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Is Different Pricing for Non-Credit Products and Services Illegal Discrimination? Yes, Says the CFPB, Massachusetts, and the FTC

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The Consumer Financial Protection Bureau made news this year when it announced that it considered discrimination to be illegal as an "unfair" practice, including in situations where fair lending laws do not apply. In March, the CFPB announced changes to its Examination Manual and said it would expand its anti-discrimination efforts to combat discrimination "across the board." But this is not just a CFPB theory. In a new kind of "Me Too" movement, enforcement agencies are lining up to join in.

CFPB

Few would maintain that intentionally charging minorities more for products based on their race or national origin is a good policy. In fact, there are probably federal and state civil rights laws that would prohibit this practice. But the CFPB's pronouncement raises many troubling issues. The first is whether this pronouncement is a proper use of the CFPB's authority. A close second, and one that the CFPB also committed to pursuing, is challenging *unintentional* discrimination under a disparate impact theory, which has no equivalent in unfairness law.

The U.S. Chamber of Commerce and other business and banking trade associations recently sued the CFPB in federal court, arguing that it exceeded its statutory authority under the Dodd-Frank Act and violated federal law by not following the procedural rulemaking requirements of the Administrative Procedures Act. For good measure, the case also challenged the CFPB's funding structure, which does not require congressional appropriations. This litigation will—at the very least—be a thorn in the CFPB's side as it tries to challenge alleged discrimination as an unfair practice.

Not long after the Chamber filed its challenge to the CFPB's pronouncement on discrimination as unfair, the U.S. Court of Appeals for the Fifth Circuit held, in another case, that the CFPB's funding scheme in Dodd-Frank is unconstitutional. This momentous decision threatens to undo everything the CFPB has done in its 11-year history. At the very least, it calls into question every action the agency now has underway. This decision is hot off the press. While speculation about its significance is running wild, no clear answer has emerged.

Massachusetts

These legal arguments have not deterred the Commonwealth of Massachusetts. Massachusetts Attorney General Maura Healey has now made intentional price discrimination the centerpiece of a new lawsuit against a dealership. *Spot Delivery* readers will recall our articles in the April 2022 issue in which we raised the specter of the CFPB challenging discretionary pricing of voluntary protection products if the average amounts paid by minorities and other protected groups were not the same as the average amounts paid by non-protected groups. Could challenges to differences in prices paid for vehicles be far behind?

In her lawsuit, the AG alleged that a franchised dealer earned higher profits from Hispanic and Black customers who bought VPPs, such as service contracts, paint protection, and GAP waivers, than it earned from White customers. The complaint alleged specifically that the dealership earned on average about $500 and $400 more in profits from Black and Hispanic customers, respectively, than from White customers. It also claimed that the percentage of profit margin was higher for these minority groups.

Although these allegations are potentially troubling, it is difficult to assess the strength of these charges from the complaint. The claims seem to fall short of making out a case of intentional discrimination against minorities. Here are some important questions:

- **Are the data based on apples-to-apples comparisons?** For example, what if Black or Hispanic customers selected more VPPs than Whites, on average, or chose more expensive products? Even one more purchased product, on average, could easily account for the differences alleged in the complaint. Massachusetts seems to recognize this problem because it also alleges that the dealership earns more profit from a single product—service contracts—sold to minorities. The complaint also acknowledges that the wholesale price of products varies by the vehicle purchased. Were the wholesale prices of these service contracts about the same? We can't tell, nor can we tell if other VPPs had similar profit disparities.

- **Are the counts of Hispanics, Blacks, and Whites accurate?** The data points for minority groups don't matter if customers have not been accurately classified. Massachusetts used proxies to estimate the race and national origin of the dealership's customers, and the estimated numbers are extremely small. The review period was January 2016 through March 2018. During that entire period, the complaint says the "population size" for Blacks buying service contracts was 19 and for all VPPs was 30—or about one sale of a VPP to a Black customer a month! Even worse, the proxy methodology that Massachusetts used counts consumers in a group by adding up even small chances of being in the group. In short, we cannot tell if even a single one of these 19 or 30 "Black" consumers would identify as Black. This is just one of many problems with building a case on proxies.

