Testimony of Commissioner Julie Menin
New York City Department of Consumer Affairs
Before the
New York State Senate Committee on Banks

Hearing on
An Examination of Predatory Lending Practices in the Subprime Auto Loan Industry

April 22, 2015

Good morning Chair Savino and members of the New York State Senate Banks Committee. I am Amit S. Bagga, Deputy Commissioner of External Affairs at the New York City Department of Consumer Affairs ("DCA"). I am here representing Commissioner Julie Menin, who was unable to attend today, but sends her best to the Committee and commits to working with you to address the important issue that is the subject of today's hearing.

I greatly appreciate the opportunity to speak with you today about predatory lending practices in the auto loan industry. DCA applauds the committee for highlighting this issue, one which has forced so many New Yorkers into a debilitating cycle of indebtedness, simply because they've purchased cars, which for so many, are necessary for daily living.

Mayor de Blasio has made addressing the issue of economic inequality the centerpiece of his administration. DCA's enforcement and investigations in the used-car market are an important part of the work the agency does to protect consumers, especially those with lower incomes, many of whom need a car to have access to better jobs and more opportunity.

Subprime Auto Lending: Challenges and Scope

A car is often the largest purchase a family might make; we know that access to a car is particularly important for many New Yorkers with lower incomes, for whom having a car can mean the difference between opportunity and poverty. A March 2014 Urban Institute study of the impact of automobile access on lower-income housing voucher recipients found that "in almost all metropolitan areas, individuals without reliable access to automobiles can reach far fewer opportunities within a reasonable travel time compared with those who travel by automobile."[1] The same report, which was based on research conducted in 10 metropolitan areas – five transit-rich ones and five with fewer public transit options – also found that across all of the metropolitan areas "automobile ownership is associated with higher employment status,

[1] Urban Institute, Driving to Opportunity: Understanding the Links among Transportation Access, Residential Outcomes, and Economic Opportunity for Housing Voucher Recipients, page 3 (March 2014).

[higher] weekly hours worked…[higher] hourly earnings, [reduced] racial disparities in unemployment rates…and [reduced] unemployment duration."[2]

Access to a car was also found to be particularly important for low-income women and female-headed households, for whom having car access often meant a higher likelihood of leaving welfare and an increase in income.[3] In fact, the president of Vehicles for Change, a Maryland-based nonprofit that repairs donated cars and then awards them mostly to single mothers near the poverty line, was mentioned in a July 2014 National Journal piece as asserting that three-quarters of the organization's clients saw an income boost of approximately $7,000 by gaining access to a car.[4]

Considering how crucial automobile access can be to economic opportunity, the growth of subprime automobile loans is alarming. Data from the credit monitoring bureau Equifax shows that the percentage of subprime auto loans as a total of all auto loans issued in the United States climbed from 20 percent in 2009 to 27 percent in 2013, representing over $100 billion in loan amounts in 2013.[5] According to a New York Times article published in March of this year, auto loans taken by subprime borrowers have more than doubled since the onset of the financial crisis, with one in four auto loans are now being issued to subprime borrowers.[6] In the last quarter of 2014 alone, lenders issued over $20 billion in subprime auto loans, nearly double the amount issued during the same period in 2010.[7]

The same article cites the stories of New Yorkers such as Zheng Hui Dong, an immigrant who purchased a vehicle from a Queens dealership for a total cost of $42,000 over the lifetime of the loan – an estimated four times the resale value of the car.[8] A similar example is also provided of Beatriz Rodriguez, who – despite filing for bankruptcy in 2014 – still makes payments on the car she uses to take care of her family.[9]

Many borrowers often fall deeper into debt traps by taking "auto title" loans or "auto pawn" loans. Auto title loans allow consumers to borrow against the equity they might have in their cars and auto pawn loans allow consumers to turn their cars in to auto pawn lenders, who in turn provide consumers with cash. Consumers are not allowed access to their cars until the loans are

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[2] ibid.
[3] ibid.
[4] Quinton, S. (2014, July 14). How Car Ownership Helps the Working Poor Get Ahead. http://www.nationaljournal.com/next-america/economic-empowerment/how-car-ownership-helps-the-working-poor-get-ahead-20140724
[5] Silver-Greenberg, J. and Corkery, M. (2014, December 25). Rise in Loans Linked to Cars is Hurting Poor. http://dealbook.nytimes.com/2014/12/25/dipping-into-auto-equity-devastates-many-borrowers/
[6] Silver-Greenberg, J. and Corkery, M. (2015, March 1). Wells Fargo Puts a Ceiling on Auto Loans. http://www.nytimes.com/2015/03/02/business/dealbook/wells-fargo-puts-a-ceiling-on-subprime-auto-loans.html?_r=0
[7] ibid.
[8] ibid.
[9] ibid.

fully paid. While auto title loans are illegal in New York, consumers in our state still have access to auto pawn loans, which are structured very similarly, with staggeringly high interest rates and short repayment periods. A December 2014 New York Times article reported that many title loans can carry interest rates of up to 500 percent, and many borrowers, unable to fulfill their debt obligations within the common 30-day cycle, are forced to renew their loans at the end of each cycle. This in turn forces them to incur fees upon each renewal.[10] Additionally, because these loans are based on assessments of a car's value and not a borrower's ability to repay, one in six title-loan borrowers will have their cars repossessed, according to the Center for Responsible Lending.[11] Because so many loans are issued to individuals who cannot afford them, borrowers often face repossession of what is often their primary mode of transportation – depriving them of a way to get to and from work.

