COMMENTS TO THE FEDERAL TRADE COMMISSION

MOTOR VEHICLE ROUNDTABLES – PROJECT NUMBER P104811

BY

CENTER FOR RESPONSIBLE LENDING
CONSUMER FEDERATION OF AMERICA
CONSUMERS FOR AUTO RELIABILITY AND SAFETY
NATIONAL ASSOCIATION OF CONSUMER ADVOCATES
NATIONAL CONSUMER LAW CENTER, on behalf of its low income clients
NATIONAL COUNCIL OF LA RAZA

FEBRUARY 1, 2012

We submit these comments in response to the request for comments as part of the Federal Trade Commission (FTC) Motor Vehicle Roundtables – Comment, Project Number P104811.

We call on the FTC to:

- Prohibit auto dealer interest rate markups;
- End yo-yo scams;
- Curb loan packing; and
- Implement steps to ensure that dealers do not fail to pay off liens on trade-in vehicles or cause other harms to consumers when the dealer closes.

These steps will create a fairer and more transparent automobile financing marketplace.

THE FTC SHOULD BAN DEALER MARKUPS ON INTEREST RATES

Dealer compensation should be divorced from the ability to increase interest rates from one consumer to another. Dealer compensation should be limited to a flat fee compensation system or a fee based on a percentage of the amount financed and with adequate disclosure of the fee.

The Role of "Indirect Lending" and Interest Rate Markups in the Auto Finance Market

Auto financing through the dealer is commonly referred to as "indirect financing," but is actually a credit transaction directly arranged by the dealer. In the vast majority of these automobile financing transactions, the dealer uses a retail installment sales contract. Under the legal structure of the retail installment sales contract, the dealer is both the creditor and the automobile seller, and as such the dealer enters into an agreement to both sell and finance a vehicle for the customer at a certain price, a certain interest rate, and a certain number of payments (along with other terms for the loan). Although the phrase "indirect financing" views the transaction from the perspective of an assignee of that retail installment sales contract, the legally significant fact is the dealer is the creditor with whom the consumer is negotiating the transaction.

Typically, the dealer does not want to retain ownership of the retail installment sales contract and collect payments into the future. The dealer typically borrows funds to purchase inventory (called "floorplan financing" or "floorplanning") and must pay a portion of that loan back to the floorplan creditor upon the sale of each vehicle. Because of this, the dealer elects to sell the retail installment sales contract to a third party, such as a finance company, bank, credit union or other investor to obtain the funding to repay the floorplan financing for that automobile.

To facilitate the process, the dealer communicates with potential loan purchasers at the same time the dealer is negotiating the terms of the sale with the consumer. Potential third-party purchasers make most of the common terms and conditions available to dealers in regularly published rate sheets and in the conditions of authorized dealer agreements that are typically entered into before loan purchasers agree to buy loans from the dealer. When a consumer applies for credit with the dealer, the dealer sends the consumer's financial information to one or several potential loan purchasers. Interested purchasers then respond to the dealer with offers to purchase that contract, specifying the interest rate and specific conditions and terms that the loan purchaser will require to purchase the loan.

The interest rate that the potential third-party purchaser is willing to accept to purchase the retail installment sales contract from the dealer is called the "buy rate." The third-party purchaser may give the dealer the opportunity to add compensation to the transaction, also called "dealer reserve" or "dealer participation." This form of compensation allows the dealer to add to the interest rate and keep some or all of the difference in net present value between the buy rate and the rate ultimately offered to the consumer. Some third parties offer a flat fee for compensation. Some third party purchasers cap the amount of dealer interest rate markup, while others allow unlimited markups.

Some third-party purchasers charge the dealer to sell the retail installment sales contract to them, purchasing those contracts for less than face value. These programs raise entirely different issues than the dealer markup on interest rate. Instead, these programs result in dealers artificially inflating the cost of the car to recoup the discount at which the dealer will have to sell the retail installment sales contract.

