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The Impact of Restricted Creditors' Remedies on Automobile Finance Companies in Wisconsin

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Synopsis

This paper studies the impact of the Wisconsin Consumer Act (which has creditor remedy restrictions that closely parallel those of the proposed FTC Trade Regulation Rule) on automobile finance company operations in Wisconsin. The data employed in the study were collected from major automobile finance companies operating in Wisconsin. For control purposes, equivalent data were also collected for Minnesota and the nation as a whole. To protect confidentiality, companies were identified only by numbers, not names.

Analysis of the data collected indicates that subsequent to passage of the WCA, automobile finance companies (in the aggregate) experienced increased delinquency rates and credit losses. As a result, at one company (#2), credit became less readily available, down payment requirements rose and a lower proportion of long-maturity new car loan contracts were granted. A second company (#3) noted that the percentage of total loans acquired from the highest-risk class of customers fell by 2/3's after passage of the WCA, and their down payment ratios tended to be somewhat higher in Wisconsin than elsewhere--even though they had made no conscious effort to restrict credit availability. Possibly, greater caution at the dealer or loan officer level accounted for this result. Like the others, the third company (#1) also indicated that it had adopted no conscious policy of restricting credit in Wisconsin. However, possibly because of credit restraint at the dealer level, its down payment requirements appeared to be somewhat higher in Wisconsin than elsewhere, and its loan maturities and application acceptance rates were more restrictive than in Minnesota.

Overall, in response to their elevated delinquency and loss experiences, all three companies appeared to engage in some implicit or explicit credit rationing to the riskiest class of borrowers (as marginal risk borrowers are likely to be least likely to be able to meet elevated down payment requirements). Because high-risk credit applicants make up only a small fraction of the market, total credit rationing may have been limited to a relatively small percentage of the total population.

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I. Overview

In 1973, enactment of the Wisconsin Consumer Act severely restricted remedies available to creditors in Wisconsin in the event of default on consumer debts. Such restrictions might theoretically be expected to have some impact on credit rates, terms, or the availability of credit to (relatively high-risk) consumers.

In general, one would expect that restrictions on creditors' abilities to collect on delinquent or defaulted debts would tend to:

- (i) raise creditors' collection costs and losses (unless credit standards were raised sufficiently to compensate by reducing defaults),
- (ii) reduce debt collection efficiency at each stage of default (which implies elevated conditional probabilities for 30-day delinquent accounts becoming more serious delinquencies, charge offs, or repossessions, and reduced possibilities for recovery subsequent to charge-off and repossession), and
- (iii) decrease repossessions by raising the cost of repossessions and/or decreasing their expected net yield.

In response to these effects from restrictions on creditors' remedies, one would expect creditors in states with restrictive remedies to adopt one or more of the following policies:

- (iv) attempt to reduce their potential credit costs or losses by spending more on applicant investigation and decreasing the availability of credit to riskier applicants, (ii) increasing down payments to reduce the likelihood of default and provide greater security in that event, (iii) limit maturities to reduce the period during which some or all of their outstanding credits are at risk, (iv) increase borrower life or health insurance coverage requirements to reduce risk (or, possibly, increase revenues from insurance commissions),
- (v) increase the finance rate which they charge to compensate for increased collection costs and losses, or
- (vi) raise the price of goods sold on credit to compensate for increased credit costs or losses.

By studying in detail the response of major automobile finance companies to creditor remedy restrictions in Wisconsin, this study attempts to determine which if any, of the hypothesized creditor reactions to remedy restrictions actually occurred.

II. Data Collection

Survey design:

An attempt was made to identify states with the most restrictive creditors' remedies. When asked, auto finance company executives identified Wisconsin and Massachusetts as the states with the most restrictive remedies, but Washington and West Virginia were also mentioned.

Each of the states with highly restrictive remedies was matched with similar, contiguous states with less restrictive remedies. Then a questionnaire was designed, shown as Exhibit A, to determine if restrictive remedies induced companies to alter their behavior in any of the ways posited above. In particular, the questionnaire attempted to gather data for both new cars and used cars (of various ages) on creditor delinquency

and loss rates, application rejection rates, down payment and maturity requirements, and creditor and customer finance rates. It also attempted to gather information on credit insurance coverage and the degree to which purchased automobile credit contracts were covered by dealer recourse or repurchase agreements (that required dealers to assume part or all of the risk associated with potential defaults on the contracts).

The three major automobile finance companies were asked to complete the questionnaire with data available through August 31, 1975. Each complied as well as it could, even though it was costly for them to prepare the requested data.

Data Availability and Comparability:

Unfortunately, each company keeps its records in a different way, and they all collect data through regional offices, which are not strictly delimited on a state-by-state basis. Thus some of the data they supplied were not readily usable.

In particular, data on dealer recourse and repurchase agreements were not useful because these agreements are negotiated by individual dealers, and dealer bargaining power depends on such factors as location and sales levels. Thus, in some companies, possibly because of high sales, urban dealers are less likely to have such agreements.

Reported data on credit life and health insurance were not very useful as they reflected only insurance acquired through the auto finance companies' insurance affiliates, not credit insurance written by dealers with other carriers, and insurance market penetration by the companies' insurance affiliates varies among states and dealers.

Also, methods of compiling data on rejected applications varied among companies. For instance, one company kept a record only of rejections on tentative loans "called-in" by dealers (and some potential borrowers might file several applications at once while other applications might not be called-in in advance). Another company kept records only of the proportion of loan applications that were rejected outright, but not the proportion that were rejected because the conditions required of the borrower before acceptance of the contract were not met. Additionally, no company was able to provide details on insurance coverage and application rejection rates for all ages of used cars. Data were either available for all cars or for all new and all used car contracts only.

