

F&I BEST PRACTICES GUIDE

Risk-Based Pricing Rule & Safe-Harbor Privacy Notices

Developed by:

David Robertson, MBA

Executive Director

Association of Finance & Insurance Professionals

Reviewed by:

Jean Noonan, Esq.

Hudson Cook

January 2011



F&I BEST PRACTICES GUIDE

Risk-Based Pricing Rule & Safe-Harbor Privacy Notices

Introduction

The announcement of a new federal, state or local regulation triggers a multi-level and multifaceted review process to determine whether it applies to the retail automobile industry and, if so, to assess the law's impact on the in-store activities it regulates and those the law is intended to benefit. AFIP looks to NADA, state and regional dealer associations, and other industry-specific associations for direction regarding the industry's stance relative to the new rules. In addition, as with this guide, AFIP engages the law firm of Hudson Cook to ensure that its training material and best practices information satisfy both the letter and spirit of the law. Please note that the practices discussed herein are limited to in-dealership-initiated finance and insurance activities.

In addition to its distribution as a standalone document, this material will be available on the AFIP website, integrated into the AFIP Certification Program curriculum, and included in its comprehensive final exam.

AFIP Disclaimer

The information herein is not legal advice, nor should it be construed as such. The readers of this material are advised to seek qualified legal counsel regarding the regulations addressed herein and the applicability of the corresponding best practices as they apply to the unique operational environments in which they will be implemented.

Hudson Cook Reviewer's Disclaimer

Nothing in these materials should be considered as rendering legal advice for specific cases. Please seek appropriate assistance from qualified legal counsel.

Risk-Based Pricing Rule

Overview

The federal government enacted the Risk-Based Pricing Rule to improve consumer awareness of the impact of one's creditworthiness, not only on the availability of credit (as with the adverse action notice when credit is denied), but also on the cost of borrowing if credit is granted. The 2003 FACT Act amendments to the Fair Credit Reporting Act directed the Federal Trade Commission and the Federal Reserve Board to better inform consumers of how their creditworthiness affects their cost of credit. Effective January 1, 2011, the Risk-Based Pricing Rule requires dealers who use credit reports to provide an informational notice to credit applicants. The Rule offers dealers two compliance options.

- (1) Dealers can provide a risk-based pricing notice to a customer who applies for financing if, based on a credit report, the contract annual percentage rate for that customer is less favorable than the APR for a "substantial portion" of its other customers; or
- (2) Dealers can provide a credit score exception notice to every customer who applies for credit.

NOTE: *The F&I best practices addressed below are based on the NADA-negotiated credit score exception notice (option 2 above). Dealers electing to implement risk-based pricing notices (option 1 above) should contact AFIP for additional information.*

The best practices set forth below are based on the assumption that the dealer has secured, either from a form provider or credit portal, printed notices fully satisfying the notification requisites established by the Rule.

Best Practices for Issuing the Exception Notice

Dealers must issue exception notices to *all in-house-initiated installment sale customers effective January 1, 2011, in cases in which a credit history report has been obtained.*

- The exception notice must be given as soon as reasonably practicable after obtaining a credit score, **but always before the financing contract is signed.**
- If the request for credit is flatly denied, the exception notice need not be given. In such cases, an adverse action notice will be sent to the customer.
- If the credit is conditioned, such as by requiring a larger down payment or a shorter repayment period, the dealer may wait to give the exception notice until the customer accepts the conditional offer. If the customer does not accept the conditions, the dealer may give an adverse action notice instead of an exception notice.

If the credit score, elements of the deal, or response from one or more funding sources indicates that the request will be granted "as agreed" with no qualifications, then the exception notice should be issued promptly, but always before the customer signs the installment sale contract.

In the case of joint credit applications, in which credit reports are obtained for more than one party (co-buyers), *each individual for whom a credit score is obtained must receive an exception notice listing only the credit score for that individual.*

In cases in which more than one credit score is obtained for a consumer, *the exception notice must reflect the credit score on which the credit acceptance decision is based.*

In cases in which more than one lender has approved the transaction, *the exception notice issued must reflect the credit score obtained by the funding source designated by the F&I person as the one to whom the installment sale agreement will be assigned.*

Proof of delivery to the customer should be established by having the customer initial or sign a copy of the notice retained in the deal jacket.