Nearly eighty percent of financed auto sales are financed through the dealer, which effectively gives dealers control over lenders' access to this market.[1] Dealers routinely advertise that they work with several lenders to get consumers financed or to find the best deal. Dealers call this financing model "dealer-assisted financing" even though on every retail installment sales contract the dealer is the original creditor. The dealers' characterization of the transaction fosters the illusion that the dealer is more like a broker than a creditor. The characterization also paints the dealer as not in control of the process even though the dealer has the ability to choose between loans, adjust the interest rate, and structure other essential terms of the loan. Even the "Understanding Vehicle Financing" guide that the FTC partnered with the American Financial Services Association Foundation and the National Automobile Dealers Association to produce fosters this confusion.

This mischaracterization of the dealer's true role in the transaction is confusing to consumers and allows the dealer to use this confusion to the dealer's advantage.

---

[1] Richard Howse, "How Different is the Indirect Channel from the Direct Channel?", JD Power & Associates, Mar 31, 2008.

The FTC Should Prohibit Dealers from Receiving Compensation Based on Increasing the Interest Rate

The FTC should write regulations banning dealer interest rate markups in the same way that the Federal Reserve and Congress in the Dodd-Frank Act have dealt with a similar issue of compensation in mortgage lending. In September 2010, the Federal Reserve issued final rules that, in part, banned compensation for mortgage originators and mortgage brokers that vary based on the terms of the loan other than the loan's principal balance.[2] These rules were the product of significant study of mortgage loan compensation practices and the impact certain compensation can have on consumers and the broader market. The findings and substance of the rule have a direct bearing on the issue of car dealer interest rate markups.

The Federal Reserve had the authority under the Home Owner's Equity Protection Act of 1994 (HOEPA) to prohibit acts and practices in mortgage loans that the Board finds to be unfair, deceptive or designed to evade the provisions of HOEPA.[3] Because HOEPA does not define an unfair or deceptive act or practice, the Board adopted the FTC's standards for unfair and deceptive acts and practices, finding mortgage compensation practices to be unfair.

Mortgage brokers and many retail loan officers historically received compensation that varied based on the terms of the loan. This compensation increased if the broker or loan officer could convince the borrower to pay a higher interest rate than that for which the borrower qualified or accept other terms unfavorable to the borrower, such as prepayment penalties.

Unlike the car dealer interest rate markup, the actual amount of compensation paid to mortgage brokers was disclosed to the borrower. In crafting the rule, the Federal Reserve conducted consumer testing and focus groups to test the efficacy of this disclosure. The Federal Reserve had previously published proposed rules that found compensation that varied based on the terms of the loan unfair and proposed using more extensive disclosures to address the issue. On further study, the consumer testing undertaken as part of that rule caused the Federal Reserve to withdraw the rule and instead propose and enact a rule that simply eliminated unfair compensation.

The Federal Reserve determined that the practice of compensation to mortgage originators varying with the terms of the loan causes substantial injury to consumers, is not reasonably avoidable, and is not outweighed by benefits to consumers or to competition. Of particular note, the Federal Reserve found:

> When loan originators receive compensation based on a transaction's terms and conditions, they have an incentive to provide consumers loans with higher interest rates or other less favorite terms. Yield spread premiums, therefore, present a

[2] 75 Federal Register 58509 et seq. (September 24, 2010).
[3] 15 U.S.C. 1639(l)(2). This authority has now passed to the Consumer Financial Protection Bureau.

> significant risk of economic injury to consumers… Because consumers generally do not understand the yield spread premium mechanism, they are unable to engage in effective negotiation… These consumers suffer substantial injury by incurring greater costs for mortgage credit than they would otherwise be required to pay.[4]

The Federal Reserve's consumer testing included several different types of disclosure and found that consumers did not understand the compensation system and its potential effect on the consumer's loan no matter how it was disclosed. Importantly, to the Federal Reserve this confusion was cause to eliminate the unfair compensation rather than allow loan providers to bury the information through confusing paperwork or in the annual percentage rate. Congress agreed with the Federal Reserve in the Dodd-Frank Act. Further, the Federal Reserve did not differentiate between mortgage brokers or loan officers of a creditor. Regardless of how car dealers choose to portray themselves, the Federal Reserve's legal analysis is directly applicable to the issue at hand because there is no debate that the dealer originates the loan.

