COMMENTS

Submitted electronically by the:

Center for Responsible Lending
National Council of La Raza

Americans for Financial Reform
Consumer Action
Consumers for Auto Reliability and Safety
NAACP
National Association of Consumer Advocates
National Consumer Law Center (on behalf of its low-income clients)
National Urban League
Public Citizen
U.S. PIRG

To the Federal Trade Commission
Regarding the
Auto Buyer Consumer Survey

Federal Register Docket No. 2016-00033

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The National Council of La Raza (NCLR), Center for Responsible Lending (CRL), Americans for Financial Reform (AFR), Consumer Action, Consumers for Auto Reliability and Safety (CARS), NAACP, National Association of Consumer Advocates (NACA), National Consumer Law Center (NCLC), National Urban League (NUL), Public Citizen, and U.S. PIRG submit the following comments regarding the Federal Trade Commission's (FTC) proposed survey of consumers who recently purchased an automobile and financed that purchase through a dealer.

I. Introduction

Cars are the most common nonfinancial asset held by American families, and for some families, their most significant asset. Cars have become a necessity for U.S households, with more than 85% of the U.S. workforce using an automobile to commute to work.[1] Car ownership is no longer a luxury but is a prerequisite to economic opportunity. The need for a car is particularly true for many low- and moderate-income families (LMI) and communities of color, who live or work beyond the reach of public transit systems.

[1] Brian McKenzie, U.S. Census Bureau, *Modes Less Traveled—Bicycling and Walking to Work in the United States: 2008-2012*, available at http://www.census.gov/hhes/commuting/files/2014/acs-25.pdf.

Given the role that cars play in the everyday lives of American families, we applaud the FTC for proposing a survey to explore issues around automobile purchases and financing. The issues raised in the FTC's and Consumer Financial Protection Bureau's (CFPB) 2011 Roundtables persist in auto financing today. Research and data have continued to illuminate potentially unfair and abusive conduct in the market. In-depth interviews will shed additional light on these abusive practices. Often, individuals are not aware they are being treated differently by dealers and lenders, and as such, interviews are a helpful tool to probe for information about a consumer's treatment and experience. This research will bolster efforts to understand the discrimination that communities of color experience and the ways that LMI families experience different treatment. This information should help further shape the map for enforcement and regulatory efforts.

However, we have concerns about the proposed methodology and the categories of questions the FTC plans to ask interview participants. These comments provide recommendations for how to improve the research methodology to shed more light on car financing issues, as well as what questions will be most relevant for understanding participants' experience in the auto lending market.

II. Survey Methodology

We understand and appreciate the FTC's desire to conduct a survey using a representative sample of car-buyers. However, we have concerns regarding the sample size and survey participant criteria outlined in the proposal. The following recommendations offer the FTC the best opportunity to gather perspectives from a diverse group of auto loan borrowers and ensure that the FTC captures information from underrepresented communities most affected by deceptive lending practices.

A. Sample Size

While we recognize there are limited resources for the survey, the proposed sample size is too small to capture information about the car purchase and financing experience from a demographic variety of borrowers. The proposal expresses a desire to include borrowers with a range of characteristics, including gender, race/ethnicity and credit scores. However the proposed sample size of 40 interviews is too small to adequately capture the experiences of borrowers who are historically disenfranchised by the system. For example, if the interviews were split evenly among prime and subprime borrowers, a pool of 20 prime borrowers would need to have appropriate representation of women, men, and all races/ethnicities. That is only 10 prime borrower females and 10 prime borrower males. Would the remaining division by race/ethnic group be done according to the size of the U.S. population? If so, that would result in 16% of the 10 interviewees, or 1-2 people, being Hispanic. That is an extraordinarily small number of respondents to capture the experiences of a community that has faced historical discrimination in this market.

By way of additional background on these discriminatory patterns, the CFPB and Department of Justice (DOJ) have entered into settlement agreements with a number of auto financers over the past year regarding interest rate markups that violated the Equal Credit Opportunity Act.[2] Specifically, the settlements describe allegations by which auto financers charged African-American and Latino borrowers higher interest rates than White borrowers with similar credit profiles. In order to effectively identify problems in the auto lending market, we recommend over-sampling demographics that traditionally face deceptive and illegal practices when purchasing or financing vehicles, particularly borrowers of color, LMI borrowers, and those with subprime credit scores. The FTC should not use 40 interviews as the floor with an option to add 40 more interviews; instead, the FTC should plan for a minimum of 80 interviews with an option to add more.

