 2013 levels. This initial calculation excludes leases that also generate income. It also assumes no prepayment, which would increase receipts; no defaults, which would decrease receipts; and no other income generated from any other sources. The Bureau then analyzed public financial statements to verify any potential outliers. Using this methodology, the Bureau found six potential larger participants with receipts from loans that fall below the \$38.5 million size standard in 2013; however, three of these entities hold a substantial number of leases and therefore likely have over \$38.5 million in combined receipts from loans and leases, assuming lease terms similar in payment size to loans. Further market research indicates the remaining three entities likely generate additional revenue from other sources, suggesting that their annual receipts also exceed the relevant size standard.

<sup>119</sup> The Bureau’s analysis concluding that few, if any, potential larger participants meet the relevant size standard is described in *supra* note 118. The Bureau also believes that it is unlikely that any small entities would be rendered larger participants of the consumer reporting or consumer debt collection markets by the proposed technical amendments to § 1090.104(a) and § 1090.105(a), since very few entities in those markets are likely to have annual receipts that are so close to the larger-participant threshold that inclusion of additional receipts from a formerly-affiliated company would affect their larger-participant status.

<sup>120</sup> According to the 2007 Economic Census, more than 2,000 small firms are encompassed under the most applicable NAICS code (522220). U.S. Census Bureau, American FactFinder Database, Estab and Firm Size: Summary Statistics by Revenue Size of Establishments for the United States: 2007, available at [http://factfinder2.census.gov/bkmk/table/1.0/en/ECN/2007\\_US/52SSSZ4//naics~522220](http://factfinder2.census.gov/bkmk/table/1.0/en/ECN/2007_US/52SSSZ4//naics~522220). Thus, even if a few small firms were classified as larger participants, they would constitute less than one percent of the small firms in the industry under that NAICS code.



automobile leases would have little impact on small nonbank entities engaged in automobile leasing. As mentioned above, the vast majority of automobile leases likely already qualify as a financial product or service under section 1002(15)(A)(ii) of the Dodd-Frank Act, and so the change in definition is unlikely to affect the larger-participant status of any small business. With respect to costs related to compliance, if the proposed definition is finalized, small nonbanks would have to comply with the UDAAP prohibition under section 1031 of the Dodd-Frank Act when providing automobile leases covered under the proposed definition. However, as with small banks, small nonbanks that provide automobile leases must already comply with similar UDAP prohibitions under section 5 of the FTC Act as well as the applicable enumerated consumer laws, such as the Consumer Leasing Act. Additionally, as explained above, there are likely to be few, if any, small nonbank businesses in the automobile financing market that would be subject to supervision irrespective of the proposed definition. To the extent that any small nonbanks are larger participants under the Proposed Rule, the Bureau believes that the proposed definition would expand the scope of leasing activities of such entities subject to supervision for compliance with section 1031. The economic impact of this expansion in scope would not be significant. Notably, even absent the proposed definition, all leasing activities of such entities would be subject to supervision by the Bureau for compliance with the enumerated consumer laws, including the Consumer Leasing Act.<sup>121</sup>

Considering the limited public information available for several of the smallest potential larger participants, the Bureau requests comment on the impact of the Proposed Rule on small

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<sup>121</sup> As noted above, with respect to the enumerated consumer laws, the scope of the Bureau's authority is defined by the scope of those laws, not by the activities listed under section 1002(15)(A) of the Dodd-Frank Act.

nonbank entities and solicits data that may be relevant to this analysis. The Bureau also solicits comments on whether NAICS code 522220 or any other NAICS code is more appropriate for this market.

Additionally, if a larger participant's annual receipts fell below the \$38.5 million SBA size standard, the Proposed Rule would not result in a "significant impact" on the entity. The Proposed Rule would not itself impose any business conduct obligations beyond those described above regarding the automobile leases defined under the Proposed Rule as financial products or services. Furthermore, the Bureau's supervisory activity would have very little economic impact on a supervised entity. When and how often the Bureau would in fact engage in supervisory activity, such as an examination, with respect to a larger participant (and, if so, the extent of such activity) would depend on a number of considerations, including the Bureau's allocation of resources and the application of the statutory factors set forth in section 1024(b)(2) of the Dodd-Frank Act. Given the Bureau's finite supervisory resources, and the range of industries over which it has supervisory responsibility for consumer financial protection, when and how often a given a larger participant would be supervised is uncertain. Moreover, if supervisory activity occurred, the costs that would result from such activity are expected to be minimal in relation to the overall activities of a larger participant.<sup>122</sup> Hence, the Proposed Rule would not have a significant economic impact on a substantial number of small entities because the Proposed Rule would not impose any significant business conduct obligations on the defined class of larger