Ample evidence exists to show that interest rate markups on car loans are routinely applied unfairly and that they disproportionately affect minority borrowers. This method of compensation has proven to cause great problems for minority car buyers. Even when they have the same or better credit than their white counterparts, minority borrowers are more likely to be charged higher dealer markups. Discriminatory markups have resulted in substantial class action lawsuits representing millions of black and Hispanic car buyers.

Dealer interest rate markup is also a practice with significant financial impact for consumers. According to research from the Center for Responsible Lending, dealer interest rate markups totaled $25.8 billion in additional interest paid for those who bought cars in 2009.[5]

Further, while dealers are legally creditors, they act more like loan brokers – dealers shop loans among multiple potential purchasers of that loan and then choose one for the customer. As stated previously, dealers routinely advertise that they work with multiple lenders to obtain financing. Dealers refer to the financing as "dealer-assisted financing" even though the dealer is in fact the creditor. As such, it is very important to understand the incentives behind the transaction and eliminate those that stifle competition or put consumers in more expensive loans than necessary.

---

[4] 75 Federal Register 58509, at 58515. Research from the Center for Responsible Lending supported this finding – broker compensation led to subprime consumers paying more than necessary, and the compensation system led to discriminatory pricing, particularly for subprime borrowers. See Keith Ernst, Debbie Bocian, and Wei Li, *Steered Wrong: Brokers, Borrowers, and Subprime Loans*, Center for Responsible Lending, April 8, 2008.

[5] Delvin Davis and Joshua M. Frank, *Under the Hood: Auto Loan Interest Rate Hikes Inflate Consumer Costs and Loan Losses,* Center for Responsible Lending, April 19, 2011

The ability of the dealer to add to the interest rate for its own gain creates a perverse incentive for the dealer to push the consumer into the most favorable loan for the dealer rather than the loan that provides the lowest-cost for the consumer. The result of these misaligned incentives is “reverse competition,” a classic illustration of market failure. To stay in the auto finance business, lenders compete for dealers’ business by offering larger and larger interest rate kickbacks, compensation, and incentives. This reverse competition drives prices to consumers up rather than down. This impact on the market is the same that led the Federal Reserve to prohibit this manner of compensation on mortgage loans.

A survey of more than 1,000 people who had purchased a car in the two years prior found that those who were either told or were led to believe that the dealer had found them the best rate in the market were charged two percent more in interest on their loans than their similarly situated peers.[6] The Federal Reserve also found that those who trusted mortgage originators tended not to shop around and generally received more expensive loans as a result.[7]

The only consumer disclosure about the dealer markup is a general disclosure that informs the consumer that a dealer may be gaining compensation through the interest rate and that the buyer has the right to negotiate that rate. A CRL-commissioned poll of North Carolina voters found that an overwhelming majority—79%—were unaware of the practice, despite the general disclosure.[8] These results are completely consistent with the FRB analysis of such disclosures in the mortgage market.

Consumers cannot effectively shop if the compensation system creates perverse incentives to steer consumers into more expensive loans.

Recommendation

Dealer compensation should be divorced from the ability to increase interest rates from one consumer to another. Rather, compensation should be based on more objective criteria that remove incentives that solely benefit the dealer. The compensation system should incent the dealer to find the lowest-cost financing for the consumer. Dealer compensation should be limited to a flat fee from the loan purchaser or a fee based on a

---

[6] CRL conducted survey through Macro International’s CARAVAN interviews and includes a sample size of 1,007 customers across the U.S., 81% of whom owned a car or truck as of Nov 2008. The primary findings are based on approximately a quarter of those respondents (sample size of 268) who reported using a loan financed through their car dealership. Survey on file with CRL.

[7] 15 Federal Register 58509 at 58515.