B. Follow-up Survey

In addition to the interviews, FTC should engage in a broader market study to confirm the issues that are raised in the exploratory interview phase. This written survey should have a much larger sample size that is more reflective of the entire car purchase market and can be used to confirm the attitudes and findings discovered in the interview phase. Such a survey would provide the FTC with statistically significant information about the issues plaguing the auto purchasing and financing markets and bolster enforcement and regulatory efforts.

C. "Buy here pay here" Dealers

"Buy here pay here" (BHPH) dealers are 10% of the car finance market but operate much differently from the traditional dealer model. This model is an important area to explore and one that is rife with abuse. However, given the significant difference in how BHPH operates, it merits its own survey. For instance, BHPH dealers do not sell the loan contracts to third parties, and as such have a different economic incentive than dealers who sell their loans. BHPH customers also traditionally have lower credit scores, meaning there is a chance for over-representation in the category of subprime borrowers.

BHPH should be removed from the 80 interview interviews sample, and the FTC should conduct 10-20 additional interviews exclusively with BHPH consumers. Questions corresponding to these borrowers should reflect the BHPH lending experience and business model and not be confused with the traditional dealer model.

III. Proposed Survey Questions

Below we suggest particular areas in which the FTC should focus its participant interview questions. Due to the well-documented abuses in auto financing, it is critical for the FTC to devote significant time to questions about this part of the process. In addition, we have included recommendations for specific question in the appendix to this comment.

A. Yo-Yo Scams

[2] http://www.consumerfinance.gov/newsroom/cfpb-and-doj-reach-resolution-with-toyota-motor-credit-to-address-loan-pricing-policies-with-discriminatory-effects/; and http://www.consumerfinance.gov/newsroom/cfpb-takes-action-against-fifth-third-bank-for-auto-lending-discrimination-and-illegal-credit-card-practices/; and http://www.consumerfinance.gov/newsroom/cfpb-and-doj-reach-resolution-with-honda-to-address-discriminatory-auto-loan-pricing/

Abuses related to conditional delivery agreements and yo-yo scams persist. Survey data suggests that yo-yo scams are a significant problem, especially for lower-income and lower-credit score borrowers.

The yo-yo scam occurs when a consumer believes or is led to believe that the financing is final when in fact the dealer is not treating it as final. Due to the pervasive use of conditional finance agreements, the dealer claims the ability to cancel the deal if the dealer decides that none of the offers by third-party assignees to purchase the finance contract are acceptable.

Conditional loan agreements, or "spot delivery" agreements are virtually standard in car loan contracts, whether the financing is actually final or not. The condition to the contract is the dealer's decision whether to sell the contract to a third-party loan purchaser. If the dealer decides that it is unsatisfied with the return from selling the contract, the dealer can then press the consumer to agree to different terms.

The dealer has substantial leverage over consumers – the dealer is likely holding the consumer's downpayment, trade-in vehicle or both. A dealer can simply refuse to return one or both, leaving the consumer in a significant financial predicament. It is not surprising, then, that most consumers choose to simply sign the new contract. If the consumer decides to pursue legal remedies, the consumer is all but guaranteed to be subject to an arbitration clause that requires the case to be heard by an arbitrator of the dealer's choosing.

The Center for Responsible Lending (CRL) has twice analyzed yo-yo scams. First, in April 2012 CRL published the findings of a survey conducted among agencies that work directly with consumers on auto lending-related issues. CRL contacted 32 employees of five agencies who reported serving more than 2,100 consumers with auto lending problems. These respondents reported that more than 500 (27%) of these consumers complained of a yo-yo scam.[3]

Respondents stated that consumers with low credit scores or lower incomes were most likely to report being the victim of a yo-yo scam. Further, many consumers reported being threatened with legal action or a refusal to return a downpayment or trade-in to induce the consumer to sign the new contract.[4] The outcomes were also consistently negative for the consumer – most ended up paying a higher interest rate and/or negotiating a new finance contract for the same car. In some cases, the consumer ended up driving home in a different car.[5]

CRL also surveyed more than 1,000 consumers who had financed a car about their car financing experiences in 2009.[6] Among these consumers, 4.5% reported being the victim of a yo-yo scam or having a dealer attempt a yo-yo. However, as income level decreased, the percentage of

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[3] Delvin Davis, Center for Responsible Lending, *Deal or No Deal: How Yo-Yo Scams Rig the Game against Car Buyers,* April 2012, available at http://www.responsiblelending.org/other-consumer-loans/auto-financing/research-analysis/Deal-or-No-Deal-How-Yo-Yo-Scams-Rig-the-Game.pdf.
[4] *Id.*
[5] *Id.*
[6] Delvin Davis and Joshua M. Frank, Center for Responsible Lending, *Car Trouble: Predatory Auto Loans Burden North Carolina Consumers,* April 2009, available at http://responsiblelending.org/sites/default/files/nodes/files/research-publication/car-trouble.pdf.

consumers reporting a yo-yo increased. For example, 11% survey respondents making $40,000 or less per year reported a yo-yo, while 25% of those making $25,000 or less reported a yo-yo.[7]

The yo-yo scam remains a significant issue in the car lending market. We urge the FTC to include questions about yo-yo scams, particularly focusing on the tactics used and potential demographic indicators.