Moreover, data on loan-to-value ratios and contract rejection rates were uniformly available only for all-new and all-used cars. However, one company provided complete data for late-model and old-model used cars, and all but one company provided loan-to-value ratio data for all requested subcategories of used cars.

Finally the companies were not generally able to provide the data requested for each of the indicated states. The main problem arose from the fact that they accumulate data in regional offices that may serve more than one state. Thus, some companies had no data available for certain states such as Rhode Island, and the data obtained from offices in one state partially applied to loans originated in another state.

Because of problems posed by data non-comparability, the analysis of auto finance company data was primarily restricted to a company-by-company analysis. In addition, because of limitations in the usefulness of various¹ state data, the analysis was focused on Wisconsin.

¹ In particular, data on Rhode Island were often clustered with Massachusetts data so it was not possible to compare those two geographically contiguous states; data on West Virginia were not found useful because severe restrictions on creditors' remedies

The analytical focus on Wisconsin was deemed appropriate, not only because of data availability, but also because the Wisconsin Consumer Act (WCA) most closely parallels the proposed FTC Creditor Remedy Trade Regulation Rule. Based on available questionnaire data, comparisons were made between loan terms and credit availability in Wisconsin both with the nation as a whole and with a similar geographically contiguous state, Minnesota. In addition, because one of the auto finance companies voluntarily provided extensive historical information on its Wisconsin lending activities, both before and after passage of the Wisconsin Consumer Act, an attempt was made to obtain similar data from the other two companies. One was able to comply with that request.

Measurement Problems

Before proceeding to an analysis of the data, it should be noted that there are four major reasons that it theoretically may be difficult to measure responses by automobile finance companies to reductions in their remedies. First, a creditor operating in more than one state may not attempt to recoup increased operating costs or losses resulting from restricted creditors' remedies in one state by altering his policies in only that state. While risk-reduction policies would most likely be concentrated in that state (where they would yield the greatest potential return), rate or price increases designed to recoup extra operating expenses or losses might apply nationwide. In addition, when a creditor has national operating policies and procedures, the cost of adjusting these to individual jurisdictions may not be justified.

Second, different creditors respond to reduced remedies in different ways. Thus, a uniform response of creditors to reduced remedies is not to be expected.

Third, part or all of the potential increase in collection costs or losses of automobile finance companies may be passed on to dealers through dealer recourse or repurchase agreement, or through changes in the dealer rate spread (the difference between the finance rate paid by the customer and the finance rate earned by the finance company on the purchased contract). Nonetheless, dealers in turn, can adjust to remedy-induced changes in their net revenues by either increasing the prices of their automobiles and associated services (such as maintenance charges) or (in the event they are liable under recourse or repurchase agreements) raising down payments, shortening maturities, or eliminating credit to high-risk applicants. Not all of these policies may be apparent unless dealers are surveyed directly.

Finally, responses by automobile finance companies and dealers to reduce risk would tend to be concentrated in states with expensive collection costs and/or high losses per bad account--most likely those states with restrictive creditors' remedies. They would also be concentrated on the highest risk forms of credit--such as used automobiles, particularly older model used automobiles where down payments are typically low because borrowers have little cash and, probably, limited abilities to repay their debts. Thus, much of the creditor response to remedy reduction, insofar as it occurs, may fall on a relatively small segment -- the high-risk segment -of the market. If one looks only at aggregate figures, he may underestimate the true impact of remedy reductions on that segment of the market.

Analysis of Empirical Data

The analysis that follows is based primarily upon comprehensive data on the lending activities of the three major auto finance companies for Wisconsin, Minnesota, and the nation as a whole. In addition, two of the

became effective only in September 1974, too late to have much effect; and data on Washington were hard to assess because it has a tight (12%) rate ceiling.

three major auto finance companies provided detailed historical data for Wisconsin from the year prior to the March 1, 1973 enactment of the WCA through August 31, 1975.

Due to the diversity of data, for purposes of exposition, it is useful to present the Wisconsin (vs. National and Minnesota) experience of each company individually. Then, insofar as possible, observations that apply to all companies will be made. To protect the confidentiality of the data, only index numbers, absolute differences, or percentage comparisons are disclosed.

Company 1:

Company I seemed to be least concerned about the Wisconsin Consumer Act. It was the only company that did not have or provide detailed historical data on its Wisconsin lending, and it noted that it used the same credit standards in Wisconsin as it did in all other states in the same geographic region. However, it also used 100 percent dealer recourse agreements as a standard practice. Thus, some credit rationing or price adjustments to altered risk may have occurred at the dealer level.

Evidence that dealer and creditor risks may have been somewhat higher for Company 1 in Wisconsin than in other states was shown by the fact that the company's delinquency rate over the year ending in August 1975 was 67 percent higher in Wisconsin than in the nation as a whole and 200 percent higher than in Minnesota. However, the repossession rate in Wisconsin was only half the national average, albeit somewhat higher than the repossession rate in Minnesota.

Data for the month of August 1975, provided mixed evidence on possible credit restriction by Company 1 in Wisconsin vis-à-vis other states. In particular, evidence on loan turndowns was mixed. The Wisconsin application rejection rate was 12 percentage points higher than the Minnesota rejection rate but one percentage point lower than the national rate. Also, while the acceptance percentage for loans in the highest acceptable risk category was 0.2 percentage points lower in Wisconsin than nationally, the acceptance rate for such loans in Wisconsin was 1.3 percentage points above the Minnesota rate.

