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December 3, 2009

The Hon. Christopher J. Dodd, Chairman
The Hon. Richard C. Shelby, Ranking Member
& Members of the Committee on Banking
United States Senate
Washington, DC 20510

Re: Auto Dealers and the Consumer Financial Protection Act

Dear Chairman Dodd, Ranking Member Shelby, and Committee Members:

The undersigned civil rights organizations applaud the efforts of the committee to create the Consumer Financial Protection Agency (CFPA). We are especially pleased that the current Senate bill would ensure that any entity that engages in unfair, deceptive or abusive activities regarding car financing, including auto dealers, will be within the jurisdiction of the CFPA. The CFPA's full set of tools is especially important in preventing discriminatory lending, which can be difficult to prove but is often preventable with simple rules.

Dealers, whether arranging financing or providing financing themselves, all too often engage in discrimination against minorities. Dealers are typically the loan broker and the originator, and also the entity with both discretion and first hand exposure to the car buyer. This often results in dealers' arranging financing that discriminates against classes of car buyers:

- Detailed research by academics earlier this decade on millions of auto loans revealed that auto dealers were far more likely to mark up the loan rates of minorities. Class actions revealed discrimination at GM, Toyota, Ford dealerships, among others. As a result, courts ordered most major car finance companies to cap rates and provide funds for minority-related consumer education, though the orders expire soon.
- Just two months ago, the Department of Justice brought an action alleging that Nara Bank and two car dealers charged non-Asian-American customers higher interest rate mark-ups.¹ Unfortunately, this is the only such case brought in many years by either the DOJ or the FTC, the two entities charged with enforcing the Equal Credit Opportunity Act. Given the widespread nature of the problem revealed in the academic studies and private litigation, the current structure has failed to effectively police auto finance.

¹ <http://www.justice.gov/opa/pr/2009/September/09-crt-1063.html>.

- Analyses have shown that Latinos pay higher used car loan rates than other Americans,² that African-American women pay more than African-American men, and both pay more than whites.³

Dealers are deeply engaged in auto finance. In fact the major source of dealer profits come not from the sale of the car itself, but rather from their "Finance and Insurance" departments, that arrange auto financing to maximize dealer profit in the auto financing and add-ons.⁴ One common profit center for dealers in these transactions is "dealer markups." A dealer markup involves the dealer arranging financing at terms worse than what the consumer qualifies for. A car buyer, whose credit history would entitle the consumer to an 8 percent loan, will be put in a 10.5 percent loan by the dealer and the dealer and the lender will split the extra profits. It is estimated that dealer markups cost consumer \$20 billion per year in unnecessary finance expense.⁵

While markups are bad for all consumers, they are especially unfair to minority car buyers. As academic studies and class action litigation have shown, minority car buyers pay significantly higher dealer markups than non-minority car buyers *with the same credit scores*.⁶ In addition, whistleblowers and former F & I managers have stated that people of color have been deliberately targeted by dealers for discriminatory treatment.⁷

Unfortunately, individual buyers don't often know when discrimination has occurred. While "yield spread premiums," a practice in the mortgage industry similar in many ways to dealer markups, are evident upon the face of the mortgage documents to those with the experience and time to understand them, consumers who have been the victim of dealer markups have no way of knowing that they are paying more for credit than the lender says they need to.

Dealer markups are not the only finance-related activity that gives the dealers both the discretion

² See Hispanic Americans Pay Higher Used Car Loan Rates, Consumer Federation of America, available at: [http://www.americasaves.org/elements/www.americasaves.org/File/Hispanic%20America%20Saves%20Tele%20PR%209-22-08\(1\).pdf](http://www.americasaves.org/elements/www.americasaves.org/File/Hispanic%20America%20Saves%20Tele%20PR%209-22-08(1).pdf).

³ See Ian Ayres, *PERVASIVE PREJUDICE? UNCONVENTIONAL EVIDENCE OF RACE AND GENDER* (Univ. of Chi. Press 2001).

⁴ 2009 F&I Statistics, F&I Management & Technology, December 30, 2008, at 28, stating that "After experiencing slight declines in 2005, F&I's contribution recaptured some ground in 2006 and continued to rise in 2007 and 2008, representing more than half of total profits. Lower gross margins on the sale of new units has helped increase the importance of F&I contributions. Source: CNW Market Research."

