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Chairman Green, Ranking Member Barr, and Members of the Subcommittee, my name is Kristen Clarke, and I am the President and Executive Director of the Lawyers' Committee for Civil Rights Under Law ("Lawyers' Committee"). Thank you for the opportunity to testify today about discrimination in the automobile loan industry.

The Lawyers' Committee is a national civil rights organization created at the request of President John F. Kennedy in 1963. President Kennedy sought to enlist the private bar's leadership and resources in combatting discrimination and the resulting inequalities across America. For the past five decades, the Lawyers' Committee has been on the front lines of the fight for equality in the areas of economic justice, voting rights, fair housing, criminal justice, education, hate crimes, and more.

Unchecked Auto Lending Discrimination Contributes to the Growing Racial Wealth Gap

Almost 55 years after the passage of the federal Civil Rights Act of 1964, a stark racial wealth divide remains—a typical white family has $140,500 in wealth, while a typical Black family has just $3,400.[1] Evidence and data make clear that abusive, predatory automobile lending and lack of access to equitable financial services are factors that contribute to the wealth gap that we are witnessing today. Eliminating lending discrimination, root and branch, particularly across the automobile industry, stands as a core civil rights priority today.

Wealth provides families a safety net when faced with job insecurity, relocation, or emergency situations. Our country's long history of segregation and institutional racism has prevented families of color from accessing affordable credit and building generational wealth. Research has shown that lenders wrongly correlate race with risk, leading consumers of color to have a harder time getting credit for major life purchases. And when they do get credit, it is more expensive.[2] Lending discrimination, including in the auto finance market, contributes to the economic instability of families of color and the widening racial wealth gap.

Americans need reliable transportation to get to work, school, and other essential places. Communities of color that are deprived of economic investment often lack effective public transportation.[3] Many who cannot rely on good public transportation systems need an affordable loan to get a car and to help them build good credit. In fact, most consumers need a loan to finance the purchase of a car.[4]

As the third-largest source of outstanding household debt after mortgages and student loans,[5] car loans and their impact on communities of color warrant the close and immediate attention of Congress. African Americans and other consumers of color face discrimination in various ways when purchasing and financing a car. Studies have shown that buyers of color face significant bias in the auto market and are often charged higher car prices, higher interest rates, and more expensive insurance on the basis of their race or ethnicity. They are also targeted for predatory sales and repossession schemes.

A significant portion of car buyers receive financing through car dealers.[6] Car dealers often sell financing contracts to indirect lenders, including banks or finance companies, for a fee. Indirect lenders compete for the financing contracts from the originating car dealers by allowing them to increase their interest or “buy” rate with a discretionary profit-generating dealer markup. According to the Consumer Financial Protection Board (CFPB), “markups can generate compensation for dealers while giving them the discretion to charge consumers different rates regardless of consumer creditworthiness.”[7] Many consumers are not aware that car dealers can tack on additional interest to their loan for the sole purpose of making a profit.

One of the most pernicious ways in which racial bias seeps into auto lending is through discretionary dealer markups. Indirect auto lenders often have no controls in place to prevent discretionary markup pricing disparities resulting from car dealers’ racial bias, resulting in people of color being burdened with more expensive car loans than white consumers.[8] Widespread racial discrimination in indirect auto lending is not new and has been well documented over the past thirty years. In 1991, Professor Ian Ayres found that Black male consumers in Chicago were asked to pay more than two times the markup of white male consumers.[9] In 2012, a similar study out of Vanderbilt University by Mark Cohen analyzed more than 1.5 million GMAC car loans between 1999 and 2003, and found that Black borrowers paid on average $362 more than white borrowers in extra interest over the life of the car loan. Despite only representing 8.5 percent of all borrowers, Black borrowers paid nearly 20 percent of the $422 million in subjective markups.[10] And in 2015, the National Consumer Law Center released compelling data from indirect auto lending litigation spanning from the late 1990s to the early 2000s evidencing that African Americans were subjected to “statistically significant racial disparities” in “every state with sufficient data and in every region of the country.”[11]