Some evidence of credit restriction appeared in the company's down payment data--where down payments were assumed to be inversely related to reported loan/value ratios (which are calculated by dividing the value of the loan advance by the finance company by the value of the car as determined by standard guide books).

Based on loan/value ratio data, the company's down payment requirements appeared to be one to three percent more restrictive in Wisconsin than in Minnesota or the nation as a whole for new cars and late model used cars. However, for older model used cars the down payment requirements were more mixed, but that may be due in part to variations in loan size. For five-year and older used cars, average Wisconsin loan-to-value ratios were lower than in Minnesota's (by eight percentage points), but higher than the national standards (by three percentage points). For three and four year old used cars, average loan-to-value ratios were five percentage points higher in Wisconsin than nationally or in Minnesota, but the average loan size was 13 percent lower in Wisconsin than nationally and loan-to-value ratios tend to be higher on lower-valued used cars. The difference in average loan size, plus the small number of observations in that used car category, may explain much of the difference.

Loan maturities in Wisconsin generally were approximately the same as for the nation as a whole, but averaged substantially shorter (usually one to four months shorter) than loan maturities on the same type of loan in Minnesota.

Customer finance rates and average note sizes were generally lower in Wisconsin than in Minnesota or the nation as a whole. However, creditor rates (i.e. the net yield to the creditor on the discounted auto paper) were higher in Wisconsin than in the nation as a whole in all categories except for one- and two-year old used cars.² Also, variations in average note sizes may have reflected, in part, the generally stricter down payment requirements that prevailed in Wisconsin--which would imply that smaller notes were issued on equal valued used cars.

Finally, credit health insurance coverage was three times more frequent in Wisconsin than nationally, and credit life insurance coverage was 35 percent more frequent. While these statistics suggest a restrictive policy, they refer only to coverage by the company's life insurance affiliate. Thus, firm conclusions are hard to draw.

Overall, Company 1 experienced elevated delinquency rates in Wisconsin but its repossession rate was not elevated. It claimed it used the same credit standards for Wisconsin as elsewhere, but its application rejection rate was much higher than in Minnesota. However, this may have reflected an inferior pool of credit applicants in Wisconsin.

Due to 100 percent dealer recourse, some credit tightening may have occurred at the dealer level. For instance, loan-to-value ratios appeared to be somewhat lower in Wisconsin than elsewhere--particularly for new and late model used cars. This implies that Wisconsin down payment requirements may have been slightly elevated. The company's loan maturities were also more restrictive than in Minnesota, but were roughly equal to national figures, while customer finance rates tended to be lower in Wisconsin than elsewhere. Finally, credit insurance coverage by the company's insurance affiliate was much more extensive in Wisconsin than elsewhere.

Company 2:

In contrast to Company 1, which seemed to have made only few overt changes in response to passage of the Wisconsin Consumer Act (but manifested sharply higher delinquency rates--possibly as a result) Company 2 noted after a year or two under the WCA that its credit costs and losses in Wisconsin had increased markedly. Because it had documented the deterioration in its Wisconsin experience for internal purposes, this company volunteered detailed historical data on its Wisconsin experience in response to our initial questionnaire. Those data showed that relative to -its national experience, Wisconsin losses and delinquencies had risen substantially and credit terms and availability had fallen sharply after enactment of the WCA.

In response to question 2 on the questionnaire, Company 2 responded: "In three of the four regulated states (Massachusetts, Washington, and Wisconsin), our repossession and loss experience has been more adverse than in the states they are being compared with. In the case of West Virginia, it would appear that the restrictions on seeking deficiencies have not been in effect long enough. (September 1974) for any effect to be evidenced.

In the case of Wisconsin, the effects of the Wisconsin Consumer Act, enacted March 1973, can be seen. You will note that Wisconsin delinquency, repossession rates, income and reserve losses, new and used car rejection rates and qualified rates are either the most adverse for all states listed, or are among the most adverse. Insofar as the average loan/value ratios in Wisconsin are concerned, new..., late model ..., and older model ... [loan-to-value ratios] are among the lowest, again reflecting a conservative purchase policy. When the Wisconsin Consumer Act was enacted, we believe bank competition either withdrew from the automobile time market or severely limited the purchases they would consider. [Company 2's Milwaukee office] has since found it necessary

² Since creditors typically pay a premium over par value to purchase notes from the dealers, thereby generating additional revenue for the dealer, the creditor rate of return on such notes will tend to be lower than the rate paid by the customer.

to become more restrictive due to adverse experience. It is our feeling that as public knowledge of the Wisconsin Act increases, we will experience more and more delays in finalizing delinquent accounts. As a consequence, our operating experience could well become more adverse."

For the year ending in August 1975, this company reported Wisconsin delinquency rates 28 percent higher than its national average, and 124 percent higher than its Minnesota delinquency experience. It also reported that losses per unit repossessed in Wisconsin were 19 percent higher than nationally, and that its total loss rate in Wisconsin was more than 30 percent above its national average (comparable data were not provided for Minnesota). Finally, while its Wisconsin repossession rate varied from the national average rate by a fraction of one percent, it was 77 percent higher than its repossession rate in Minnesota.

