Driven to Disaster:
Car-Title Lending and Its Impact on Consumers

Executive Summary

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INTRODUCTION

This report serves as an update to *Car Title Lending: Driving Borrowers to Financial Ruin*, a joint 2005 publication of the Consumer Federation of America (CFA) and the Center for Responsible Lending (CRL). In the full paper, we describe the structure of car-title loans; provide an overview and estimate of the size of the national car-title loan market; discuss the typical borrower's experience with car-title loans; and analyze newly acquired borrower-level data. Here, we present our key findings and policy recommendations.

BACKGROUND

As their name makes clear, car-title loans are secured by a borrower's title to a vehicle owned outright. While there are variations, this paper focuses primarily on 30-day car-title loans with balloon payments due at the end of the term (hereafter "car-title loans"). These loans average $951 and are underwritten primarily based on the value of the vehicle that secures the loan. The majority of state car-title loan laws either directly authorize 300 percent APR loans or set no interest rate caps at all. Car-title loans are commonly advertised with interest of 25 percent per month, which equates to an APR of 300 percent.

Table 1: Comparison of Typical Payday and Car-Title Loan Features

Features	Payday Loans	Title Loans
Typical loan size	$350	$951
Fee/interest	$16 per $100 borrowed	$25 per $100 borrowed
Typical loan term	Two weeks	30 days
Typical APR	416 percent	300 percent
Loan term	Full payment due on next payday (usually in about two weeks)	Full payment due in one month
Collateral	Secured by personal check or access to bank account	Secured by car title

FINDINGS

Approximately 7,730 car-title lenders operate in at least 21 states costing borrowers $3.6 billion each year in interest on $1.6 billion in loans.

Based on regulator data from the 21 states where car-title lenders operate, we estimate that there are approximately 7,730 car-title locations in the U.S. Although many states do not publish data on the operations of car-title lenders, five state regulators—in Illinois, Mississippi, New Mexico, Virginia and Tennessee—provide sufficient information to allow us to estimate the number of car-title loans per location nationally. Based on an analysis of this data, we estimate each car-title location, on average, originates 218 loans per year. Since there are a total of 7,730 car-title lenders throughout the 21 states with car-title lending, we find that about 1.7 million high-cost car-title loans are made each year (7,730 lenders * 218 loans per lender).

Table 2: National Car-Title Loan Market Size

Total Car-Title Loans Nationally	1.7 Million
Average Loan Amount	$951
Total Loan Volume Originated	$1.6 Billion
Average Interest Paid Per Loan	$2,142
Total Interest Paid	$3.6 Billion

The average car-title borrower renews their loan eight times, paying $2,142 in interest for $951 in credit.

The president of TitleMax, one of the nation's largest car-title lending chains with locations in many states, notes that "customer loans are typically renewed at the end of each month and thereby generate significant additional interest payments." In fact, the average TitleMax customer renews his or her loan eight times.

Using a weighted average from several states that record their per-loan average, we are able to estimate an average amount of $951 for a car-title loan nationally. Assuming a consumer will renew their loan eight times as in the TitleMax example, that consumer pays $2,142 in interest. Nationally, this means the total car-title loan market generates $3.6 billion in interest payments (1.7 million loans times $2,142 of interest per loan) while only generating of $1.6 billion of actual loan volume (not including renewed principal).

Table 3: Total Cost to Car-Title Loan Borrower for a $951 Loan, 25 Percent per Month Interest (300% APR)

Loan principal	$951
Interest ($951*25%)	$238
8 additional renewal fees ($238*8)	$1,904
Total interest paid	$2,142
Total amount paid by borrower in both interest and principal for $951 car-title loan	$3,093

Car-title loans' annualized percentage rates (APR) are especially excessive considering the value of the collateral and the relatively low amount of the loan. In our borrower-level data set, the median loan-to-value ratio was 26 percent, yet the APR was 300 percent.