<u>Federal Investigations and Enforcement Activity Must Play a Central Role in Combatting Ongoing Lending Discrimination Across the Automobile Industry</u>

Under the prior Administration, the CFPB and the Department of Justice (DOJ) prioritized rooting out auto lending discrimination. Congress formed the CFPB as an independent agency under the Dodd-Frank Act in 2010 after the recession for precisely this reason—to protect vulnerable communities, including communities of color, from predatory financial practices, and to push the financial market towards equity. In 2013, the CFPB issued important guidance making clear that as creditors under the Equal Credit Opportunity Act (ECOA), indirect auto lenders may be liable for discrimination resulting from dealers’ discretionary markups. The guidance provided auto lenders with recommendations on how to ensure compliance with fair lending laws, including ECOA, that prohibit discrimination on the basis of race and other protected categories. [12]

In December 2012, DOJ and CFPB entered into an agreement to facilitate coordination on fair lending enforcement. Under the agreement, CFPB referred matters to DOJ when CFPB had reason to believe there was a pattern or practice of lending discrimination. CFPB and DOJ investigated and entered into substantial monetary agreements with some of the largest indirect auto lenders in the United States to resolve allegations that they had violated ECOA by charging borrowers of color higher dealer markups on the basis of their race and/or ethnicity.[13] The various settlements entered into by the CFPB and DOJ, which recovered more than **$140 million** in restitution for thousands of borrowers of color, demonstrate the extent to which discrimination pervades auto lending practices.

In 2013, Ally Financial and Ally Bank entered into a settlement agreement for $80 million in damages for borrowers of color and $18 million in penalties, making it the largest auto loan discrimination settlement.[14] More than 235,000 borrowers of color paid higher interest rates for car loans between April 2011 and December 2013.[15] Data showed that 100,000 African Americans were charged approximately 29 basis points more in dealer markup than whites and were obligated to pay on average over $300 more in interest than white borrowers over the life of the loan.[16] 125,000 Hispanics were charged approximately 20 basis points more than whites, paying on average more than $200 in additional interest over white borrowers.[17] Similarly, 10,000 Asians were charged approximately 22 basis points more in dealer markup than whites and paid on average more than $200 in additional interest.[18] The settlement gave Ally the option to substantially reduce dealer markup discretion or to eliminate it all together.[19] If, however, Ally allowed dealers to continue adding discretionary markups, then Ally had to provide education to dealers, conduct portfolio-wide analyses, and undertake prompt corrective action against dealers when racial disparities arose.[20]

In July 2015, DOJ and CFPB entered into a settlement with Honda Finance for $24 million in restitution for borrowers of color.[21] Honda charged African-American borrowers 36 more points than whites in dealer markups, forcing African-American borrowers to pay $250 more in interest over the life of the loan.[22] Hispanic borrowers were charged 28 more points in dealer markups than whites and paid $200 more in interest.[23] Asians were charged 25 points more in dealer markups than whites and paid $150 more in interest.[24] CFPB and DOJ found that Honda was not monitoring whether discrimination was occurring across its portfolio of retail installment contracts, which were allowed to charge markups, and they did not employ adequate controls to prevent discrimination.[25] The settlement gave Honda the option to substantially reduce discretion or to eliminate it all together.[26]

In September 2015, CFPB and DOJ entered into an $18 million settlement with Fifth Third Bank.[27] In this case, Fifth Third Bank charged African-American and Hispanic borrowers, on average, $200 more for their car loans.[28] Fifth Third Bank was also required to either substantially reduce the amount by which loans could be marked up or to eliminate discretion altogether.[29]

Most recently, in February 2016, CFPB and DOJ entered into a settlement with Toyota Motor Credit.[30] The settlement required that Toyota create a $21.9 million restitution fund for African American and Asian borrowers.[31] Toyota charged African-American borrowers, on average, over $200 more for their car loans and charged Asian borrowers, on average, over $100 more in interest.[32] Toyota was required to either substantially reduce the amount by which loans can be marked up or eliminate discretion altogether.[33]