Data for the month of August 1975, indicate that Company 2 was substantially more restrictive in its credit acquisition policy in Wisconsin than in Minnesota or in the nation as a whole. For new cars, the company's application rejection rate was nearly double (87 percent higher than) the national average and nearly quadruple (251 percent higher than) its Minnesota rejection rate. Furthermore, the percentage of conditionally accepted contracts (contracts accepted with improvements or qualifications) was roughly 15 percent higher in Wisconsin than in Minnesota (or the nation as a whole). In addition, new car down payment percentages (as indicated by loan-to-value ratios) were four percentage points higher (more restrictive) in Wisconsin than in Minnesota or nationally and average loan maturities were lower in Wisconsin (by 1/2 month when compared to Minnesota and by 1-1/8 months relative to the nation as a whole). However, the company's consumer finance rates were lower in Wisconsin than in Minnesota or the nation (although the creditor finance rate was higher in Wisconsin than in Minnesota), while average loan sizes, probably due to higher down payments, were also lower in Wisconsin than in the nation or Minnesota.

For late model used cars, the company's application rejection rate was 76 percent higher than its national rejection rate and 224 percent higher than its Minnesota rejection rate. In addition, the percentage of conditionally accepted contracts was 33 percent higher in Wisconsin than in the nation as a whole, and 63 percent higher than in Minnesota. Down payment requirements were mixed, however. Wisconsin loan-to-value ratios were two percentage points lower than equivalent Minnesota ratios, but were one percentage point higher than in the nation as a whole. Nonetheless, average contract maturities were more than 1.2 months shorter in Wisconsin than in Minnesota and the nation as a whole. Once again, average note sizes and customer finance rates were lower in Wisconsin than in the nation as a whole, but creditor rates were higher in Wisconsin than in Minnesota.

Only limited data were available for 3-4 year old used cars. These data indicated that average note sizes for such contracts were slightly lower in Wisconsin than in Minnesota or the nation as a whole, and that average contract maturities were slightly lower in Wisconsin than in Minnesota, but were slightly higher (by 0.18 month) than in the nation as a whole. They also suggested that the company's average customer rates and creditor rates were both higher in Wisconsin than in Minnesota, but were lower than national averages in both states.

For old (five-year or older) used cars, Wisconsin application rejection rates were more than twice as high as Minnesota rejection rates and 61 percent higher than the national average. Conditionally accepted contracts were roughly equal for all three entities (seven percent higher in Wisconsin than in the nation, and eight percent lower than in Minnesota). However, substantial differences existed in loan-to-value ratios. The data implied that down payments were roughly eleven percentage points higher in Wisconsin than in Minnesota and four percentage points higher than in the nation as a whole. Average contract maturities were practically identical in Wisconsin and the nation as a whole (Wisconsin was 0.01 month lower), while Minnesota contracts had somewhat (0.39 month) shorter average maturities. Finally, dealer and creditor finance rates and average note

sizes were lower on five year and older used car contracts in Wisconsin than in Minnesota or the nation as a whole.

The supplementary data provided by Company 2 were based on its Milwaukee office experience. Those data indicate:

- (i) The percentage of its dealer's time sales contracts purchased in Milwaukee by Company 2 (rather than by other credit grantors) doubled from 1972 to late 1974 and early 1975, as banks with drew from the indirect auto credit market, then declined as Company 2 acquired credit more selectively and banks reentered the market.
- (ii) In the first year after passage of the Wisconsin Consumer Act, the number of accounts past due 60 days or more tripled. The respondent explained these changes as follows:

This was a direct result of our inability--because of legislated restrictions--to deal conclusively with problem accounts.

Because the legislated restrictions not only delayed needed collection activity but also made later collection action more difficult, it took a period of time before the more adverse delinquency condition began to be reflected in repossession and loss experience--as it ultimately is.

During the first and second years after the Act, repossession and loss rates for [our Milwaukee office] increased more sharply than did those for our total operations. During this period, of course, economic conditions were difficult generally.

During the third year after the Act (March 1975 to date), the improved economic conditions were reflected in improved overall delinquency, repossession and loss experience. The experience of [our Milwaukee office], however, has continued to worsen.

Specifically, thus far during this third year after the Act, [our Milwaukee office's] repossession and loss rates are twice as high as they were during the year prior to the Act.

Additionally, whereas the collection results achieved by [our Milwaukee office] were better than our overall operations during the year prior to the Act, they are now--thus far in the third year after the Act--significantly worse.

It should be noted that the more adverse ... Milwaukee loss experience is caused not only by a higher rate of repossession, but also by a significantly higher average loss [per new car repossession sold]--about 25 percent higher than our U.S. average. This is due to the legislated delay in taking conclusive action. The account becomes more seriously delinquent and the car continues to depreciate, so that at the time of repossession, there exists a greater margin between the outstanding balance on the account and the value of the car.

When our overall collection experience began to reflect improvement in early 1975 and the experience of [our Milwaukee office] continued to worsen, it became obvious that Milwaukee had to take corrective action--and they have.

The only practical action was to tighten purchase policy--to become more selective in the transactions acceptable for purchase.

The effect of this action is readily apparent both in the percentage of transactions rejected and in the percentage of dealer time sales purchased. During the last month for which data are available, for example, [we] purchased only one-third of dealer time sales--whereas it was more than twice that figure a year earlier. During the past eight months, the percentage of ... offerings rejected by Milwaukee was about 27 percent--more than double the overall U.S. rate and the Milwaukee rate prior to the tightening.

Certain available contract characteristic data provide some indication of the nature of the more restrictive purchase policy adopted. For example, the average amount financed on new cars as related to estimated dealer cost had been running about the same in Milwaukee as for the total operation. This average relationship has declined noticeably, particularly in recent months. Additionally, the proportion of new car volume with terms over 36 months has declined sharply.

In addition to becoming more restrictive in purchase policy, [our Milwaukee office] has strengthened its collection staff in an effort to get its collection results under better control. Given the legislated restrictions on collection activity, we do not know how much effect this action alone will have.