Dealers are only required to give the exception notice to customers approved for financing. Practical considerations, however, may cause a dealer to give the exception notice to all customers.

- Lease transactions: The Risk-Based Pricing Rule does not apply to leases. In some cases, the dealer may not know at the time it obtains the customer's credit score whether the financing will be a credit or lease transaction. The dealer may choose to give the exception notice to all customers as soon as the credit score is obtained to simplify compliance procedures.
- Counteroffers: When the credit offer is conditioned on terms the consumer did not request, the dealer may not immediately know whether the customer will accept the offer. If the customer does not accept the offer, the dealer must give an adverse action notice. When an adverse action notice is given, the dealer need not also give an exception notice. The dealer can either wait for the customer's decision or give the exception notice to all customers who receive a counteroffer as soon as the score is obtained to simplify compliance.
- California Best Practices: California law adds two additional requirements on dealers operating in California. We think it is likely that the California law is preempted by the federal law. Until this question is resolved for certain, California dealers may wish to take these additional steps required by state law.

(1) The credit score disclosure notice must be issued to customers for whom a credit score is obtained in conjunction with a consumer lease transaction (in addition to installment sale deals). In short, every customer for whom a credit history report is secured – with the exception of instances in which the request for credit is flatly denied – must receive a credit score disclosure notice.

(2) In cases in which credit scores are obtained for more than one credit reporting agency, additional credit score disclosure notices must be issued to the customer for each of the agencies issuing a credit score. For example, if three credit history reports are obtained – one from each credit-reporting agency – the customer must receive three credit score disclosure notices.

- Internet / Fax / Phone Customer Notice Procedures: Customers applying for credit on the internet, by fax, or by phone that require an exception notice should receive the notice via first-class mail at the home address listed on the credit application. A short memo accompanying the form will explain that the dealer, in compliance with the Risk-Based Pricing Rule, has sent an exception notice to the customer at the address listed on the credit application – and that this constitutes delivery of the notice. It will also state that a copy of the notice will be retained by the selling dealer.

If the transaction is conducted by phone, the text of the notice will be read to the customer in addition to sending a copy by US mail.

As with the in-person notices, it must be given to the customer before the agreement is disclosed.

Responding to General Inquiries

F&I personnel must be equipped to respond to customer inquiries stemming from the information contained in the notice.

When a customer inquires about the purpose of the exception notice, they should be told: "The credit score disclosure notice is mandated by the Risk-Based Pricing Rule. A federal government initiative, the rule is designed to make consumers aware of the fact that their creditworthiness, as indicated by their credit score, may impact their cost of credit. The program employed by this dealership requires that all installment sale customers receive a credit score disclosure notice, regardless of their credit score."

Regardless of the template used, the F&I manager must be able to help the customer locate:

- His or her credit score.
- The ranking of that score relative to the U.S. population.
- Where the customer can obtain additional information about his or her credit score.

Additional inquiries may be addressed by providing the customer with one of the two explanation sheets provided by AFIP (included herein as Credit Score Disclosure Notice Supplements 1 and 2). It is recommended that they not be issued unless the customer, after being directed to applicable sections of the notice, still has additional questions.

In most cases, with the F&I manager's help identifying the relevant sections, the information provided by the notice and the AFIP explanation sheets will lay the matter to rest. If further explanations or information are required, the F&I manager should direct the customer to the inquiry addresses provided on the notice(s).

All responses to customers about the contents of the form should be on point and direct.

DO NOT UNDER ANY CIRCUMSTANCES:

- Make any attempt to determine or relate how the customer's credit score impacted his or her cost of credit.
- Draw comparisons about how the customer might have fared had he or she qualified at a higher tier or with more money down, etc. You did not make the risk-based pricing decision. You DO NOT have the authority to respond to such inquiries.
- State or infer that the customer received "the best rate" available. You have no way of knowing what the customer's best rate might be.
- Engage in any discussions with customers as to how they might improve their credit score. You do not have sufficient information to make accurate assessments of individual situations, nor are you trained to perform such services. Give the customer a copy of the credit score disclosure notice explanation form, which along with the information found in the exception notice itself, will direct the customer to those qualified to provide such assistance.