⁵ See Center for Responsible Lending survey of dealer kickbacks using figures derived from kickback data in the 2008 Consumer Bankers Association Automotive Finance Study (2007 full-year data), and 2007 sales data for dealer-financed vehicles from CNW Market Research (excluding leases) available at <http://www.responsiblelending.org/other-consumer-loans/auto-financing/cfpa-car-dealer-hill-one-pager-rev-11-5.pdf>.

⁶ See, e.g., Ian Ayers, Expert Report, June 2004, available at: <http://www.consumerlaw.org/issues/cocounseling/content/AHFCIanAyersReportExhibits.pdf>; Cohen, Mark A. "Imperfect Competition in Auto Lending: Subjective Markups, Racial Disparity, and Class Action Litigation." Available at <http://ssrn.com/abstract=951827>.

⁷ "Report concludes hidden auto finance charges cost American car buyers as much as one billion annually; industry-wide practice has led to discrimination against African Americans and Hispanics," press release issued by Consumer Federation of America, National Council of La Raza, and Rainbow PUSH. January 26, 2004.



and incentive to engage in discriminatory pricing. When arranging financing dealers often include overpriced add-ons in a practice known as "loan packing." Because dealers are selling both the car and the financing, consumers are not likely to understand the pricing of these add-ons. In fact, the pricing is largely within the dealers' discretion. Although incredibly difficult to prove under the current regulations, this dealer discretion likely results in higher costs for minorities, just as in the example of dealer markups.

In order to bring transparency and fairness to these transactions, and effectively police the market, the CFPB must have jurisdiction over dealers when they engage in financing related activities. We commend you for the wisdom to include the financing activities of dealers in the proposed CFPB bill. We are anxious to ensure that jurisdiction over these activities remains. Should you or your staff have any questions regarding our position, please contact LCCR Counsel Rob Randhava at (202) 466-6058 or NCLR Legislative Analyst Graciela Aponte at (202) 776-1578.

Sincerely,

A. Philip Randolph Institute
American-Arab Anti-Discrimination Committee
Americans for Democratic Action, Inc.
Asian American Justice Center
Center for Responsible Lending
Common Cause
Community Action Partnership
Japanese American Citizens League
Lawyers' Committee for Civil Rights Under Law
Leadership Conference on Civil Rights
Legal Aid Society – Employment Law Center
NAACP
National Association of Consumer Advocates
National Association of Human Rights Workers
National CAPACD
National Community Reinvestment Coalition
National Congress of American Indians
National Congress of Black Women, Inc.
National Council of La Raza
National Fair Housing Alliance
National Urban League
Poverty & Race Research Action Council
Service Employees International Union

For further information about auto dealers' practices:

Fueling Fair Practices, a road map to improved public policy for used car sales and financing,
by John Van Alst, National Consumer Law Center:



<http://www.aecf.org/~media/PublicationFiles/fuelingfairpractices.pdf>

Driving a Hard Bargain: Improving the Auto Market for Latino Families, by National Council of La Raza: www.nclr.org/bankingreform.

Pursuit of the Dream: Cars and Jobs in America, produced by the Annie E. Casey Foundation:
<http://www.aecf.org/MajorInitiatives/FamilyEconomicSuccess/PursuitoftheDream.aspx>

Testimony of John Van Alst, National Consumer Law Center, before U.S. House Energy and Commerce Subcommittee on Commerce, Trade and Consumer Protection:
http://energycommerce.house.gov/index.php?option=com_content&view=article&id=1517:consumer-protection-in-the-used-and-subprime-car-market&catid=129:subcommittee-on-commerce-trade-and-consumer-protection&Itemid=70

Testimony of Rosemary Shahan, President of Consumers for Auto Reliability and Safety (CARS) before U.S. House energy and Commerce Subcommittee on Commerce, Trade and Consumer Protection:
http://energycommerce.house.gov/Press_111/20090305/testimony_shahan.pdf

Testimony of Michael Calhoun, President of Center for Responsible Lending, before U.S. House Committee on Financial Services:
<http://www.responsiblelending.org/mortgage-lending/policy-legislation/congress/cfpa-calhoun-testimony.pdf>