[8] Public Policy Polling Survey of North Carolina Voters (on file with CRL). Similarly, a California statewide poll commissioned by Consumers for Auto Reliability and Safety and CALPIRG found that most people surveyed thought that such practices were already illegal. Ninety-three percent of respondents favored requiring dealers to disclose the lowest interest rate the buyer qualified for. Decision Research "California Statewide Voter Survey Report," 2004.

percentage of the amount financed with adequate disclosure of the fee. In either case, the compensation cannot be related to the terms of the loan provided, except for the size of the loan.

A finance manager wrote in a recent column published in a trade magazine:

> "…I might be walking on thin ice here, but, as far as I'm concerned, [dealer] reserve is the least important profit category in the finance office. Yes, we earn a portion of our total profit from reserve, **but it provides absolutely no benefit to the customer**….I've said it before, and I'll say it again: **[Dealer] reserve only benefits the lender and the dealer."**[9]

Arguments made during the roundtables that eliminating dealer markups will end financing through the dealer are specious. Dealers will still need to offer financing to sell cars, and finance sources will still seek to purchase auto finance paper from dealers. Dealers would still receive compensation for the work performed in the financing process. Instead, there would be a transparent system where car buyers:

- would know the exact costs of financing;
- could make an informed choice as to the value of arranging financing themselves or "hiring' the dealer to do it for them;
- would pay a similar price for obtaining financing through the dealer as their similarly-situated peers; and
- would benefit from incentives for the dealer to find the best interest rate available to the consumer.

THE FTC SHOULD BAN YO-YO SCAMS

We urge the FTC to find that yo-yo scams are an unfair and deceptive practice. We also ask the FTC to ban the use of spot delivery agreements unless the condition is related to something other than assignment of the finance contract and is not subject to the dealer's discretion.

Description of the Yo-Yo Scam

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. 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. Yo-yo scams are possible because of the

[9] Marv Eleazer, "The Great Rate Debate," *F&I Showroom News* (October 7, 2011).

pervasive practice of conditioning or purporting to condition finance contracts on the dealer's decision whether to accept the sale of the contract to a third-party loan purchaser.

Conditional sales agreements, spot deliveries and yo-yo scams are three different things. In a conditional sales agreement, there is an action that the consumer must take to complete the sale, such as arranging financing to purchase car from a source other than the dealer. In some states, the dealer is required to keep the car on its insurance policy and provide use of dealer license plates until the deal is completed and title is transferred to the buyer.[10]

A spot delivery occurs when the dealer allows the customer to drive off the lot with the car – "on the spot" – while the deal is not technically final.[11] The dealer asserts the right to cancel the deal if the dealer decides that none of the offers to purchase the financing contract are acceptable. Most consumers either believe that the deal is final or that the deal is as good as final. The dealer encourages the borrower to drive the car away before financing is final to remove the consumer from the marketplace. If the consumer leaves the lot thinking the contract is not final, the consumer may shop around and perhaps buy a car elsewhere.

In the yo-yo scam, the dealer allows the customer to leave the lot on a spot delivery but pulls the consumer back to the dealer like a yo-yo on a string. The consumer is then pressured to sign a new finance contract with worse terms for the consumer. It is the use of the spot delivery that allows for the yo-yo scam to occur. Spot deliveries are so pervasive that nearly every finance transaction with the dealer is a potential yo-yo scam. There are several causes that lead to yo-yo scams. In some cases, the dealer knows the chance exists that the originally-offered financing may not be available, because the third-party purchaser may send an offer with stipulations or conditions. For example, the purchaser may want more financial information from the consumer or the purchaser may require a larger down payment or a co-signer. In this situation, rather than take the risk that the consumer may shop elsewhere, the dealer sends the consumer home with the car and the conditions or stipulations unmet.

In other cases, the dealer does not have an offer to purchase the contract from a third-party and sends the consumer home hoping to sell the contract quickly. Perhaps the dealer knows it cannot deliver on the financing agreement but doesn't want to lose the consumer. Or, the dealer is dissatisfied with the terms potential loan purchasers have offered. Whatever the reason for entering into this type of transaction, the goal is the same. The dealer wants to make the consumer believe the deal is final so that the consumer does not purchase a car elsewhere or decide not to purchase at all.