DO emphasize that the form is only issued to those whose credit has been accepted by one or more funding sources.

Issued in Accordance with the

Risk-Based Pricing Rule Consumer Education Program

The Risk-Based Pricing Rule is a government mandate to make consumers more aware of how their creditworthiness impacts the cost of borrowing.

Under the Rule, if a consumer applies for credit, that consumer must be notified of his or her current credit score and its ranking in comparison to the general U.S. population. The method employed by this dealership requires that all credit customers be notified of their score, regardless of their credit ranking.

Your credit score places you in the upper 40 percentile of all Americans and, as such, this notice is for informational purposes only. Congratulations on your high ranking.

Consult the exception notice for additional information.

Each customer who requests more information about the credit score disclosure notice will be given one of two (but not both) credit score disclosure notice supplements.

Credit Score Disclosure Notice Supplement 1

Information Provided by



Issued in Accordance with the

Risk-Based Pricing Rule Consumer Education Program

The Risk-Based Pricing Rule is a government mandate to make consumers more aware of how their creditworthiness impacts the cost of borrowing.

Under the Rule, if a consumer applies for credit, that consumer must be notified of his or her current credit score and its ranking in comparison to the general U.S. population. The method employed by this dealership requires that all credit customers be notified of their score, regardless of their credit ranking.

Your credit score places you in the upper 40 percentile of all Americans and, as such, this notice is for informational purposes only. Congratulations on your high ranking.

Consult the exception notice for additional information.

Each customer who requests more information about the credit score disclosure notice will be given one of two (but not both) credit score disclosure notice supplements.

Credit Score Disclosure Notice Supplement 1

Information Provided by



Issued in Accordance with the

Risk-Based Pricing Rule Consumer Education Program

Your request for funding has been accepted by one or more sources – in some cases, subject to certain terms and conditions.

The Risk-Based Pricing Rule is a government mandate to make consumers more aware of how their creditworthiness impacts the cost of borrowing.

Under the Rule, if a consumer applies for credit, that consumer must be notified of his or her credit score and its ranking in comparison to the general U.S. population in cases in which one or more funding sources has agreed to extend credit.

The exception notice provides your current credit score based on the scoring scale used by the credit bureau issuing the report. Because there is a direct correlation between the risk associated with extending credit and the cost of credit, any effort on your part to improve your credit score may result in lower borrowing costs.

Consult the exception notice for additional information.

See reverse for the six components of your credit score.

Each customer who requests more information about the credit score disclosure notice will be given one of two (but not both) credit score disclosure notice supplements.

Credit Score Disclosure Notice Supplement 2

Information Provided by



Issued in Accordance with the

Risk-Based Pricing Rule Consumer Education Program

Your request for funding has been accepted by one or more sources – in some cases, subject to certain terms and conditions.

The Risk-Based Pricing Rule is a government mandate to make consumers more aware of how their creditworthiness impacts the cost of borrowing.

Under the Rule, if a consumer applies for credit, that consumer must be notified of his or her credit score and its ranking in comparison to the general U.S. population in cases in which one or more funding sources has agreed to extend credit.

The exception notice provides your current credit score based on the scoring scale used by the credit bureau issuing the report. Because there is a direct correlation between the risk associated with extending credit and the cost of credit, any effort on your part to improve your credit score may result in lower borrowing costs.

Consult the exception notice for additional information.

See reverse for the six components of your credit score.

Each customer who requests more information about the credit score disclosure notice will be given one of two (but not both) credit score disclosure notice supplements.

Credit Score Disclosure Notice Supplement 2

Information Provided by



How Credit Scores Are Calculated

Your credit score is influenced by several factors. While the scoring models for each credit bureau will vary, there are six primary elements that each bureau will evaluate.