We presume the business [our Milwaukee office] is not now buying is being purchased by banks or other financing sources.

At about the same time we tightened purchase policy, banks generally were again becoming more active in auto financing as a result of the easing in the money market.

We are told banks are being relatively liberal in approving auto credit. To the extent this is true, we would attribute it to (a) their attempt to regain their former level of participation in the market and, (b) the fact they generally have not had the recent adverse collection experience [that we have had].

We believe that these other financing sources who are now purchasing the bulk of available auto financing in Milwaukee will begin developing adverse experience in the not too far distant future. Should this develop, it seems clear the availability of auto credit in Milwaukee will be reduced. Certainly, [our company] after its experience, will not again pick up the slack.

The Milwaukee office statistics provided by Company 2 support the above statements and show in addition that its Milwaukee repossession rate has risen from 107 basis points below its national average repossession rate (in the year prior to implementation of the Act) to 87 basis points above its national average repossession rate (in 1975). Thus, Milwaukee consumers have not been spared repossessions as a result of passage of the Act (as repossessions by Company 2 have risen relative to the national average by nearly two, full percentage points).

Finally, the company's data show a percentage of losses charged to income for Milwaukee which is over three times the national average, in contrast to a rate that was practically equal to (one basis point below) the national average in the year before the Act became effective.

In sum, the data submitted by Company 2 indicate that its collection and loss experience deteriorated substantially in Wisconsin after implementation of the Wisconsin Consumer Act. As a result credit terms and availability were sharply restricted. As a consequence, by August 1975 (and for the 12 months ending August

31, 1975) the company's application rejection rates were substantially higher in Wisconsin than elsewhere and their loan down payment and maturity requirements on accepted applications--with few exceptions--were less lenient in Wisconsin than elsewhere. However, the customer finance rates were usually lower in Wisconsin than elsewhere, even though creditor rates obtained by the company were usually higher in Wisconsin than Minnesota.

Company 3:

Company 3, like Company 2, indicated that its credit standards had become more restrictive in Wisconsin subsequent to the effective date of the Wisconsin Consumer Act. However, it also noted that it had made no conscious effort to restrict credit. As evidence of restrictions in credit availability it noted that the percentage of accepted loans in the highest acceptable risk class fell by 2/3 from the period prior to the effective date of the Wisconsin Consumer Act to 1975. In addition, data submitted by the company show that the firm's proportion of over-36 month new car contracts is significantly lower in Milwaukee than nationally, and that its Milwaukee new car loan-to-value ratios are presently substantially below national average loan-to-value ratios on its new car loans. Furthermore, average loan-to-value ratios for its Milwaukee used car contracts have declined slightly since late 1972-early-1973.

The last results must be qualified, however, by noting that the company's loan-to-value ratios in Wisconsin have been substantially more restrictive than the national average in each of the last four years. Hence, little change has occurred from the year preceding implementation of the Act to present. Also, the company's application rejection rates for Milwaukee non-recourse contracts over the last year were not above (were almost exactly equal to) national application rejection rates for nonrecourse contracts, and their rejection rates on Milwaukee recourse contracts (on which dealers would bear much or all of the loss) were the same or lower than their national application rejection rates for recourse contracts.

Generally higher down payments and reduced availability of credit to the highest risk customers in Milwaukee lowered the company's total Milwaukee delinquency rates from 1972 to 1975 (both absolutely and relative to the nation as a whole). However, 60-day-and-over (or hardcore) delinquency rates rose, rather than fell, during that period and increased from a level only slightly above the national level in 1972-73 to a level substantially above the national level in 1974-75. As a result, the ratio of 60-day-plus to 30-day delinquencies deteriorated in Milwaukee, from 17 percent in 1972-73 to 24 percent in 1974-75, while the national rate remained practically stable at 17 percent. These results support the hypothesis that restrictions in creditors' remedies increase long-term relative to short-term delinquencies. While tighter standards have reduced short-term and total delinquencies, remedy restrictions appear to have made it much more difficult to obtain prompt repayment of defaulted loans.

Aside from data cited above, only limited additional data on the historical Milwaukee experience were available from Company 3. The additional data indicate that the company's average loss per repossession declined in Milwaukee (as well as nationwide) from 1972 through 1975.

Data submitted by Company 3 in response to the primary questionnaire indicate that credit losses (as a percentage of outstanding balances at the end of August 1975) were 19 percent higher in Wisconsin than in the nation as a whole, and 72 percent higher than in Minnesota. Its average loss-to-liquidation ratio (which expresses losses as a percentage of total repayments, charge-offs, and other liquidations of outstanding loan balances during the year), however, was the same for Wisconsin and the nation, but 75 percent higher in Wisconsin than in Minnesota. These results held in spite of the fact that the company's average loss per

repossession was nine percent lower in Wisconsin than in the nation as a whole (albeit, 24 percent higher than Minnesota losses per repossession).

Wisconsin delinquency rates during the 12 months ending in August, 1975, were four percent higher than in the nation as a whole and 56 percent higher than in Minnesota. However, the repossession rate (based on the number of contracts outstanding on August 31, 1975 and average monthly repossessions) in Wisconsin was 35 percent lower than the national average rate and 26 percent lower than the Minnesota rate.

For new car contracts originated in August, the data indicate that Wisconsin credit availability was substantially lower than credit availability in Minnesota. The application rejection rate was twice as high in Wisconsin as in Minnesota and the proportion of accepted credit applicants in the highest-risk class was less than half as great. However, Wisconsin and national credit availability appeared to be nearly identical; high-risk acceptance rates were identical while overall Wisconsin rejection rates were 93 percent of the national average rate.

