

# CHARAPP & WEISS, LLP

DRIVING YOUR SUCCESS

## A TILA Primer

During 2011, you will be hearing a lot about the Dodd-Frank Act. Even though dealers are exempt from the direct jurisdiction of the Consumer Financial Protection Bureau that is created by the Act, it still completely revamps federal regulation of the country's financial system. As the Act's provisions go into effect, dealers will regularly learn of the new obligations for which they will be responsible.

One section that can have a dramatic impact on your business is the expansion of the jurisdiction of the Truth in Lending Act. Since its original passage decades ago, the Truth in Lending Act only applied to transactions in which the amount financed was \$25,000 or less. That covered almost all vehicles financed when TILA was passed. In recent years, with the steadily increasing prices of vehicles, most luxury vehicles and even many midsized vehicles were exempt from the Act for a consumer who wished to bring a legal action involving a vehicle financed for more than \$25,000. With the enactment of the Dodd-Frank Act, TILA's maximum jurisdiction has now been increased to \$50,000, and the law will once again cover most vehicles financed.

Since TILA may be reinvigorated as a basis for lawsuits against dealers, it is a good time for a dealership to review its practices in the F&I department to avoid TILA claims. Here is a quick primer on TILA Dos and Don'ts.

**DO give the customer a copy of the Retail Installment Sale Contract once it is signed.**

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**A TILA PRIMER I**

Regulations under TILA, known as Regulation Z, make clear that the dealer must give the customer a copy of the contract to keep at the time the customer becomes obligated – that is when the customer signs the retail installment sale contract.

**DO provide a copy of the unsigned RISC if the customer changes his or her mind in F&I, won't sign and requests a copy.**

The purpose of TILA is complete disclosure of material credit terms so that, among other things, consumers can meaningfully shop for credit. If consumers cannot have a copy of the unsigned document if they choose not to complete an installment sale, then they cannot meaningfully shop for credit. If a customer decides to not complete a transaction and asks for a copy of the RISC, a copy should be provided, either from the multi-copy pack or by means of a machine made copy.

**DO have a process to protect against packing claims.**

Packing is a claim generally made by plaintiffs' attorneys when they cannot point to any other

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specific wrongdoing under TILA. A packing claim is generally based upon oral misrepresentations allegedly made to the customer. Packing has numerous definitions, but generally it is misleading the customer as to the monthly payment for the vehicle so that the dealership can sell additional products and services without adequate disclosure of their sale. Use a process that you can point to if a customer makes a claim that the products and services included in the RISC were not voluntarily purchased.



employee intentionally obscured a portion of the disclosures.

▪Do use a menu.

### **DO make sure that the menu You use enhances compliance.**

A properly constructed menu must do some specific things to help protect your dealership.

- Do show the monthly payment for the vehicle alone to show that the customer understood the monthly payment without additional products and services.
- Do show the a la carte price of each product in addition to package prices to avoid a claim that the customer purchased a package unaware that products could be bought individually. Many dealerships

use menus offering packages of products and services. This can be a valuable sales tool to make a presentation about the benefits of packages to customers. The problem is that somewhere on the menu the customer must be aware of the pricing of each product or service on an a la carte basis. The dealership does not want to face a claim from a customer that he or she purchased GAP and road hazard coverage along with the extended service contract because that was the only way the customer thought the service contract was available.

- Do get the menu signed and the choices initialed. When choices are initialed and the menu is signed, there is clear evidence that the customer saw the menu and made his or her own choices of products and services to buy.
- Do disclose prominently in the menu that purchases of additional products and services are not required for finance approval. If they are required, then they must be a part of the APR calculation; if they are not required and they are adequately disclosed, they can be sold without impact on the APR.

### **DON'T Pass Along Finance Source Fees.**

Fees to the finance source in connection with assignment of a retail installment sale contract, especially for subprime credit, are more prevalent than ever. If fees are passed along either directly or indirectly to the customer, TILA requires that they be considered part of the finance charge, increasing the APR for the transaction. If a dealer wishes to avoid having a fee treated as additional finance charge that increases the APR, a dealer must be careful that it does not pass

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along the fee directly or indirectly to the customer. How does a dealer show compliance?