In the typical yo-yo transaction that a dealer has claimed to cancel, the consumer is lured back to the dealership under one of several guises. When the customer returns to the

---

[10] See, e.g., N.C.G.S. 20-75.1.

[11] Shoals Ford, Inc. v. Clardy, 588 So.2d 879 (Ala. 1991).

dealer, the customer is presented with a new deal at a higher interest rate or with a larger down payment requirement in order to keep the car. Frequently, the dealer states that "the lender" has changed its mind and won't finance at the rate or with other terms promised.

When the dealer claims the ability to unilaterally cancel the transaction, the dealer can offer an interest rate that the dealer knows it may not be willing or able to actually provide without the risk of suffering a significant penalty. Instead, the dealer forces the consumer to either agree to a different interest rate or loan terms or return the car to the dealer.

Of further concern, many dealers claim the right to immediately repossess the vehicle when the dealer decides to cancel the deal. The dealer also claims the right to charge rental fees, fees for wear and tear, and for fees incurred to repossess the vehicle.

To further increase leverage on the consumer after the yo-yo string is pulled, the dealer may refuse to return the consumer's trade-in or the consumer's down payment. The dealer may also threaten to charge the consumer fees for use, wear and tear, or other items. In some cases, the dealer may threaten the consumer with prosecution for auto theft if the consumer does not immediately return the car to the dealer. Under this significant pressure, many consumers agree to the new terms.

Recommendation

We ask that the FTC find that yo-yo scams are an unfair and deceptive practice. We also ask the FTC to ban the use of spot delivery agreements unless the condition is related to something other than assignment of the finance contract or something in the sole discretion of the dealer.

These practices give the dealer an unfair bargaining position over the consumer and distort competition. If the dealer wants to ensure that the deal, as structured, will be to the dealer's liking or that all conditions from the subsequent purchaser can be met, then the dealer should not allow the customer to leave the lot with the car or allow the buyer to sign a retail installment sales contract. A credit contract should not be signed unless the dealer is prepared to honor the deal as agreed between the consumer and the dealer.

Several years ago, the Michigan Department of Commerce issued a letter stating that the practice of conditioning the retail installment sales contract upon future sale of the finance contract violates the Michigan Motor Vehicle Sales Act.[12] The logic outlined in that letter is clear and should apply universally – if the buyer signs a completed retail installment sales contract and leaves the lot with the car, then the dealer, who is the creditor on the contract, should have to stand by the terms of the contract.

[12] Letter of Murray Brown, Deputy Commissioner, Michigan Department of Commerce, found at http://www.michigan.gov/documents/cis_ofis_spotdel_24239_7.pdf.

Conditioning the consummation of the credit agreement on the dealer's sale of the credit contract places the onus on the consumer when it properly belongs to the dealer. A dealer engages in more auto financing transactions in a day or a week than the average consumer will in a lifetime. The dealer has the experience and the wherewithal to know what potential third-party purchasers will require, while the customer has no idea. The dealer should take the time to meet the conditions and stipulations of potential purchasers and to verify that the borrower's information is correct. Dealers should not be allowed to force consumers to fix the dealer's miscalculation or haste. Additionally, this protection will level the playing field by allowing dealers that take the time to ensure that the deal is final before delivering the car to the consumer to effectively compete in the marketplace.

THE FTC SHOULD CURB LOAN PACKING

We call on the FTC to require dealers to disclose the actual costs of every ancillary product sold during the financing process, disclose the cost of the car with and without ancillary products, and prohibit dealers from representing that purchase of ancillary products is required to obtain financing.

Background

Loan packing occurs when the dealer adds a number of ancillary products to the loan amount while hiding or misrepresenting the price, terms, or value of these products. This can happen when the products are sold in a package with a number of other items and the cost of these products is expressed as an increase in monthly payment. Loan packing can also occur when the consumer tells the dealer up front what the consumer considers an affordable monthly payment. The dealer structures the deal in such a way that the loan has the monthly payment the consumer stated but includes as many ancillary products and as much interest rate markup as possible to maximize the profit on the deal.