Also for new car contracts, the company's average loan-to-value ratio in Wisconsin was four percentage points below its national average (and 1/2 percentage point below its Minnesota average). However, average maturities were one or two months longer in Wisconsin than in the nation and Minnesota, and average creditor and customer finance rates were lower in Wisconsin than the nation and Minnesota. Average new car note sizes were approximately the same in the nation and Wisconsin, but lower in Minnesota.

For used car contracts, the evidence on credit availability was mixed. While, application rejection rates were 69 percent higher in Wisconsin than in Minnesota, the percentage of highest risk accepted applicants was four percent higher in Wisconsin than in Minnesota. Also, Wisconsin used car credit availability appeared to be slightly less restrictive than in the nation as a whole (while application rejection rates were equal in Wisconsin and the nation, the proportion of high risk used car customers accepted in Wisconsin was 25 percent greater than the proportion accepted in the nation as a whole). Average loan-to-value ratios for Wisconsin used-car credits were 6-1/2 percentage points lower than the national and Minnesota averages. However, once again, Wisconsin maturities were somewhat longer (by one to two months) than elsewhere, while average note sizes were mixed (with Minnesota at the low end and Wisconsin in the middle). Average customer finance rates were still higher in the nation and Minnesota than in Wisconsin, but average creditor rates were lowest in Minnesota.

Although contract acceptance and rejection rates, etc., were not available by age of used car for Company 3, data on maturities, rates, and loan-to-value ratios were available. The most interesting observation gleaned from these data was that Wisconsin loan-to-value ratios on five-year and older used cars were 20 percent lower (in absolute terms) than equivalent loan-to-value ratios in Minnesota and 30 percent lower than those prevailing in the nation as a whole. Thus, down payments requirements on old model used-cars were evidently substantially higher in Wisconsin than elsewhere. Also, both customer and creditor rates were higher on five-year and older used-car credits in Wisconsin than in Minnesota, and Wisconsin creditor rates were also higher than in the nation as a whole. Average maturities were substantially longer in Wisconsin, however, even though average note sizes were approximately the same in all areas under consideration.

The loan-to-value ratio data for old used cars support the observations of Whitford and Lawyer, that many dealers raised down payments substantially on older model used cars after the Wisconsin Consumer Act was passed.³

³ See Whitford and Lawyer, H. "The Impact of Denying Self-Help Repossession of Automobiles: A Case Study of the Wisconsin Consumer Act," Wisconsin Law Review, 1975, pp. 607-657.

For new used cars, loan-to-value ratios were either the same or slightly lower in Wisconsin than in Minnesota and the nation as a whole. Thus, in contrast to the older model used cars, if anything, down payment requirements were slightly higher in Wisconsin than elsewhere for late model used cars. Also, late model used-car credit maturities were generally longer in Wisconsin (by 0 to 2 months) than in the nation or Minnesota. Finally, customer finance rates were lower in Wisconsin than elsewhere, but Wisconsin creditor finance rates were higher than Minnesota creditor finance rates for all used car categories.

In sum, data for Company 3 suggested that credit loss rates and serious contract delinquency rates were somewhat elevated in Wisconsin. They also suggested that, even without a conscious policy, credit availability in Wisconsin, particularly, to the highest risk customers, had diminished markedly after passage of the WCA. Also, Company 3 down payments tended to be higher in Wisconsin than elsewhere. Nonetheless, contract maturities tended to be longer in Wisconsin than elsewhere and average customer finance rates and overall delinquency rates were lower.

Summary:

Summary tables 1-3 provide weighted average data for all items of information for which comparable data were available from all companies. For ease in comparison, index numbers which show the relationship of state figures to national average values are included in the tables. These data basically confirm with less detail, the company-by-company patterns observed above.

Overall, passage of the WCA appeared to increase delinquencies and losses in Wisconsin for all three companies and to make at least two of them less willing to extend credit. It also appeared to cause down payment requirements to be higher than would otherwise be the case. Contrasts of this sort were most marked when comparisons were made between Wisconsin and Minnesota, but they also tended to hold for comparisons between Wisconsin and the nation as a whole. Other possible indices of possible credit restraint, such as contract maturities and finance rates, showed a more mixed picture. Overall, customer finance rates were somewhat lower in Wisconsin than elsewhere and average creditor rates were mixed.

Historical data for Wisconsin credit which two of the three companies provided showed a marked deterioration in credit loss and long-term vs. short-term delinquency experience after passage of the WCA. Those data also indicated that credit terms in Wisconsin--particularly down payment requirements and the percentage of over 36-month new car contracts--fell relative to national levels and that loans to the highest acceptable risk classes of customers fell sharply after passage of the act.

Elevated contract rejection-rates and increased down payments suggest that automobile credit in Wisconsin became less available to marginal risk borrowers after passage of the WCA. While only two of the three companies documented an increase in credit standards, the third company used 100 percent dealer recourse agreements and some policy changes might have occurred at the dealer level. This appeared to be the case because the company's Wisconsin delinquencies were markedly elevated (which would provide an incentive for tightening up) while its Wisconsin loan-to-value ratios tended to be lower than its national average and Minnesota experience (which indicates that some tightening may have occurred at the dealer level). Thus, all three companies appeared to engage in some explicit or implicit credit rationing to the riskiest class of borrowers (as marginal risk borrowers are least likely to be able to raise a substantial down payment). Interviews conducted by Whitford and Lawyer⁴ with used-car dealers in Milwaukee indicated that after passage of the WCA they, too, had significantly tightened up on down payment requirements, particularly on lower valued used cars--that tend to be purchased on credit by the lowest income, highest risk borrowers.