In each of the indirect lending investigations, the retail installment contracts analyzed by CFPB and DOJ did not contain information on the race or national origin of borrowers. To evaluate differences in dealer markup, the CFPB and DOJ assigned race and national origin probabilities to applicants. CFPB and DOJ employed a proxy methodology that combined geography-based and name-based probabilities, based on public data published by Census Bureau, to form a joint probability using the Bayesian Improved Surname Geocoding ("BISG") method. The joint race and national origin probabilities obtained through BISG was then used directly in the CFPB's and DOJ's models to estimate disparities in dealer markup on the basis of race or national origin.[34]

In addition to its actions against indirect lenders, DOJ partnered with the North Carolina Attorney General to reach a deal with two North Carolina "buy here, pay here" used car dealerships that intentionally targeted African-American customers for unfair and predatory credit and repossession practices.[35] Reverse redlining is the practice of intentionally targeting African Americans for the extension and servicing of credit on unfair and predatory terms without meaningfully assessing the customers' creditworthiness.[36] The suit alleged that two "buy here pay here" used car dealerships in Charlotte, North Carolina, had sales prices, down payments, and interest rates that were disproportionately high compared to other subprime used car dealers.[37] The suit further alleged that the dealerships were not engaging in a meaningful assessment of the consumers' creditworthiness or ability to repay, causing their default and repossession rates to be disproportionately high.[38] There were also claims that the dealerships engaged in predatory repossession tactics when customers were not even in default.[39] The dealers agreed to reform their practices and to pay $225,000 in restitution to the impacted consumers.

This administration, however, has turned a blind eye to auto lending discrimination even though continuing research shows that it is an ongoing problem. A 2018 study by the National Fair Housing Alliance using matched pair testers in Virginia showed that almost 63 percent of the time, borrowers of color received costlier auto loans even though they were *more* qualified than their white counterparts and that the borrowers of color would have paid an average of $2,351 more over the life of the loan as a result of the discrimination.[40]

Under the Trump administration, DOJ has retreated from fair lending enforcement against auto lenders. The CFPB has also stopped bringing enforcement actions against auto lenders engaging in discriminatory practices. In addition to defanging the enforcement authority of the Office of Fair Lending and Opportunity,[41] the administration rescinded the 2013 CFPB guidance encouraging indirect auto lenders to proactively comply with ECOA.[42] Not surprisingly, several lenders who had previously implemented flat fee models in response to the CFPB's guidance have reverted back to discretionary dealer rate programs.[43]

Congress Must Reject Impending Attacks on Disparate Impact Liability

Since the beginning of the Trump administration, the CFPB has made clear its goal to attack disparate impact liability as a method of proving and establishing an ECOA violation. For example, during his tenure as the Director of the CFPB, Mick Mulvaney released a statement maintaining that the CFPB would be reexamining the requirements of the ECOA, including disparate impact.[44] Since she has replaced Mulvaney, Director Kathleen Kraninger has stated to the Senate Banking Committee that the CFPB is currently studying whether disparate impact should be used to prove discrimination.[45] This move would be devastating for those who seek to hold lenders accountable, taking away one of the CFPB's most powerful enforcement tools for ensuring fair lending. Therefore, Congress must take this opportunity to make clear that it intends to protect disparate impact liability as a way to root out discrimination.

Congressional Response to Modern Day Auto Lending Discrimination

This administration's lack of enforcement will continue to result in auto lenders prioritizing profit over equality and nondiscrimination. Therefore, we ask Congress to enact robust legislation to increase protections for borrowers of color in the auto lending market. Legislative proposals considered by Congress should either prohibit or significantly limit discretionary dealer markups. To the extent dealer markups are allowed, auto dealers and lenders must be required to disclose important credit terms, including dealer markups, to borrowers earlier in the car buying process, not after the credit transaction is finalized, as currently required by the Truth in Lending Act.

Furthermore, Congress should use its extensive oversight authority over the Justice Department's Civil Rights Division and CFPB to understand the significant downturn in their enforcement activity in this area. The U.S. Justice Department has significant resources and unique expertise in this area. The retreat of our federal government has led to the resurgence of discriminatory and predatory lending practices, as evidenced by lenders who are reverting back to discretionary pricing schemes. Such a lack of enforcement allows discriminatory practices to continue without recourse, deepening the harm to African Americans, Latinos, and other borrowers of color, and weakening civil rights laws.