B. Add-On Products

In the financing process, consumers are also faced with decisions related to add-on products. These products can include extended warranties, prepaid maintenance plans, protection plans for paint, fabric, wheels and tires, credit insurance, roadside assistance plans and many others. While consumers may have general knowledge about different add-on products the dealer may offer, details about the products and their coverage are difficult, if not impossible, to find and are often disclosed only after the product has been sold. The value and coverage of these products can vary widely and some can be riddled with exclusions that result in significant holes in coverage.

It is also important to recognize that the negotiations around add-on products occur at the end of an otherwise lengthy car buying and financing process. The consumer has already researched the kind of car to buy and negotiated the price, and potentially negotiated the value of a trade-in vehicle. The consumer then has to decide whether to make a down payment and, if so, how much. Once in the finance office, the consumer has to decide whether to accept the dealer's financing, and then is presented with the slate of available add-on products.

This results in significant pressure to make a decision on the spot. Add-on products are expensive, and most buyers would rather finance them along with the car than pay cash. The dealer knows this – the cost of add-on products is most often expressed in terms of the impact on monthly payment. If the consumer wants to take time to think about whether to purchase a particular product, the entire financing process must be put on hold. The system as currently constructed effectively cuts off deliberation. Given that purchasing these products can add hundreds or thousands of dollars to the transaction, some opportunity for thought and comparison is warranted.

Survey data also raise the question of whether these products are targeted at certain consumers. The results of a 2012 CRL survey showed that African American and Latino buyers were almost twice as likely to be sold multiple add-on products as White borrowers.[8] More troubling, African American and Latino consumers more often reported being told that add-on products were required in order to receive a particular car loan.[9] In the case of some Latino borrowers that took part in a series of community focus groups with the National Council of La Raza (NCLR), the offer from the dealer to finance the vehicle purchase was entirely contingent on the buyer accepting these add-on products. Buyers were coerced into accepting these products or risk losing the dealer's financing.

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[7] *Id.*

[8] Delvin Davis, Center for Responsible Lending, *Non-Negotiable: Negotiation Doesn't Help African Americans or Latinos on Dealer-Financed Car Loans,* January 2014, available at http://www.responsiblelending.org/other-consumer-loans/auto-financing/research-analysis/CRL-Auto-Non-Neg-Report.pdf.

[9] *Id.*

Any survey on the car financing experience needs to fully explore issues with add-on products, including but not limited to:

- The cost of the add-on products purchased
- How the add-on products were presented to the consumer
- Whether the consumer was aware that the products were included in the loan
- Whether the consumer compared the terms and conditions of the product purchased with other available products
- Whether the dealer led the consumer to believe certain products were required or mandatory
- Whether the consumer's understanding of the coverage and terms of the product matched with the actual coverage and terms of the product

C. Car Dealer Interest Rate Markup

The issue of dealer interest rate markup received quite a bit of attention during the 2011 Roundtables, including panels on the increased fair lending risk dealer markup presents. When a consumer finances a car purchase through an auto dealer, the dealer has the discretion to increase the interest rate offered by the bank or lending institution and keep some or all of the difference as compensation. This difference between the interest rate priced for risk and the additional interest the dealer adds for compensation is the dealer interest rate markup.

As mentioned earlier, the CFPB and the DOJ have entered into several consent agreements with banks to settle allegations of discrimination in those banks' auto lending portfolios.

Past survey data has shed light on the problems with dealer interest rate markup, and we would suggest that the FTC include similar questions in its survey. The 2012 CRL survey found that even though African American and Latino consumers were more likely to report trying to negotiate their interest rates than White borrowers, borrowers of color still reported receiving higher interest rates than White borrowers.[10] Relatedly, African American and Latino borrowers were also more likely to report having been told misleading information about their interest rate, often being led to believe that the rate they received was the best possible rate.[11]

This information is important. Consumers are told that the best way to combat dealer interest rate markup is to negotiate the interest rate. The data show that for borrowers of color, negotiation didn't work and dealers actively took steps to end efforts to lower the interest rate. Other data have shown the pervasiveness and breadth of dealer interest rate markup. This data show why asking consumers negotiate is not sufficient protection.