⁴ Whitford and Lawyer, op. cit.

It is difficult to know how many people were rationed out of the finance company auto credit market by increased down payment requirements and/or increased credit standards after passage of the WCA. For low-income applicants the rationing might have been quite severe--as one company noted that it was now accepting only 1/3 as many "highest acceptable risk" applicants as it had prior to the WCA. For higher income applicants it would likely have been far less noticeable. Because high-risk applicants make up only a fraction of the automobile credit market, total rationing might have been limited to relatively small percentage of the total population.

Table 1

Auto Finance Company Repossession and Loss Rates

Average Values for 12 mo. ending Aug. 31, 1975	Level			As % of national level	
	Wisc.	Minn.	Nation	Wisc.	Minn.
# of accounts outstanding	43,072	40,521	4,936,510	0.9	0.8
repossessions/account outstanding(%)	8.36	3.92	7.63	109.6	51.5
Delinquency rate (30 days or more)	3.184	1.574	2.447	130.1	64.3

TABLE 2

Characteristics of New Car Paper Acquired August 1975

	Over (Under) National Average				
	Wisc.	Minn.	Nation	Wisc.	Minn.
Avg. Amount Financed	\$3,801	\$3,839	\$4,082	(\$281)	(\$243)
Average Cust APR	12.226%	12.946%	13.110%	(0.884)p.p.	(0.164)p.p.
Average Creditor APR	10.699%	10.679%	10.950%	(0.251)p.p.	(0.271)p.p.
Avg. Loan/Value Ratio	83.312%	87.123%	86.800%	(3.488)p.p.	0.323 p.p.
Avg. Cont. Maturity (Mos.)	37.438	37.990	37.912%	(0.474)	(0.078)
Application Rejection Rates	27.378%	9.550%	18.227%	9.151 p.p.	(8.671)p.p.

Memo:

Number of Contracts	853	1,160	121,070
Acquired	0.70%	0.96%	100.00%
% of U.S. Total			

P.P. = Percentage Points

Exhibit A:

**Auto Credit Survey Questionnaire
October 30, 1975**

This survey is intended to obtain data on the relative terms and availability of new- and used-car credit both in several key states and for the nation as a whole. All information supplied by individual firms on this survey form will be held strictly confidential. It is believed that most of the data requested can be obtained by modifying computer programs used to prepare monthly new- and used-car loan rate and credit terms data for submission to [the Federal Government] ... for the month of August 1975. In addition, we would like to obtain

similar data from you for the same month for the following states: (i) Wisconsin (ii) Minnesota (iii) West Virginia (iv) Virginia (v) Washington (vi) Oregon (vii) Massachusetts (viii) Rhode Island. Tables for recording data are attached.

The data which we need both for the nation as a whole and for each indicated state should be broken down as it is for the [Federal Government] by new- and used-cars and by 1 and 2, 3 and 4, and 5 year and older used car contracts. The particular items in which we are most interested are the creditor finance rate, the customer finance rate, the average loan/ value ratio, the average contract maturity and the number and dollar amount of contracts financed.

Additional data and information which would be useful for our study, should have it available, involve answers to the following questions:

- (1) Do you require dealer recourse agreements on your auto paper more frequently in Wisconsin, Massachusetts, Washington, and West Virginia than you do in states which have less stringent restrictions on creditors' remedies (or in the U.S. as a whole)? If you could document your observations statistically, possibly by calculating the percentage of loans with recourse provisions and with dealer reserve balances, it would be extremely helpful.
- (2) How does your repossession and loss experience differ in the eight indicated states from your repossession and loss experience in the nation as a whole? Again, if your observations could be documented statistically it would be most useful. Loss rates would be most useful if they were related to balances outstanding, while repossession rates would be most useful if related to total number of loans outstanding for residents of the state.
- (3) Are there any systematic differences in your willingness to grant credit in the states of Wisconsin, Massachusetts, West Virginia, and Washington, versus the nation as a whole? I.e., do you have different cut-off limits on credit-score evaluations, or policy restrictions on minimum income levels or maximum debt-to-income levels, etc. which must be met before an individual can qualify for a loan in those states? If so, can you document those differences statistically by citing differences in credit application rejection rates, credit score cut-off points, or other indices which might allow credit availability in the indicated states to be compared to credit availability in the nation as a whole?
- (4) Is there a difference in the degree of borrower coverage by credit life, health, and accident insurance in contracts drawn in Wisconsin, Massachusetts, West Virginia, and Washington versus contracts made in the U.S. as a whole? If statistical data can be easily compiled on this point, by new- and used-car category, it would also be helpful.

Useful statistics would include measures of premiums on each category of insurance divided by the total amount financed (as defined by truth in-lending) for new contracts acquired during August 1975, both in each indicated state and in the nation as a whole.

We thank you for any information which you are able to provide on these topics. We have provided forms for your convenience in providing the data. If there are instances in which you can provide similar information, but in a different fashion, please provide those data rather than none at all. As previously noted, all data which you submit will be kept strictly confidential and will be seen only by the staff of the Credit Research Center. If you are unable to provide the indicated data for August, please contact Robert Johnson or Richard Peterson of the Credit Research Center (phone 494-5043), so that we can establish a different month for all reporting firms. We hope that you will be able to provide this information by November 30, 1975.