Through the direct financial counseling that we have provided through our Office of Financial Empowerment ("OFE"), the first municipal initiative in the country with the specific mission to empower and protect consumers with lower incomes, has shown this cycle of indebtedness can exacerbate the many challenges borrowers might already face, such as paying for housing, childcare, or even basics such as food and utilities. By peddling subprime auto loans, lenders – and by extension, dealers – are forcing hard-working Americans to make a false choice between the economic security that comes with employment and being mired in a cycle of debt; a choice nobody should have to make.

This is why DCA, through our licensing and patrol enforcement authority over secondhand auto dealers in New York City, as well as our broad jurisdiction to conduct legal investigations into predatory business practices, has chosen to pursue bad actors, investigate lenders, and, work with others to create an innovative safe lending product with clear terms for consumers. I would like to take this opportunity to discuss our jurisdiction and our work on this issue to date.

DCA's Jurisdiction

In addition to the Licensing and Consumer Protection Laws that DCA has the authority to enforce, Chapter 64 of the New York City Charter also gives DCA authority to investigate and bring action against businesses for engaging in deceptive practices.

The agency exercises its broad grant of authority in a number of ways. DCA's enforcement division conducts regular patrol inspections of New York City businesses to ensure compliance with New York City laws and rules, our legal division investigates complaints, conducts "fitness" reviews, and we can also bring charges, impose fines, and seek consumer restitution, penalties, and injunctive relief. Finally, the agency may enter into comprehensive settlement agreements or consent orders, which generally involve compliance requirements, injunctive

[10] Silver-Greenberg, J. and Corkery, M. (2014, December 25). Rise in Loans Linked to Cars is Hurting Poor. http://dealbook.nytimes.com/2014/12/25/dipping-into-auto-equity-devastates-many-borrowers/
[11] ibid.

relief, consumer notice provisions, the payment of fines and, where applicable, the payment of restitution to consumers.

DCA regulates used car dealers in two ways: first, by licensing the approximately 877 secondhand auto dealers in New York City; and second, through our Consumer Protection Law, which covers all people and entities that do business in New York City.[1] Since January 2014, we have received 1,491 complaints about secondhand auto dealers and we have issued 166 violations. In the same time period, we have also assessed more than $620,000 in fines against used car dealers and secured nearly $1 million in restitution for consumers.

In the last year, we have utilized our jurisdiction to launch a broad investigation into the sale of unrepaired recalled used cars, forced dealerships who have engaged in a variety of predatory practices into paying hundreds of thousands in fines and consumer restitution, and most notably, we launched, for the first time ever, an investigation into possible predatory subprime loans being arranged through dealerships.

Planet Automotive

In October 2014, DCA announced the result of its investigation into deceptive advertising and high-pressure sales tactics at Planet Automotive (now "Planet Auto Mall"), a used car dealership in Queens. Our investigation resulted in the company and its owner having to pay $441,000 in penalties and restitution to 39 consumers.

From 2009 through 2014, 165 consumers filed complaints with DCA, the State Attorney General's Office, and the Better Business Bureau about Planet Automotive, which had been previously doing business as KG Suzuki. The company advertised used vehicles at discounted prices on various websites, luring consumers to travel to the dealership in Long Island City. Once the consumers were there, sales representatives disclosed additional charges that were not included in the advertised price. The dealership also did not allow consumers to shop around for loans, and instead required them to finance all purchases through a lender chosen by Planet Automotive. Customers were made to wait hours before being able to meet with a finance representative, who then pressured them into signing unclear and incomplete agreements, which the dealership later altered, increasing the amounts owed to much higher than what was agreed upon.

DCA's settlement agreement with the company required oversight of the dealership by an independent monitor for at least one year. This monitor is working with the company to reform its business practices, update its documents and forms, and will be reporting to DCA on the dealership's compliance efforts. DCA also required Planet Automotive to clearly post all prices, cancellations, and finance terms in all consumer contracts, and conspicuously post the Used Car

[1] New York City Administrative Code ("NYC Code") §§ 20-700, *et seq*., 20-101, *et seq*. (Consumer Protection Law), and 20-264, *et seq*. (SHAD Licensing Law); Title 6 of the Rules of the City of New York, Chapter 2, Sections 2-101 and 2-103.