- 1) **Payment history** (does the borrower have a history of consistently paying accounts on time and in full?)
- 2) **Available credit** (how much credit is currently available to the borrower?)
- 3) **Credit utilization** (how much of the credit available to the borrower is currently being used?)
- 4) **Credit balances** (what is the total of both current and delinquent account balances?)
- 5) **Length and types of credit history** (how long has the borrower's credit history and what types of credit has s/he had?)
- 6) **Recent credit** (how many credit accounts has the borrower opened recently and how many recent inquiries have been made about the customer's credit?)

Provided for informational purposes only.

How Credit Scores Are Calculated

Your credit score is influenced by several factors. While the scoring models for each credit bureau will vary, there are six primary elements that each bureau will evaluate.

- 1) **Payment history** (does the borrower have a history of consistently paying accounts on time and in full?)
- 2) **Available credit** (how much credit is currently available to the borrower?)
- 3) **Credit utilization** (how much of the credit available to the borrower is currently being used?)
- 4) **Credit balances** (what is the total of both current and delinquent account balances?)
- 5) **Length and types of credit history** (how long has the borrower's credit history and what types of credit has s/he had?)
- 6) **Recent credit** (how many credit accounts has the borrower opened recently and how many recent inquiries have been made about the customer's credit?)

Provided for informational purposes only.

Safe Harbor Privacy Notice

Overview

F&I personnel have been issuing the initial privacy notice to installment sale and consumer lease customers during the deal-consummation process for the better part of a decade. Under the authority of the Gramm-Leach-Bliley Act, customers are to be informed about how the dealer, acting as the creditor, uses the customer's nonpublic personal information. In certain cases in which the information is shared with a non-affiliated third party, usually for marketing purposes, the customer has the right to "opt out" – deny the dealership permission to share his or her information with specific types of third parties.

In December of 2009, the Gramm-Leach-Bliley Act was amended and new model privacy notice forms became available. The new forms provide "safe-harbor" protection if they are properly constructed and implemented. Effective December 31, 2010, the original sample clauses will no longer enjoy safe-harbor protection.

A safe harbor is not a statutory provision, but rather a legal construct providing the basis for a defense against challenges emanating from the application of a particular rule or regulation. However, the safe-harbor protection only applies if the law in question has been properly interpreted, implemented and applied.

In the case of the privacy notice, the government has provided a set of sample forms allowing dealers to select the one that best meets their needs – as well as strict guidelines about how the forms can be modified and applied to real-world situations.

NOTE: *The selection and final construction of the new privacy notices are beyond the purview of the F&I department. The practices below are based on the assumption that the dealer has elected to employ the privacy notice in sync with his or her organizational structure and method of operation – and that the parameters of the notice have been properly documented and conveyed to those charged with their implementation.*

Best Practices for Issuing Safe-Harbor Privacy Notices

If a dealership has not already adopted the revised model policy notices, it should do so right away. Beginning in January 2010, only the new model forms enjoy safe-harbor protection.

The circumstances under which the privacy notice forms are issued have not changed. In those situations in which a credit application has been obtained and submitted for approval to a credit portal – or one or more prospective lenders or lessors – the customer must be issued a privacy notice.

Caution is required when issuing the new notices because the safe-harbor protection only applies if they are properly used. It is important that the model forms be completed by qualified legal counsel in consultation with business executives in strict compliance with the instructions and that they accurately reflect the dealer's information-sharing practices.

DO NOT UNDER ANY CIRCUMSTANCES:

- Take any action relative to the new privacy notice unless you have been given clear, simple instructions on the customers who must receive it, have received the proper training, and are fully cognizant of how the notice is to be applied to the full complement of real-world applications.
- Fail to issue the notice to those customers who are to receive it.
- If dealer policy dictates, fail to place a copy of the privacy notice signed by the customer in the deal jacket.

Properly Applying Best Practices

The concept of best practices entails the identification and application of the most efficient and effective methods for applying governmental, regulatory agency, lender and vendor, and dealership policies to actual job situations.

About AFIP

The Association of Finance & Insurance Professionals is the sanctioning body for the F&I trade. AFIP sets the standard for technical competence and ethical conduct by certifying in-dealership financial services personnel and the field representatives of the lenders, vendors and agents who service the F&I function. Additionally, AFIP provides a host of compliance and best practices products. For more information on the AFIP Certification Program or other AFIP compliance products, go to www.afip.com.