Congress should also consider action that would require auto lenders to report borrower demographic information, including race and ethnicity, in connection with its loans to facilitate fair lending analysis and enforcement. The Home Mortgage Disclosure Act (HMDA), which requires mortgage lenders to collect, report, and publicly disclose borrower demographic data, provides a model to guide reform. HMDA requires nearly all mortgage lenders to report detailed information on the mortgage applications they receive, and whether they originate the loan.[46] HMDA is enforced by the Office of the Comptroller of the Currency ("OCC") and administrative sanctions, including civil money penalties, may be imposed by the OCC for noncompliance.[47] Only very small lenders, or those operating exclusively in rural areas, are exempt from HMDA reporting.[48] HMDA data include each applicant's requested loan size, income, race, and ethnicity, as well as information on the purpose of the loan (purchase, refinancing, improvement), any co-applicants, and the loan's priority (first or second lien).[49] The census tract location of the property is also reported.[50] Because of its robust collection, HMDA data facilitates the straightforward identification of discriminatory patterns and practices by lenders engaged in conduct that unquestionably harms consumers along lines of race.

Borrowers of color deserve to participate in the marketplace free from discrimination. Yet, they face extensive hurdles in gaining fair and equal access to auto lending credit which further threatens economic mobility and progress. In the absence of the CFPB and DOJ undertaking enforcement action to protect African Americans and other borrowers of color from discrimination in auto lending, we urge legislators to prioritize this issue by enacting legislation that will hold auto lenders accountable and further strengthen existing protections under ECOA.

Conclusion

Discriminatory auto lending poses grave financial danger to African American, Latino and other vulnerable consumers. Increasingly, lenders are taking advantage of a highly unregulated and unmonitored market to promote discriminatory and predatory practices. We thank this committee for sounding an alarm about this aspect of the auto loan market and for undertaking careful fact-finding to identify appropriate remedial responses. We urge Congress to fully leverage its investigative, oversight and law-making powers to safeguard the rights of our nation's most vulnerable consumers, to hold predatory auto lenders accountable and to ensure that our federal agencies are carrying out their role and responsibility in enforcing the law.

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[1]Emanuel Nieves and Dedrick Asante-Muhammad, *Running in Place: Why the Racial Wealth Divide Keeps Black and Latino Families from Achieving Economic Security* (Washington, DC: Prosperity Now, 2018), 5.
[2] Angela Hanks, Danyelle Solomon and Christian E. Weller, *Systemic Inequality: How America's Structural Racism Helped Create the Black-White Wealth Gap*, Center for American Process (Feb. 21, 2018),

https://www.americanprogress.org/issues/race/reports/2018/02/21/447051/systematic-inequality/ (Last Accessed April 29, 2019).

[3] Lisa Rice and Erich Schwartz, Jr., *Discrimination When Buying a Car: How the Color of Your Skin Can Affect Your Car-Shopping Experience* (Washington, DC: National Fair Housing Alliance, 2018), 9.

[4] *Id*, 6.

[5] *Id.*

[6] *Id.*

[7] *See generally* CFPB press releases announcing agreements with Ally Financial Inc., Honda Finance Corporation, Toyota Motor Credit, and Fifth Third Bank. Available at www.cfpb.gov.

[8] *Id.*

[9] *See* Jason Hernandez, *Loan Discrimination At the Auto Dealership: Current Cases, Strategies and the Case For Intervention By Attorneys General*, Columbia University, https://web.law.columbia.edu/sites/default/files/microsites/career-services/Loan%20Discrimination%20At%20The%20Auto%20Dealership.pdf.

[10] *Id.*

[11] "Racial Disparities in Auto Loan Markups State-by-State Data," National Consumer Law Center, June 2015.