The sale of ancillary products, such as extended warranties, security systems, insurance products and the like is the main source of profit for the finance department outside of the dealer interest rate markup. These products are problematic for four reasons. First, these products are sold at a significant price markup, and may provide limited or no value to the customer. Second, the dizzying array of products provided to the consumer at the end of a long sales and financing process provides ample opportunity to sell customers on products that the consumer does not fully understand or have time to effectively compare to other products. Third, the sale of such add-ons contributes to negative equity and excessive debt because the cost is added to the sales price and financed into the loan the dealer is selling the customer. Fourth, the products siphon off money that could be spent to purchase a better vehicle.

The presentation of ancillary products is not consistent across the industry. Some dealers use a menu presentation that shows the different products, their cost, and the impact on the loan. Others sell ancillary products in packages that hide the full cost of the additional products. Consumers are often led to believe that purchasing these products is a requirement to obtain financing or to qualify for a particular interest rate.

Recommendation

The FTC has a long history of viewing loan packing as an unfair and deceptive practice, and state UDAP laws have similarly long been used to attack loan packing.[13] To reinforce this position, and encourage more widespread compliance than sporadic enforcement has achieved, we urge the FTC to promulgate a rule that provides consistency and curbs some of the worst abuses in selling ancillary products, including the following provisions:

- Require the use of a menu that shows both the actual price of the ancillary product and the impact on monthly payments;
- Require dealers to clearly and conspicuously disclose to the customer the full price of the car with and without the ancillary products;
- Require that consumers be informed at the beginning of the transaction about the products that will be offered at the end of the transaction; and
- Prohibit dealers from representing that ancillary products are a requirement for obtaining financing.

THE FTC SHOULD ADDRESS UNPAID LIENS ON TRADE-IN VEHICLES AND DEALER CLOSURES

We call on the FTC to require dealers to pay existing liens on trade-in vehicles, and take steps to assist consumers who are victim to unpaid liens on trade-in vehicles.

Background

When auto dealers go out of business, they often leave their customers in the lurch. While dealer closings have harmed consumers for decades, the current economic downturn spurred even greater dealer closings. Under the terms of the auto industry bailout, Chrysler closed 789 dealers while General Motors closed 1100 dealers, respectively. Dealers associated with other manufacturers and independent dealers also closed by the hundreds.

One of the risks when a dealership closes is that it will not pay off liens on trade-in vehicles. When a consumer trades-in a vehicle on which there is still an outstanding loan, the dealer promises to pay off the lien using a portion of the proceeds from the loan used to finance the vehicle the consumer is purchasing.[14] If the dealer does not follow through

---

[13] *See, e.g.* National Consumer Law Center, *The Cost of Credit* §§ 8.5.4, 8.7.4 n. 837 (4th Ed. 2009).

[14] For more information about the scope of negative equity and its impact on the auto market leading up to the market's collapse, see comments by Nobel Prize-winning economist Nouriel Roubini, posted at:

on this promise, the balance the consumer owed on the trade-in vehicle remains unpaid and there continues to be a lien on the vehicle.

The consumer who is driving the newly-purchased car is unaware the lien has not been paid on their old vehicle until the lender holding the lien on the car the consumer traded in notifies the consumer that the loan is in default. The consumer is now obliged to keep making the payments on their new loan, which is inflated due to the addition of the old loan into the new one, along with the loan the consumer thought was paid off. Often this is financially impossible and the consumer ends up losing the new vehicle. We have found that when dealerships closed, they have often left hundreds of consumers with unpaid liens on their trade-in vehicles.[15]

The problem of an unpaid lien turns leads to another abuse when the dealer then sells the trade-in vehicle to another consumer. This practice is called "car kiting," because the dealer is selling a car that the dealer does not own. The new consumer has no idea about the existence an outstanding lien on the vehicle he or she is buying and that the dealer is selling a vehicle it does not own. Typically, the consumer makes payments to the lender, only to have their vehicle repossessed by the former owner's lien holder. The result is that consumers lose their down payment, thousands of dollars worth of payments, and the car.