Generally by avoiding the traps that lead to liability.

- **Don't** demand that the customer pay the fee.
- **Don't** add the fee to the buyers order as a fee passed along to the customer.
- **Don't** increase the price of the vehicle sold to make up for the fee because the price increase may be deemed to be an additional finance charge. Vehicles sold to customers for whom fees will be demanded must be priced at a level that will allow the dealer to make money while absorbing the fee as part of its overhead.
- **Don't** tell the customer that he or she would have paid less if the dealership did not have to pay fees to the finance source.
- **Don't** increase the price of an advertised vehicle at the time of sale to cover a fee. If a vehicle is advertised, and you cannot afford to absorb the fee, sell a vehicle with a higher profit margin.
- **Don't** increase the price shown on a vehicle, either the MSRP shown on the Monroney sticker for a new car or the asking price displayed on a used car, to offset the fee.
- **Don't** raise the price of a delivered vehicle. If you are unable to get the customer financed

at standard rates and you rewrite the finance contract with a subprime credit company, do not charge a higher transaction price. If you cannot sell the vehicle at the price delivered for standard financing, rescind the transaction and sell the customer another car.

### **DO have a Policy About Processing Fees and Charges.**

When a vehicle is sold, only the processing fee or charge allowed by state law should be charged. Fees such as a federal regulation compliance fee, a customer initiation fee, a warranty registration fee and any of a host of other ingeniously named charges should not be added upon sale of a vehicle. Most states – and that includes Virginia, Maryland and Pennsylvania – provide a “safe harbor” for dealers by specifically providing for processing fees or charges and detailing how the charges can be assessed. Those state statutes should be followed strictly.

### **DO make sure that your customer understands the finance approval process.**

Despite computer portals where approvals can sometimes be quickly and easily obtained, dealers still must spot deliver many vehicles subject to final finance approval by an assignee. There should be no misunderstanding of the nature of a customer's approval when he or she drives off the lot in a newly purchased vehicle. One of the most prevalent claims that dealers face from disappointed buyers who must return spotted vehicles is that they thought they had a completed deal. Customers should understand that final credit approval will require acceptance by the credit source.

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- **Don't** tell a customer that the deal has been finally approved unless it is true.
- **Don't** mislead a customer about the fact that the retail installment sale contract will be assigned.
- **Don't** mislead the customer about the possibility that further information may be demanded by a potential assignee and the customer's need to cooperate to obtain assignee approval.
- **Don't** mislead a customer as to the identity of potential assignee.

### **DO be careful with Promissory Notes.**

Don't use a promissory note form that triggers TILA coverage. In general, the provisions of the Truth in Lending Act and Regulation Z apply to an offer or extension of credit when four conditions are met:

1. The credit is offered or extended to consumers;
2. The offering or extension of credit is done regularly;
3. The credit is subject to a finance charge or payable by a written agreement in more than four installments; and
4. The credit is primarily for personal, family or household purposes.

Subject to notable exceptions, dealers generally meet conditions 1, 2, and 4 to coverage by TILA of the extension of credit under TILA because they regularly do business with consumers who purchase vehicles on credit for personal, family or household purposes. Often, dealers will take promissory notes for down payments or to cover bad checks. Dealers will also take "one shot" notes pending the completion of the customer's financing, either by the dealer or another creditor. Dealers must understand that once interest is charged or the note is for more than four installments, the third



requirement for application of the Truth in Lending Act is met. Here are some examples:

- The dealer decides to charge interest on a note that is taken for a down payment.
- The customer provides a bad check. The customer gives the dealer a note to pay off the check in six monthly installments without interest.
- The dealer decides to charge a "fee" for allowing the customer to provide a down payment note or a "one shot" note.

In each of these transactions, the dealer has extended credit subject to TILA. It is unlikely F & I personnel will give the necessary TILA disclosures in any of these circumstances. The F & I personnel probably don't even have the ability to make the disclosures.

For these reasons, dealers who use notes must be very careful.

- **Don't** charge interest.
- **Don't** charge a "fee" that can be construed as a finance charge for the extension of the credit.
- **Don't** extend credit that is payable in more than four installments.