Consumer Financial Protection Bureau

June 20, 2013

The Honorable Terri Sewell
U.S. House of Representatives
1133 Longworth House Office Building
Washington, DC 20515

Dear Representative Sewell,

Thank you for your May 28, 2013 letter about indirect auto lenders' lending practices and compliance with anti-discrimination laws, such as the Equal Credit Opportunity Act (ECOA). The Consumer Financial Protection Bureau (Bureau) shares your commitment to ensuring that lending practices are fair and equitable and that credit markets function competitively and efficiently for all consumers and honest businesses. We appreciate the opportunity to work with you on these important goals.

As you note in your letter, consumers must be able to shop for credit without fear of discriminatory practices. For that reason, the Bureau takes very seriously its duty to address discrimination across the consumer credit industry, including indirect auto lending by depository and nonbank institutions. Certain policies and practices that allow discretion in pricing can create a significant risk of discrimination on the basis of race, national origin, and other prohibited bases such as sex. Historically, the failure to properly or consistently monitor such policies and practices for compliance with anti-discrimination laws has been a contributing factor in discrimination, both in auto lending and in other product markets like mortgages.

ECOA makes it illegal for a "creditor" to discriminate in any aspect of a credit transaction because of race, color, religion, national origin, sex, marital status, age, receipt of income from any public assistance program, or the exercise, in good faith, of a right under the Consumer Credit Protection Act. As you may know, we published CFPB Bulletin 2013-02, Indirect Auto Lending and Compliance with ECOA, on March 21, 2013 (Bulletin).[1] The Bulletin explains that the standard practices of indirect auto lenders likely make them "creditors" under ECOA and that a lender's discretionary markup and compensation policies may alone be sufficient to trigger liability under ECOA if the lender regularly participates in a credit decision and its policies result in discrimination. By describing the relevant laws and regulations that apply to indirect auto lending, the Bulletin aims to help indirect lenders recognize and mitigate the risk of discrimination resulting from discretionary dealer markup and compensation policies.

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

In your letter, you also requested background information about the Bureau's investigation into alleged practices within the auto lending industry. In the Dodd Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank), Congress gave the Bureau the authority to supervise depository institutions with more than $10 billion in assets and their affiliates, and certain nonbank financial institutions that provide consumer financial products and services, including mortgage, payday, and student lending. The Bureau supervises for compliance with ECOA, which includes coverage of indirect auto lending.

The Bureau's ongoing supervision of depository institutions and their affiliates currently includes examinations of ECOA compliance in indirect auto lending. Subject to certain exceptions, the Bureau has enforcement authority over both banks and nonbanks in the auto lending market, and it will use that authority wherever appropriate to address discrimination. As required by Congress, the Bureau's fair lending rules similarly apply to both banks and nonbanks. The Bureau's combination of rulemaking, supervision, and enforcement authorities allows the Bureau to promote a level playing field throughout the indirect auto lending market, including both banks and nonbanks as Congress intended.

Your letter also inquired about the methodology that we use in determining whether fair lending violations exist within the auto market. Our agency is committed to being open and transparent in all appropriate circumstances, including in our review of indirect auto lending.

The evaluation of whether an indirect auto lender is in compliance with ECOA requires multiple steps. A typical fair lending examination of an indirect auto lender would include a review of credit denials, interest rates quoted by the lender to the dealer (called "buy rates"), and any discretionary mark-up of the buy rate by the dealer (the interest rate quoted by the dealer to the consumer minus the "buy rate").

Determining whether discrimination has occurred is a case-specific and fact-intensive inquiry. The Bureau is accordingly evaluating possible discrimination in both auto lending and in other markets on a case-by-case basis. Our analysis considers appropriate analytical controls in reviewing data to determine whether a specific policy results in unlawful differences on a prohibited basis.

While fair lending analyses of mortgage lending are simplified by the availability of lender data reported under the Home Mortgage Disclosure Act, this is not the case with indirect auto lending. Information on race, ethnicity, and gender is typically not collected as part of an auto lending transaction. Therefore, the Bureau uses a proxy methodology to differentiate among consumers based upon these characteristics. The concept of using proxies for unavailable data is a widely accepted mathematical and statistical approach used across many disciplines, including, to our understanding, by the auto industry itself for marketing purposes. Various proxy methodologies are publicly available and have been used for decades in a number of different Civil Rights contexts, including voting rights cases, Title VII cases, and constitutional challenges, including jury selection and equal protection matters. In keeping with our commitment to transparency, the Bureau has previously indicated that when we utilize proxy data, we use both surnames and geographic location. The Bureau conducts its proxy analysis by using publicly available data from the Social Security Administration and the Census Bureau. We understand that many responsible lenders regularly use proxies in their own fair lending analyses where self-reported race, ethnicity, and gender data are unavailable. The Bureau has encouraged lenders who are not currently doing so to select a reasonable proxy method and to monitor their data for fair lending risk.

In the course of the Bureau's supervisory work, we have found frequent instances where lenders had robust fair lending compliance programs for mortgage lending, but weak or non-existent fair lending compliance programs for other types of consumer lending. As the Bulletin states, lenders may choose to address the risk of discrimination resulting from certain markup and compensation policies in a variety of ways, including: imposing controls on dealer markup and compensation policies; or revising these policies to address unexplained pricing disparities on a prohibited basis; or eliminating dealer discretion to mark up buy rates and fairly compensating dealers using another mechanism that does not result in discrimination. For all lenders, the Bulletin also emphasizes the need for self-monitoring as a tool to address fair lending risk. It contains additional suggestions for monitoring and corrective action to mitigate that risk, including regular analyses to determine whether there are pricing disparities on a prohibited basis across the indirect auto lender's overall portfolio or at the individual dealer level. If differences are found, those analyses may help lenders understand the cause of the disparities as well as potential solutions.

Thank you for bringing your concerns to the Bureau's attention and for the opportunity to respond. We look forward to working with you on this important issue of economic fairness as we continue to work to ensure a more level playing field for consumers and businesses alike.

Sincerely,

Richard

Richard Cordray
Director

Thank you for your continuing interest in our work –
Rich

cc: The Honorable David Scott
The Honorable Joyce Beatty
The Honorable Daniel Kildee
The Honorable Lacy Clay
The Honorable Patrick Murphy
The Honorable John Delaney
The Honorable Gary Peters
The Honorable Bill Foster
The Honorable Ed Perlmutter
The Honorable Denny Heck
The Honorable Kyrsten Sinema
The Honorable Gregory Meeks