Car kiting is devastating to consumers because it ruins their credit, often causing them to lose their vehicles through no fault of their own. And, for many consumers, their car is their only way to get to work. For those consumers, the loss of a car can also mean the loss of their livelihoods. Consumers who are victimized by car kiting also tend to be responsible borrowers with good credit. Otherwise, they would not have qualified for another loan.

The negative impact is lasting, since repossessions remain on consumers' credit histories for seven years. Because employers commonly pull credit reports as a condition of employment, and landlords rely on credit reports to assess the viability of prospective

---

http://www.economonitor.com/nouriel/2008/05/04/negative-equity-in-auto-loans-and-the-bust-of-the-auto-bubble/

15 For data about the scope of the problem and specific examples, see the legislative analysis for California SB 729, sponsored by the California District Attorneys Association, establishing a restitution fund for victims of dealer closings, posted at: http://www.leginfo.ca.gov/pub/07-08/bill/sen/sb_0701-0750/sb_729_cfa_20070425_141418_sen_comm.html, legislative analysis for California SB 95 (Corbett, 2009), sponsored by Consumers for Auto Reliability and Safety, to require auto dealers to tender payment on liens before they transfer ownership of vehicles, or within 21 days. In addition to being supported by many consumer organizations, this measure also attracted supported from the California Bankers Association, California Credit Union League, Alliance of Auto Manufacturers, California Financial Services Association, Carmax, Alameda County District Attorneys Association, Los Angeles County District Attorneys Association, and California Statewide Law Enforcement Association.

tenants, the fallout from unpaid liens traps consumers in a cycle of debt and ruined credit that also becomes a barrier to employment and housing.

Among the other problems consumers encounter due to dealership closings:

- Consignment sales -- dealers sell the trade-in vehicles, then pocket the proceeds;

- Prepaid service plans or services -- dealers offer prepaid "lifetime" services, like free oil changes that are redeemable only at the dealership, then go out of business -- sometimes within a short period of time;

- Unfunded add-ons -- Dealers sell extended service contracts, "guaranteed asset protection" plans (GAP), roadside assistance, and other insurance or service-related add-ons, then keep the proceeds without passing through the payment or activating the policy;

- Vehicles Left for Service -- when the dealership closes, consumers are unable to access their cars.

Some states -- including Virginia, West Virginia, and California -- have established restitution funds for victims of dealer closings. More typical are states that require dealers to post bonds, which are usually in such small amounts that they are exhausted by the first few claims. Other states like Washington and Illinois have set up task forces including motor vehicle departments and/or state attorneys general.

Recommendation

We recommend that the FTC:

- Engage in rulemaking to require dealers to pay off liens on traded-in vehicles before they sell them, along the line of California's SB 95;

- Establish a task force with state attorneys general, district attorneys, and state motor vehicle departments to promptly identify victims, particularly those in the military, of dealership closings and work to mitigate the damage to consumers, helping restore their credit and enabling them to re-enter the auto market and either keep their jobs or find new ones;

- Publicly seek complaints from victims and take appropriate action, including enforcement efforts and referrals to the U.S. Department of Justice for criminal enforcement; and

- Work with states that have established restitution funds to help raise consumer awareness about the existence of the funds.

DATA COLLECTION

More publicly-available data would help to effectively monitor the auto lending market. In particular, data about dealer interest rate markups, even in the aggregate, would be illuminating. The FTC could collect data on the number of finance contracts that are renegotiated to further study the impact on consumers. And, data about the penetration rate of add-on products and which customers are most likely to purchase them would also help to determine whether additional scrutiny on those products is required. We would be glad to work with FTC to determine appropriate data to collect.

Conclusion

We thank the FTC for its attention to the issues related to auto financing. We urge the FTC to take action on these abuses, as they unnecessarily cost consumers billions of dollars each year and prevent transparency and fairness in this market.