SPECIAL NOTICE TO F&I PRACTITIONERS

The AFIP Certification Program provides exposure to the state and federal regulations governing the F&I process. Equally important, the individual covenants found within the documents used to establish legally binding agreements with lenders and vendors offer specific guidance as to their limitations and performance expectations. Knowledge is the key to compliance – always read and fully understand the key provisions of the documents you are asking customers to sign.

The two customer notice forms contained on pages 7 - 10 can be obtained as standalone documents (for easier printing) at www.afip.com/downloads.htm.

You Can't Get Rich in F&I Unless You're Smart

And you aren't smart unless you know the rules... The AFIP Certification Program makes sure you know how to apply state and federal regulations and enforces a professional code of ethics. Self-study materials and local testing means no time away from the store.

"If you order today, my manager says he'll knock \$320 off the price of the course."
(Details below)



Order now at
proshop.afip.com

~~\$870~~ \$550*

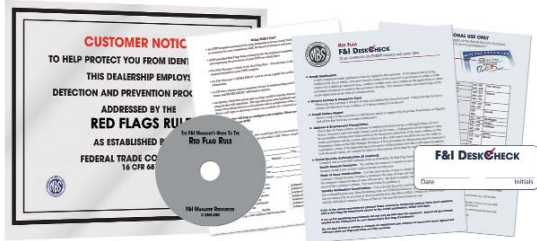
*per person with the coupon code "bestpractices"

*Plus S&H and applicable taxes



Stop ID Theft with These Tools From AFIP

DealerAide



+1 Hour Personnel Orientation Session

DealerAide: Red Flags Rule

- Turnkey solution comes with everything you need to have a written Red Flags program in two weeks or less.
- Fill out a five-step form and receive a customized template.
- Minimal disruption to established systems.
- Comes with a one-hour orientation, one ID theft prevention sign, and F&I desk check card and stickers.

Only ~~\$250~~ \$175* per dealership with coupon code **"bestpractices"**

Safeguards Rule Compliance Kit

- Comes with everything you need to write and implement your program.
- Fully customizable.
- Minimal disruption to established systems.
- Comes with secure document area signs and stickers, organizational binder, an orientation video and one free training session for the corporate compliance officer.
- Most popular Safeguards program solution on the market.



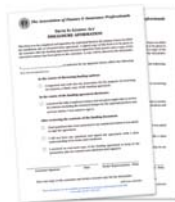
Only ~~\$495~~ \$350* per dealership with coupon code **"bestpractices"**

Need Compliance Supplies?

Secure Document Area Signs \$6.00* ea.

TILA forms \$30.00* per 100

Red Flags Rule signs \$25.95*ea.



Order now at [proshop.afip.com!](http://proshop.afip.com)

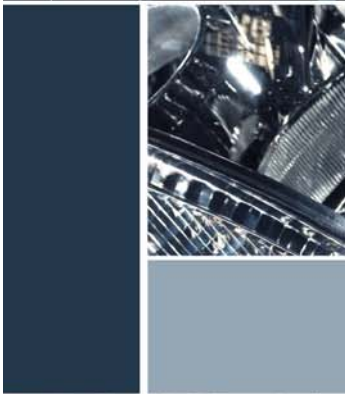
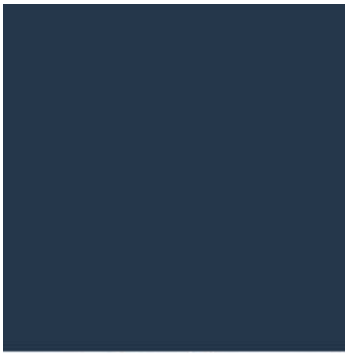
* Plus S&H and tax where applicable. Each store must have their own DealerAide or Safeguards Kit.

www.afip.com

info@afip.com

817.428.2434

All Safeguards and Red Flags Rule products created by Members Benefits Services, Inc. Marketed by AFIP.



Association of Finance & Insurance Professionals
5100 Thompson Terrace, Suite B • Colleyville, Texas 76034
817.428.2434 • info@afip.com • www.afip.com