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<sup>122</sup> As noted in part VI.B.2.b above, the Bureau estimates that the cost of participation in an examination would be approximately 0.013 percent of the annual revenue generated from originations for an entity at the threshold of 10,000 aggregate annual originations.

participants and the cost of supervisory activities would be nominal in relation to the revenue of a larger participant whose annual revenue fell below the \$38.5 million SBA size standard.<sup>123</sup>

Finally, section 1024(e) of the Dodd-Frank Act authorizes the Bureau to supervise service providers to nonbank covered persons encompassed by section 1024(a)(1), which includes larger participants. Because the Proposed Rule does not specifically address service providers, effects on service providers need not be discussed for purposes of this RFA analysis. Even were such effects relevant, the Bureau believes that it would be very unlikely that any supervisory activities with respect to the service providers to the approximately 38 potential larger participants of the proposed market for automobile financing would result in a significant economic impact on a substantial number of small entities.<sup>124</sup>

Accordingly, the undersigned certifies that the Proposed Rule would not have a significant economic impact on a substantial number of small entities.

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<sup>123</sup> Because the Proposed Rule aggregates the activities of affiliated companies in part by adding together annual originations, two companies that are small businesses might, together, have aggregate annual originations over 10,000. The Bureau anticipates no more than a very few such cases, if any, in the automobile financing market.

<sup>124</sup> As noted above, according to the 2007 Economic Census, more than 2,000 small firms are encompassed under NAICS code 522220, and the number of those firms that are service providers for the 38 potential larger participants will be only a small fraction of that number. Other service providers may be classified under NAICS code 522320 for financial transactions processing, reserve, and clearing house activities, which also includes more than 2,000 small firms. U.S. Census Bureau, American FactFinder Database, Estab and Firm Size: Summary Statistics by Revenue Size of Establishments for the United States: 2007, *available at* [http://factfinder2.census.gov/bkmk/table/1.0/en/ECN/2007\\_US/52SSSZ4//naics~522320](http://factfinder2.census.gov/bkmk/table/1.0/en/ECN/2007_US/52SSSZ4//naics~522320). Still other service providers are likely to be considered in other NAICS codes corresponding to the service provider's primary business activities. As noted above with respect to larger participants themselves, the frequency and duration of examinations that would be conducted at any particular service provider would depend on a variety of factors. However, it is implausible that in any given year the Bureau would conduct examinations of a substantial number of the more than 4,000 small firms in NAICS code 522220 and 522320, or the small firm service providers that happen to be in any other NAICS code. Moreover, the impact of supervisory activities, including examinations, at such small firm service providers can be expected to be less, given the Bureau's exercise of its discretion in supervision, than at the larger participants themselves.

## **VIII. Paperwork Reduction Act**

The Bureau has determined that this Proposed Rule would not impose any new recordkeeping, reporting, or disclosure requirements on covered entities or members of the public that would constitute collections of information requiring approval under the Paperwork Reduction Act, 44 U.S.C. 3501, *et seq.*

### **List of Subjects in 12 CFR Part 1000, 12 CFR Part 1090**

Consumer protection, Credit.

### **Authority and Issuance**

For the reasons set forth in the preamble, the Bureau proposes to add 12 CFR part 1001 and amend 12 CFR part 1090, subpart B, to read as follows:

### **PART 1001—FINANCIAL PRODUCTS OR SERVICES**

Sec.

1001.1 Authority and purpose.

1001.2 Definitions.

1. The authority citation for part 1001 is to read:

**Authority:** 12 U.S.C. 5481(15)(A)(xi); and 12 U.S.C. 5512(b)(1).

2. Add a new part 1001 to Chapter X in Title 12 of the Code of Federal Regulations to read as follows:

#### **Part 1001—Financial Products or Services.**

##### **§ 1001.1 Authority and purpose.**

Under 12 U.S.C. 5481(15)(A)(xi), the Bureau is authorized to define certain financial products or services for purposes of title X of the Dodd-Frank Act, Public Law 111-203, 124

Stat. 1376 (2010) (Title X) in addition to those defined in 12 U.S.C. 5481(15)(A)(i)-(x). The purpose of this part is to implement that authority.

**§ 1001.2 Definitions.**

Except as otherwise provided in Title X, in addition to the definitions set forth in 12 U.S.C. 5481(15)(A)(i)-(x), the term “financial product or service” means, for purposes of Title X:

(a) extending or brokering leases of an automobile, as defined by 12 CFR 1090.108(a), where the lease:

(1) qualifies as a full-payout lease and a net lease, as provided by 12 CFR 23.3(a), and has an initial term of not less than 90 days, as provided by 12 CFR 23.11; and

(2) is not a financial product or service under 12 U.S.C. 5481(15)(A)(ii).

