FOR IMMEDIATE RELEASE: **MARCH 22, 2013**
Contacts:
NCLC: John Van Alst, (617) 542-8010 or jvanalst@nclc.org
CRL: Chris Kukla, (919) 313-8520 or chris.kukla@responsiblelending.org
CARS: Rosemary Shahan, (530) 759-9440 or rs@carconsumers.org
NACA: Ellen Taverna, (202) 452-1989 or ellen@naca.net

Consumer Financial Protection Bureau Will Hold Auto Lenders Accountable For Discrimination in Auto Lending

Dealers should not be allowed to impose higher interest rates than necessary on consumers

(BOSTON) Yesterday the Consumer Financial Protection Bureau (CFPB) announced it would hold banks and other lenders liable for any auto loans in their portfolio that are discriminatory. Consumer advocates were encouraged by the announcement and hope it is the first step toward eliminating unfair interest-rate markups by auto dealers. Dealers should not be allowed to sell a consumer a higher interest rate than necessary. A flat-fee system would ensure that the dealers have an incentive to provide the lowest interest rate possible.

In the vast majority of cases, dealers can arbitrarily increase the interest rate on cars financed through them and keep some or all of this excess as compensation. This gives dealers an incentive to steer car buyers to loans that provide the most compensation for dealers, rather than the loan that is best for the buyer. Further, this system is hidden from the consumer – most consumers have no idea that their interest rate may be padded to enrich the dealer.

As the CFPB announcement reinforces, interest-rate markups often have a disparate impact on car buyers of color. In several nationwide cases against auto lenders over the past decade, the National Consumer Law Center and co-counsel challenged markups based upon racial disparities. The cases, settled between 2003 and 2007, showed widespread racial disparities on interest-rate markups by dealers that were not related to credit risk. Data from millions of loans subject to the litigation showed that African-Americans were more likely to have their loans marked up and that the markups were higher than those for white borrowers. The settlements reached in these cases limited the amount of markups for a time, but the limits have expired.
"We know that this practice was not confined to just the lenders sued, and did not stop after the settlements," said John Van Alst, attorney at the National Consumer Law Center. "A rule eliminating these markups would ensure a level playing field and end this abuse for everyone."

"Consumers for Auto Reliability and Safety spearheaded efforts to eliminate markups in California, but auto dealers were able to convince the legislature to accept caps instead," said Rosemary Shahan, president of CARS. "Clearly, as this bulletin shows, caps don't address the harm this practice causes."

In addition to leading to discrimination, unfair and arbitrary dealer markups hurt consumers in general because they lack transparency and distort the marketplace. These interest-rate markups cost American families billions of dollars. The Center for Responsible Lending (CRL) estimated that consumers who bought cars in 2009 paid $25.8 billion in extra interest over the lives of their loans due to dealer interest rate markups. CRL research also showed consumers with a loan that includes a padded interest rate are more likely to fall behind on payments and, ultimately, to lose their cars to repossession. "Our research clearly shows that dealer interest rate markups significantly raise costs for borrowers, especially borrowers of color," said Chris Kukla, senior vice president at CRL. "Dealer interest rate markups just make loans riskier for borrowers and lenders alike."

In the lead-up to the mortgage meltdown, mortgage brokers were often marking up loans in a system analogous to auto dealer markups, contributing to the foreclosure crisis we are still grappling with today. We also know from available auto lending data that giving auto dealers discretion to increase interest rates increases risks for borrowers and lenders alike. "A rule prohibiting the practice would level the playing field and encourage fair and transparent competition in the auto finance market," said Ellen Taverna, legislative director for the National Association of Consumer Advocates (NACA).

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Since 1969, the nonprofit **National Consumer Law Center®** (NCLC®) has worked for consumer justice and economic security for low-income and other disadvantaged people, including older adults, in the U.S. through its expertise in policy analysis and advocacy, publications, litigation, expert witness services, and training.

The **Center for Responsible Lending** is a nonprofit, nonpartisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is affiliated with Self-Help, one of the nation's largest community development financial institutions.

Consumers for Auto Reliability (CARS) is a national, award-winning non-profit auto safety and consumer advocacy organization dedicated to preventing motor vehicle-related fatalities, injuries and economic losses.

The **National Association of Consumer Advocates** (NACA) is a nonprofit association of consumer advocates and attorney members who represent hundreds of thousands of consumers victimized by fraudulent, abusive and predatory business practices. As an organization fully committed to promoting justice for consumers, NACA's members and their clients are actively engaged in promoting a fair and open marketplace that forcefully protects the rights of consumers, particularly those of modest means.