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Memorandum of Support

New York must cap interest rates in auto retail installment contracts so working families can own reliable, affordable cars

A.7585 (Zebrowski)/S.5947 (Sanders)

"An act to amend the personal property law, in relation to limiting the amount of certain credit service charges in motor vehicle retail installment contracts."

Empire Justice Center strongly supports A.7585 (Zebrowski)/S.5947 (Sanders) because it will cap interest rates in auto retail installment contracts, reducing the ability of auto dealers to impose extremely costly and often unaffordable credit terms on low-income New Yorkers when they purchase new or used vehicles. The proposed cap is one reform that would help curb abusive practices in the subprime auto lending market.

A car is one of the largest assets that a typical person will ever own, second only to a home. In areas without extensive, reliable public transportation, like upstate New York and rural areas, a consumer must have a car in order to get or keep a job, attend medical and other appointments, and fulfill family responsibilities. Most people who buy cars take out loans to do so, often directly from the dealer (retail installment contracts). Over a quarter of all car loans are subprime loans, made to borrowers considered to be risky based on their credit history. Subprime borrowers are often desperate to obtain financing to purchase a vehicle.

In Rochester New York, Empire Justice Center staff members have heard from local consumer advocates that communities of color are targeted for disparate pricing of subprime loans for used cars. Borrowers of color, with the same credit scores as their white counterparts, pay higher interest rates, even when debt to income and other characteristics of the borrowers and the loan are the same.

Subprime car loans routinely reach interest rates as high as 24.99%, just under New York's criminal usury cap. At rates that high, consumers can end up paying more in interest than the cost of the car. With the most expensive loans being made to the people least able to afford them, the default rates on these subprime car loans are especially high. Car loan defaults are currently reaching record numbers. Almost 10% of subprime loans are in default, compared to the overall default rate for all car loans of around 1%. Buy Here, Pay Here dealerships, which focus particularly on the subprime market, have default rates of around 25%. As a result of these high-cost loans leading to high default rates, the same often defective used cars are repeatedly repossessed and flipped, with the sellers pocketing consumers' down payments and trade-ins and even suing the consumers for the unpaid loan balance while meanwhile reselling the car and beginning the cycle again with a new consumer. The repossessions appear on consumers' credit reports, making it even more difficult for them to obtain reasonably priced credit.

New York has been a leader among states in consumer protections against abusive financial services and products, prohibiting predatory mortgages, high-cost check-cashing, and payday lending. In particular, New York has long had among the country's strictest usury laws, imposing a 16% civil cap on interest rates. As a result, New York consumers have been protected from abusive products such as payday loans, which enmesh consumers in an inescapable cycle of debt. Unfortunately, New York law lags when it comes to protecting consumers when they purchase cars on credit, because here practices have been allowed to flourish that can result in a similarly inescapable debt cycle.

Although New York courts have exempted most car loans from New York's general civil usury cap based on an archaic rule called the "time price doctrine," for decades the Legislature protected New Yorkers from predatory, high-cost lending by including interest-rate caps directly in the Motor Vehicle Retail Installment Sales Act. Those caps were removed in 1994 as part of an omnibus financial deregulation package, leaving the less protective 25% criminal usury rate as the only limit on these loans. Until the repeal in 1994, New York imposed caps of 7% on new car financing and up to 13% for used car loans.

A.7585/S.5947 would restore the balance that existed for decades before the 1994 financial deregulation by reinserting interest-rate caps directly into the Motor Vehicle Retail Installment Sales Act and subjecting car loans to the already high enough 16% rate that applies to other New York lending. Therefore, Empire Justice supports this bill.

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