Further, even though there are many who reported negotiating the interest rate, two-thirds of those surveyed were unaware of the ability of dealers to mark up the interest rate.[12]

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[10] Delvin Davis, Center for Responsible Lending, *Non-Negotiable: Negotiation Doesn't Help African Americans or Latinos on Dealer-Financed Car Loans,* January 2014, available at http://www.responsiblelending.org/other-consumer-loans/auto-financing/research-analysis/CRL-Auto-Non-Neg-Report.pdf.

[11] *Id.*

[12] *Id.*

The FTC survey should further explore how consumers are affected by the ability of dealers to mark up the interest rate. The survey can look at whether there are apparent interest rate disparities, and it can continue to probe whether consumers truly understand how the market works, whether consumers are taking steps to protect themselves, and whether those protection efforts are fruitful.

IV. Conclusion

The survey, if done correctly, has the opportunity to shed additional light on consumer protection issues in car lending. The biggest abuses are well known. However, additional survey data can show how regulators can and should respond to best protect consumers. In particular, the FTC should be thinking about how to use all of its tools to protect consumers in this market. While education is important, there are abuses that need to be addressed through enforcement and regulation. Better understanding of this market can help to guide the agency toward lasting solutions to the issues that have negatively affected consumers for too long.

APPENDIX

SUGGESTED QUESTIONS

The following list of suggested questions is not intended to be exhaustive, nor should it be seen as a limit on the scope of potential questions. Rather, it is designed to be a starting point for a larger discussion of potential questions.

1. What was the interest rate on this car loan?
2. What was the starting principal balance?
3. What was the loan term?
4. Which soft add-on products were included in the transaction, and were they financed or paid in cash?
5. Did you try to negotiate any of the following:
    a. The interest rate?
    b. The monthly payment?
    c. The price of the car?
    d. The value of your trade-in?
    e. The amount of down payment required?
    f. The length of the loan?
6. Were you aware that any of these are negotiable?
    a. The interest rate?
    b. The monthly payment?
    c. The price of the car?
    d. The value of your trade-in?
    e. The amount of down payment required?
    f. The length of the loan?
7. Did your dealer tell you or lead you to believe that the interest rate you received was the best interest rate available?
8. Were you told that the purchase of additional products such as extended warrantees, service contracts, or insurance protections were required for the financing to be approved?
9. How many dealers did you visit before deciding to purchase the car?
    a. Did you also compare the costs of financing between dealers, or just the price of the car?
10. Did you consult any lenders other than the dealer about financing? If so, how many?
11. On car loans financed at the dealership, dealers receive an interest rate quote from an outside lender. After receiving a rate from the lender, the dealer will often add points to the interest rate before presenting the loan offer to the customer. The bulk of the additional interest is retained by the dealer as compensation. Are you aware your dealer could raise your interest rate, and keep the difference as compensation for making your loan?
    a. If yes: How did you know?
        i. I noticed a written disclosure
        ii. The dealer explained this to me verbally
        iii. I already knew this before negotiating my loan
    b. If no: If you had known the dealer could raise your interest rate, what would have been your most likely response?

i. Try to negotiate the interest rate down
ii. Try to find financing outside of the dealership instead
iii. Walk away from the deal altogether
iv. Still accept the interest rate the dealer offered

12. Sometimes a dealer will allow a customer to drive home with a car before the loan is actually finalized. If the dealer is not satisfied with the available financing options, the dealer might ask the customer to return the car and renegotiate a new deal. During the process of shopping around for this most recent car purchase, did any dealer give you the keys to a car before all financing was actually finalized?
13. Did the dealer ask you to return the vehicle and ask you sign a different financing agreement?
14. Upon returning the vehicle, did the dealer tell you that they could not return your trade in or down payment?
15. What was the outcome after returning the vehicle to negotiate a new deal?
    a. Negotiated on the new deal, and got a better deal than the original
    b. Negotiated on the new deal, but got a worse deal than the original
    c. Did not try to negotiate on the new deal, and got a better deal than the original deal
    d. Did not try to negotiate on the new deal, and got a worse deal than the original
    e. Ended up not purchasing a car from them at all
16. How confident were you in negotiating during the process?
17. Did you trust the dealer to give you the best possible price for the car or the best financing?
18. Have you considered refinancing your car loan/have you actually refinanced your car loan?