**PART 1090—DEFINING LARGER PARTICIPANTS OF CERTAIN CONSUMER FINANCIAL PRODUCT AND SERVICE MARKETS**

3. The authority citation for part 1090 continues to read as follows:

**Authority:** 12 U.S.C. 5514(a)(1)(B); 12 U.S.C. 5514(a)(2); 12 U.S.C. 5514(b)(7)(A); and 12 U.S.C. 5512(b)(1).

4. Section 1090.101 is amended by revising the definition of “*Nonbank covered person*” to read as follows:

**§ 1090.101 Definitions.**

\* \* \* \* \*

*Nonbank covered person* means, except for persons described in 12 U.S.C. 5515(a) and 5516(a):

(1) Any person that engages in offering or providing a consumer financial product or service; and

(2) Any affiliate of a person that engages in offering or providing a consumer financial product or service if such affiliate acts as a service provider to such person.

5. Section 1090.104 is amended by revising paragraph (a)(iii)(D) of the definition of “annual receipts” to read as follows:

**§ 1090.104 Consumer reporting market.**

(a) \* \* \*

(D) The annual receipts of a formerly affiliated company are not included if the affiliation ceased before the applicable period of measurement as set forth in paragraph (ii) of this definition. The annual receipts of a nonbank covered person and its formerly affiliated company are aggregated for the entire period of measurement if the affiliation ceased during the applicable period of measurement as set forth in paragraph (ii) of this definition.

6. Section 1090.105 is amended by revising paragraph (a)(iii)(D) of the definition of “annual receipts” to read as follows:

**§ 1090.105 Consumer debt collection market.**

(a) \* \* \*

(D) The annual receipts of a formerly affiliated company are not included if the affiliation ceased before the applicable period of measurement as set forth in paragraph (ii) of this definition. The annual receipts of a nonbank covered person and its formerly affiliated company are aggregated for the entire period of measurement if the affiliation ceased during the applicable period of measurement as set forth in paragraph (ii) of this definition.

7. Add a new § 1090.108 to subpart B to read as follows:

**§ 1090.108 Automobile financing market.**

(a) *Market-related definitions.* As used in this section:

*Aggregate annual originations* means the sum of the number of annual originations of a nonbank covered person and the number of annual originations of each of the nonbank covered person's affiliated companies, calculated as follows:

(i) *Annual Originations.*

(A) Annual originations means the sum of the following transactions for the preceding calendar year:

- (1) Credit granted for the purpose of purchasing an automobile;
- (2) Automobile leases;
- (3) Refinancings of obligations described in (1) above, and any subsequent refinancings thereof; and
- (4) Purchases or acquisitions of obligations described in (1) or (3) above or of automobile lease agreements.

(B) The term annual originations does not include investments in asset-backed securities.

(ii) *Aggregating the annual originations of affiliated companies.* The annual originations of a nonbank covered person must be aggregated with the annual originations of any person (other than an entity described in paragraph (c)) that was an affiliated company of the nonbank covered person at any time during the preceding calendar year. The annual originations of a nonbank covered person and its affiliated companies are aggregated for the entire preceding calendar year, even if the affiliation did not exist for the entire calendar year.

*Automobile* means any self-propelled vehicle primarily used for personal, family, or household purposes for on-road transportation. The term does not include motor homes, recreational vehicles (RVs), golf carts, and motor scooters.

*Automobile financing* means providing the transactions identified under the term “annual originations” as defined in this section.

*Automobile lease* means a lease that is for the use of an automobile, as defined in this section, and that meets the requirements of 12 U.S.C. 5481(15)(A)(ii) or 12 CFR 1001.2(a).

*Refinancing* has the same meaning as in 12 CFR 1026.20(a), except that the nonbank covered person need not be the original creditor or a holder or servicer of the original obligation.

(b) *Test to define larger participants.* Except as provided in paragraph (c), a nonbank covered person that engages in automobile financing is a larger participant of the automobile financing market if the person has at least 10,000 aggregate annual originations.

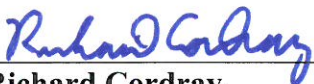
(c) *Exclusion for dealers.* The following entities do not qualify as larger participants under this section:

- (1) persons excluded from the authority of the Bureau by 12 U.S.C. 5519; and
- (2) persons who meet the definition in 12 U.S.C. 5519(f)(2); are identified in 12 U.S.C. 5519(b)(2); and are predominantly engaged in the sale and servicing of motor vehicles, the leasing and servicing of motor vehicles, or both.



[THIS SIGNATURE PAGE PERTAINS TO THE PROPOSED RULE ENTITLED,  
“DEFINING LARGER PARTICIPANTS OF THE AUTOMOBILE FINANCING  
MARKET AND DEFINING CERTAIN AUTOMOBILE LEASING ACTIVITY AS A  
FINANCIAL PRODUCT OR SERVICE”]

Dated: September 16, 2014.

  
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Richard Cordray,

*Director, Bureau of Consumer Financial Protection.*