Buyer's Bill of Rights. The dealership must also provide any consumer who wants financing with a notice stating that consumers are not required to finance through the dealership, as well as other information about credit scores, obtaining a credit report, the finance charge for the purchase of add-ons, including warranties and insurance, and the total finance charge and monthly installment cost to purchase the vehicle without add-ons. Additionally, in a first for a settlement agreement, we were able to require the dealership to check the recall status of each vehicle and repair all safety defects prior to sale.

Santander Consumer USA and Santander Consumer Funding 3 LLC

In November 2014, DCA issued subpoenas to the two auto financing arms of Banco Santander, S.A. in an effort to collect documentation regarding subprime loans underwritten by the lenders as part of DCA's first-ever investigation into the lending practices of used-car dealers. Both financing arms provide both direct loans, which consumers can arrange directly with the lender, as well as indirect loans, which are arranged by a third party, such as a used car dealership.

According to Santander Consumer USA's 2013 Annual Report, the company had retail installment loans with more than 2 million customers across the U.S. and relationships with nearly 14,000 automotive dealers in the U.S., including dozens of car dealerships in New York City. At the time the subpoenas were issued, used car financing represented nearly two-thirds of their outstanding installment loans, 88 percent of which were subprime.

DCA's investigation has been focused on indirect auto loans financed by the lenders and the agency is examining records of these loans over the past three years. New York City regulations governing used car dealers require that if a dealership recommends a financing company such as Santander to a consumer, the dealers must disclose the interest rate that the company can charge and other terms and charges. DCA's earlier investigations into dealer lending practices uncovered information that suggested that dealerships might not be complying with this requirement. Instead, dealers are directing consumers to costly loans which benefit the dealer and ultimately harm the consumer.

Santander Consumer USA is also currently licensed by DCA as a debt collection agency and our investigation is also looking into the company's debt collection practices; we will be happy to share more information with the Committee on this investigation at the appropriate time.

DCA's stated mission is to protect and empower consumers and business alike to ensure a fair and vibrant marketplace. As such, we see our role as including innovation that creates a fairer marketplace – for both businesses and consumers. We have been working with the advocacy, private, and public sectors to innovate new ways to protect consumers, such as facilitating the creation of new products that can push the marketplace to be fairer.

Auto Loan Initiative

A key example of this innovation is our initiative to create or promote a safer loan product for qualified secondhand auto borrowers. This product will help protect consumers from falling into the cycle of indebtedness we've spoken about today and would also alter the marketplace for such loans by introducing one or more products that could be both safe and competitive.

In March of this year, DCA issued a Request for Expression of Interest ("RFEI") to banks and credit unions; this is an invitation to the industry to create products that meets guidelines we've developed or submit to us for review an existing safe and affordable loan product. DCA's unique role as a regulator and a direct service provider enabled us to take lessons learned from our investigations into secondhand auto dealer practices and utilize our in-house, top-notch policy expertise in the Office of Financial Empowerment to create a solution to what is becoming an intractable problem.

DCA's auto loan initiative seeks to link consumers to direct financing options with reputable banks and credit unions in New York City who agree to various consumer-friendly terms and offer interest rates lower than New York State's usury cap of 16 percent. With new consumer-friendly loan products on the market, the car-buying public will benefit from increased competition and increased access to loan information, helping to ensure that consumers can find loans they are qualified for and can afford. These efforts will also help support consumers' financial stability and may also help lower default rates. Financial institutions can benefit from a broader customer base through referrals and additional marketing.

Our Office of Financial Empowerment will engage and review submissions from institutions insured and regulated by the Federal Deposit Insurance Corporation (FDIC) or the National Credit Union Administration (NCUA). The following are among the requirements contained in the RFEI:

- loans should cover the cost of used vehicles at the time of purchase and/or to refinance existing auto loans;
- the lender must describe criteria that make the loan affordable;
- the lender must also provide a description of fair debt collection practices to consumers used by the institution;
- loans cannot include as "required" any "add-ons," such as credit insurance, roadside assistance, extended warranty protection, or vehicle service contracts;
- the lender must guarantee that there is no compensation given to the secondhand auto dealer for referrals;
- loans must have no or a low loan application fee (e.g., $25 or less); *and*

- the lender must provide clear and transparent marketing materials and loan disclosures.

This new auto loan initiative will add to DCA's solution-based products, which include the NYC SafeStart bank account, introduced in 2009. The account is designed to serve people with limited banking experience and/or a poor track record with banking, allowing them to build their track record as a desirable customer. These accounts have a low minimum balance requirements, no monthly maintenance fees, and no overdraft fees.

From protecting consumers with low incomes to conducting major investigations into predatory business practices, DCA has been utilizing our broad jurisdiction to ensure that we are creating a fairer and more vibrant marketplace, which, as I stated earlier, is our core mission. We will continue to pursue this mission through our legal, enforcement, and services work, which has already clearly shown that used-car consumers are in need of protection on a variety of fronts.

We look forward to an ongoing dialogue with the committee on this important topic. Thank you for the opportunity to testify today. I will be happy to answer your questions.