Table 3

Characteristics of Used Car Paper acquired in August, 1975

Characteristics	Wisc.	Minn.	Nation	Wisc.	Minn.	Nation	Wisc.	Minn.	Nation
Number of contracts acquired (% of National level)	263	211	37,359	215	148	21,241	151	150	12,859
Total Amount financed (\$) (% of National level)	(0.7)	(0.6)		(1.0)	(0.7)		(1.2)	(1.2)	
Average customer A.P.R. (%) (% of National level)	731,385	742,835	109,961,037	387,865	271,531	38,642,908	138,933	143,400	12,961,754
Average creditor A. P. R. (%) (% of National level)	(0.7)	(0.7)		(1.0)	(0.7)		(1.1)		
Average loan/ value ratio M (% of National level)	14.72	15.04	16.01	17.61	17.43	19.26	19.82	20.65	21.53
Average loan maturity (mo.) (% of National level)	(91.9)	(93.9)		(91.4)	(90.5)		(92.0)	(95.9)	
	12.07	11.90	12.35	10.65	12.57	13.72	15.55	15.57	16.88
	(97.7)	(96.4)		(77.6)	(91.6)		(92.1)	(92.2)	
	93.29	114.39	93.47	N.A.	N.A.		98.45	112.57	108.42
	(99.8)	(122.4)					(90.80)	(103.8)	
	32.27	39.69	33.32	22.74	26.49	21.83	20.38	19.23	19.62
	(96.9)	(119.1)		(104.2)	(121.3)		(103.9)	(98.0)	

2. If it is possible for you to determine losses and repossessions by state, please rep the following information as possible.

Average value for 12 months Ending in August, 1975

	Nationwide		By State							
			Mass.	Minn.	Ore.	R.I.	Va.	W.Va.	Wash.	Wisc.
Receivables Outstanding										
# of acct's <i>outstanding</i>										
Delinquency rate (accounts delinquent 30 days or more)										
# of Repossessions										
Gross Losses										
Net Losses										
Losses per unit repossessed										
Losses on repossessions as percent of receivables										

3. Are there any differences in your willingness to grant credit to residents of Wisconsin, Washington, and Massachusetts than to residents of other states, such as different credit minimum income requirements, etc? Relatedly, has there been any change in the quality o have acquired in Wisconsin since the Wisconsin Consumer Act became effective? If so., pl if possible document those differences statistically.

2. If it is possible for you to determine losses and repossessions by state, please report as much of the following information as possible.

Month of August, 1975	Nationwide	By State							
		Mass.	Minn.	Ore.	R.I.	Va.	W.Va.	Wash.	Wisc.
Receivables Outstanding									
# of acct's <i>outstanding</i>									
Delinquency rate (accounts delinquent 30 days or more)									
# of Repossessions									
Gross Losses									
Net Losses									
Losses per unit repossessed									
Losses on repossessions as percent of receivables									

3. Are there any differences in your willingness to grant credit to residents of Wisconsin, West Virginia, Washington, and Massachusetts than to residents of other states, such as different score limits, minimum income requirements, etc? Relatedly, has there been any change in the quality of paper which you have acquired in Wisconsin since the Wisconsin Consumer Act became effective? If so, please if possible document those differences statistically.

Characteristics of New Car Paper acquired August, 1975.

	Nationwide	By State							
Characteristics		Mass.	Minn.	Ore.	R.I.	Va.	W.Va.	Wash.	Wisc.
Number of contracts acquired									
Total amount financed									
Average customer A.P.R.									
Average creditor A.P.R.									
Average loan/value ratio									
Average contract maturity									
Percentage of contract with:									
dealer recourse or repurchase agreements									
dealer reserves									
credit life ins.									
credit health ins.									
Total life, health, and accident insurance premiums									
Application rejection rates									
Percentage of accepted applications in highest risk									

Characteristics of Used Car Paper, for 1-2 year old cars, acquired in August, 1975.

Characteristics	Nationwide		By State						
		Mass.	Minn.	Ore.	R.I.	Va.	W.Va.	Wash.	Wisc.
Number of contracts acquired									
Total amount financed									
Average customer A.P.R.									
Average creditor A.P.R.									
Average loan/value ratio									
Average contract maturity									
Percentage of contract with:									
dealer recourse or									
repurchase agreements									
dealer reserves									
credit life ins.									
credit health ins.									
Total life, health, and accident									
insurance premiums									
Application rejection rates									
Percentage of accepted									
applications in highest risk									

Characteristics of Used Car Paper, for 3-4 year old and older used cars, acquired in August, 1975.

Characteristics	Nationwide		By State						
		Mass.	Minn.	Ore.	R.I.	Va.	W.Va.	Wash.	Wisc.
Number of contracts acquired									
Total amount financed									
Average customer A.P.R.									
Average creditor A.P.R.									
Average loan/value ratio									
Average contract maturity									
Percentage of contract with:									
dealer recourse or									
repurchase agreements									
dealer reserves									
credit life ins.									
credit health ins.									
Total life, health, and accident									
insurance premiums									
Application rejection rates									
Percentage of accepted									
applications in highest risk									

Characteristics of Used Car Paper, for 5 year old and older used cars, acquired in August, 1975.

Characteristics	Nationwide		By State						
		Mass.	Minn.	Ore.	R.I.	Va.	W.Va.	Wash.	Wisc.
Number of contracts acquired									
Total amount financed									
Average customer A.P.R.									
Average creditor A.P.R.									
Average loan/value ratio									
Average contract maturity									
Percentage of contract with:									
dealer recourse or									
repurchase agreements									
dealer reserves									
credit life ins.									
credit health ins.									
Total life, health, and accident									
insurance premiums									
Application rejection rates									
Percentage of accepted									
applications in highest risk									