- **Is there any evidence of intentional discrimination?** It seems not. The complaint uses pejorative language in its attempt to condemn common business practices, such as trying to earn a profit on things sold. In short, the complaint claims that the dealer *should have known* that allowing a discretionary pricing

> policy and paying commissions to managers for sales would have resulted in unfair and discriminatory pricing.

It is noteworthy that this spunky dealership did not settle the claims. The great majority of AG investigations in Massachusetts are resolved through an Assurance of Compliance. The progress of this case bears watching.

FTC

Not to be outdone, the FTC filed a settlement with a Maryland-based dealership group, alleging that it discriminated against Black and Latino customers and charged illegal "junk fees." The junk fee claim was based on an alleged practice of tacking on hundreds or thousands of dollars over advertised prices for certifying the car as a certified pre-owned vehicle or for inspecting or reconditioning a used car. The FTC alleged that sometimes the dealerships claimed that such additional fees were "required."

The complaint alleged that the dealership violated the Equal Credit Opportunity Act by charging Black and Latino customers higher rate spreads or "markups" than it charged non-Latino White customers. The dealership had adopted a policy that would have allowed employees to reduce or waive the standard markups only for documented reasons, which would have protected against a discrimination claim if the dealer had properly implemented the policy. The FTC claimed that the dealership did not follow its policy, which left the dealership with no legitimate, nondiscriminatory explanations for its average rate spread differences to different demographic groups. The FTC alleged that one creditor that took assignment of the dealership's contracts notified the dealership twice of statistically significant higher rate spreads charged to Black customers but that the dealership took no action to address these concerns.

The FTC also claimed that the dealership discriminated against Black and Latino customers by charging them extra fees for inspection, reconditioning, vehicle prep, and certification more often and in higher amounts than non-Latino White customers.

The claim relating to higher average rate spreads to minorities is nothing new as an alleged violation of the ECOA. But the ECOA applies only to discrimination in a credit transaction, and the alleged discrimination in charging higher fees for inspections and similar services is not credit-related. This is where the FTC broke new ground for that agency. It said that discrimination in both rate spreads—a credit fee—and the cost of inspections—a non-credit fee—was an unfair practice that violated Section 5 of the FTC Act.

Before we leave the FTC case, note that the Commission charged the owner and president of the dealer group, as well as the vice president, with the violations of the ECOA and the unfair and deceptive acts and practices. The complaint alleged that these individuals knew of the violations and had the authority to stop them, but the violations persisted.

The two Republican commissioners of the five-member FTC objected to holding the two executives personally liable. They also opposed the use of the UDAP authority for alleged discrimination. One of the two voted against the settlement, but the other voted in favor but dissented in part.

The FTC's complaint, majority statement, and press release in this matter make the conduct look like a clear, even egregious, case of bad conduct. This is not unique. All complaints and press releases make the companies sued look terrible.

On one hand, it is refreshing to read a description of facts that do not line up nicely with the frequently cherry-picked facts in the complaints and the often-overblown rhetoric of the press releases. On the other hand, these facts did not prevent the FTC from voting to accept the settlement by a 4-to-1 vote.

These dealerships and their executives did not get much love from the FTC for their willingness to settle the claims without a fight. They agreed to pay the FTC $3.38 million to be used for consumer redress. This amount is especially noteworthy because the Supreme Court has held that the FTC lacks the authority to obtain consumer redress for violations of Section 5 in situations like this! Further, the obligations of this settlement will remain with the companies and individuals for 20 years.

If there are only two takeaways for dealerships and their leaders from this settlement, here they are:

1. Robust compliance policies are important, but they will get you nothing without vigorous and continuing oversight of your implementation of them.

2. Handwringing over evidence that your dealerships are doing something of which you don't approve is not a compliance strategy. You must move swiftly and firmly to ensure the conduct stops and consider whether compensation to your customers is appropriate.

Be careful; it is dangerous out there!

Commonwealth of Massachusetts v. Jaffarian's Service, Inc., Mass. Super., Civil Action No. 2277CV00881 (filed September 15, 2022), and *Federal Trade Commission v. Passport Automotive Group, Inc.*, D. Md., Case No. 8:22-cv-02670-GLS (complaint and stipulated order filed October 18, 2022).

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