In the absence of meaningful underwriting, lenders protect themselves from losses on car-title loans by lending a relatively small percentage of the car value and threatening repossession to ensure that the borrower decides to prioritize servicing their car-title debt over other obligations. Looking at borrowers in the CFA/CRL dataset, the median loan-to-value (LTV) ratio for car-title borrowers was 26.4 percent.

Table 4: Summary of CFA/CRL Dataset used in LTV Calculations

Median Loan Size	$845
Median Car Value	$3,150
Median Loan-to-Value Ratio	26.4%
Median APR	300%

One in six borrowers in our data set faced repossession, with repossession fees averaging half of the borrower's outstanding loan balance.

Our analysis of the CFA/CRL dataset further found that one out of every six loans (17 percent) incurred a repossession fee. The repossession fee—most typically between $350 and $400—is added to the borrower's running balance, causing the borrower to become even more indebted despite also losing the collateral. These fees and others, despite the low loan-to-value ratio, mean nearly all proceeds of the repossession sale go directly to the lender.

POLICY RECOMMENDATIONS

Car-title loans carry inherently unsuitable terms that cause already vulnerable borrowers to pay more in fees than they receive in credit while putting one of their most important assets at risk. Other than assessing the resale value of the borrower's car, lenders do little, if any, meaningful analysis of the borrower's ability to repay the loan. As a result, most car-title loans—though structured as short-term— repeatedly generate new interest and origination fees for the lender upon each renewal.

Non-purchase loans secured by ownership of a vehicle should be strictly regulated. Safeguards are necessary to protect vulnerable consumers from losing their most valuable asset and means of transportation. Any loan secured by an important asset—such as a household's means of transportation to work—must come with significant safeguards, as is now standard in home mortgage lending.

A good starting point for these protections are the Federal Deposit Insurance Corporation (FDIC) Affordable Small Dollar Loan Guidelines, which suggest that small loans be made under the following parameters to be sustainable for borrowers:

FDIC Small Loan Guidelines

- Loan amount: $2,500 or less
- Minimum 90-day loan term
- 36% APR or lower
- Approval: Generally within 24 hours; streamlined underwriting, including proof of identity, address, income, and credit report (while a minimum credit score is not required, the report can shed light on repayment ability based on other obligations)

Congress and the States can act to limit rates on car-title loans. In addition, state and federal policymakers, including the Consumer Financial Protection Bureau, can enact protections related to loan terms and underwriting processes.

States should not grant exemptions to their existing interest rate limits for car-title loans. Many states with car-title lending have caps of around 36 percent on the annual interest rates that may be charged for small loans. Car-title lenders, along with their payday counterparts, have persuaded some state legislatures to exempt them from this limit, arguing that their loans are very short-term and, therefore, an annual interest rate limit is inappropriate to apply. Yet as we have seen, most loans are renewed multiple times and are therefore not short-term. In addition, though some lenders argue that they cannot make loans at less than triple-digit rates, other lenders continue to make small loans within limits of around 36 percent, with or without a car title as collateral.

Car-title loans should be structured as installment loan products with reasonable limits on interest and an evaluation of the borrower's ability to repay the loan. An installment product should include equal monthly payments that amortize the loan over the term, giving borrowers the chance to pay down their debt gradually, and should not include a final balloon payment. Pairing a longer loan term with equal amortizing payments and solid underwriting standards was found to be the key to success in the FDIC's small loan pilot program.

Borrowers should have adequate protections in the event of a default. Such protections include notice prior to repossession or sale of the vehicle, a right to redeem the vehicle, and a ban on deficiency balances (in which the borrower owes principal plus accrued interest and fees to the lender if the sale of their car does not cover the outstanding debt owed). Sales of repossessed vehicles should be commercially reasonable with any surplus returned to the borrower.

Policymakers must remain vigilant in enforcing their state lending laws. Car-title lenders should not be able to evade small-loan rate caps and other protections. Car-title loan companies in several states have taken advantage of narrow definitions in laws, or loopholes or gaps in the law, to charge higher rates than their state legislatures intended.

About the Center for Responsible Lending

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.

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