[12] Indirect Auto Lending and Compliance with ECOA, CFPB Bulleting 2013-02, Mar. 21, 2013 *available at* https://files.consumerfinance.gov/f/201303_cfpb_march_-Auto-Finance-Bulletin.pdf.

[13] *Supra* note 7. Ally Financial, Honda Finance, Toyota Motor Credit and Fifth Third Bank agreed to limit the amount of their dealer markups and collectively paid over $140 million in restitution for thousands of borrowers of color.

[14] Consumer Fin. Prot. Bureau, *CFPB and DOJ Order Ally to Pay $80 Million to Consumers Harmed by Discriminatory Auto Loan Pricing*, (Dec. 20, 2013) https://www.consumerfinance.gov/about-us/newsroom/cfpb-and-doj-order-ally-to-pay-80-million-to-consumers-harmed-by-discriminatory-auto-loan-pricing/ (Last Accessed April 29, 2019).

[15] *Id*.

[16] *Id*.

[17] *Id*.

[18] *Id*.

[19] *Id*.

[20] *Id*.

[21] Consumer Fin. Prot. Bureau, *CFPB and DOJ Reach Resolution with Honda to Address Discriminatory Auto Loan Pricing*, (Jul. 14, 2015), https://www.consumerfinance.gov/about-us/newsroom/cfpb-and-doj-reach-resolution-with-honda-to-address-discriminatory-auto-loan-pricing/ (Last Accessed April 29, 2019). *See Also* Dept. of Justice, *Justice Department and Consumer Financial Protection Bureau Reach Groundbreaking Settlement to Resolve Allegations of Auto Lending Discrimination by Honda*, (Jul. 14, 2015), https://www.justice.gov/opa/pr/justice-department-and-consumer-financial-protection-bureau-reach-groundbreaking-settlement (Last Accessed April 29, 2019).

[22] *Id*.

[23] *Id*.

[24] *Id*.

[25] *Id*.

[26] *Id*.

[27] Consumer Fin. Prot. Bureau, *CFPB Takes Action Against Fifth Third Bank for Auto-Lending Discrimination and Illegal Credit Card Practices*, (Sept. 28, 2015) https://www.consumerfinance.gov/about-us/newsroom/cfpb-takes-action-against-fifth-third-bank-for-auto-lending-discrimination-and-illegal-credit-card-practices/ (Last Accessed April 29, 2019).

[28] *Id*.

[29] *Id*.

[30] Consumer Fin. Prot. Bureau, *CFPB and DOJ Reach Resolution With Toyota Motor Credit To Address Loan Pricing Policies With Discriminatory Effects*, (Feb. 2, 2016) https://www.consumerfinance.gov/about-us/newsroom/cfpb-and-doj-reach-resolution-with-toyota-motor-credit-to-address-loan-pricing-policies-with-discriminatory-effects/ (Last Accessed April 29, 2019).

[31] *Id*.

[32] *Id*.

[33] *Id*.

[34] *See, e.g.*, https://files.consumerfinance.gov/f/201602_cfpb_consent-order-toyota-motor-credit-corporation.pdf.
[35] Dept. of Justice, *U.S. Justice Department and North Carolina Attorney General Reach Settlement to Resolve Allegations of Auto Lending Discrimination by "Buy Here, Pay Here" Used-Car Dealerships*, (Feb. 10, 2015), https://www.justice.gov/opa/pr/us-justice-department-and-north-carolina-attorney-general-reach-settlement-resolve (Last Accessed April 29, 2019).
[36] *Id*.
[37] *Id*.
[38] *Id*.
[39] *Id*.
[40] *Supra* note 3, at 5.
[41] Makada Henry-Nickie, *On Fair Lending, Mulvaney's Actions at CFPB Speak Louder than His Words*, (Washington, DC: Brookings Institution, 2018). *Available at* https://www.brookings.edu/research/on-fair-lending-mulvaneys-actions-at-cfpb-speak-louder-than-his-words/.
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[48] Alexander W. Butler, Erik J. Mayer, and James P. Weston, *Discrimination in the Auto Loan Market* (Feb. 6, 2019).
[49] *Id.*
[50] *Id.*