Testimony of "Jim Dough"
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Special Committee on Aging Hearing
"Equity Predators: Stripping, Flipping and Packing
Their Way to Profits"

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Introduction

Good afternoon. Thank you for inviting me to share my experience as a finance company employee. I've worked for finance companies for more than seven years. My testimony is based on my experience as an employee of three of this country's largest finance companies. Because I still work in the finance industry and fear retaliation, I do not wish to reveal my identity; however, everything I say today is true.

During my employment with finance companies, I've served as a finance officer, assistant branch manager and branch manager. I've worked at several different branches and under the supervision of many different managers and supervisors. I was responsible for supervising branch employees, making arrangements with retail dealers for installment loans, contacting prospective and current customers, making loans, servicing loans and collecting loan payments from delinquent customers.

Targeting Customers

Finance companies try to do business with blue-collar workers, people who haven't gone to college, older people who are on fixed incomes, non English-speaking people and people who have significant equity in their homes. In fact, my perfect customer would be an uneducated widow who is on a fixed income -- hopefully from her deceased husband's pension and social security -- who has her house paid off, is living off of credit cards, but having a difficult time keeping up her payments, and who must make a car payment in addition to her credit card payments.

The finance companies I've worked for use three primary methods to obtain new customers. First, they often send guaranteed loan vouchers to potential customers. These vouchers, also known as "live checks", permit someone to obtain a loan between $500 to $3500 simply by either stopping in at the nearest branch, or by signing the back of the check and depositing it at a bank. Second, finance companies often run different types of promotions using the mail to seek business from new customers. Sometimes the companies offer contests and prizes to entice new customers to take out loans. Third, finance companies obtain many of their customers by participating in retail sales installment loans. The finance companies arrange to do installment financing with local retail dealers. When a retail customer wants to finance the purchase of a stereo, for example, the finance company, rather than the retail dealer, actually makes the loan and gains a new customer.

The Initial Flip

When a finance company obtains a new customer through one of the methods I've just described, it receives information about the customer's credit history, employment, income, home ownership and debts. As soon as the finance company makes that retail loan, for example, a branch employee reviews information about the customer, works up a financial plan and contacts the customer. Although we would tell customers that we were calling to see if they got their merchandise, the real purpose of the call was to solicit the customer into converting the retail installment loan into a more profitable personal loan or home equity loan. Going into the call, since you already have all the information on the customer, then you can go ahead and work out a payment plan, payment options, bill consolidation plans, or home equity plans. We called this the "up-sell," and our goal was always to up-sell to the biggest loan possible. The conversion of a retail installment loan, live check or other small loan into a personal or home equity loan is also known as a flip.

To flip one of these small loans into a personal or home equity loan, we were trained to sell the monthly "savings," that is, how much less per month the customer would be paying if we flipped the loan. In reality, the "savings" that we were trained to sell to customers were just an illusion. The uneducated customer would jump for the "savings," thinking that he would have more money to buy other things. What the customer wouldn't figure out and what we wouldn't tell him is that he would be paying for a longer period of time and in the end would pay a whole lot more.

Flipping Current Borrowers

Finance companies require branch employees to make contact every three months with customers to prevent payoffs and up-sell to bigger loans. At some of my branches, we tried to call every one of our real estate customers at least once a month. The purpose of these contacts was to flip as many loans as possible. Our tactic was to try to gain the trust and confidence of the customer. We typically began a telephone solicitation by asking if there were any new events in the customer's life that called for additional money. We were trained that we should always ask the customer if he or she needed more money. For our home equity customers, we stressed that the interest on the loan was tax deductible. Because the terms of those loans did not usually exceed fifteen years, we told customers that they could retire earlier because their house would be paid off sooner. For our debt consolidation customers, we stressed that they could take the money that they were saving in their monthly payments and invest it in a mutual fund.

The term "flipping" is commonly used by finance companies. In my experience in the industry, flipping was a common practice. We were instructed and expected to flip as many loans as possible. One of my supervisors imposed a daily requirement that each branch employee obtain at least two applications from present borrowers to refinance their loans. In other words, each branch employee was supposed to try to flip at least two loans each day.

When I served as a branch manager, increasing the number of refinance loans was a frequent topic at branch manager, district and state-wide meetings. Among the things we were taught at these meetings was to target "blue collar" workers for loan flips. We were also told to target present customers who were delinquent on their loan payments. Delinquent customers made good flipping candidates because we could put additional pressure on them. We were instructed to tell those customers that they could either bring their account balance current or refinance their loan. We knew that these customers would almost always agree to refinance because they didn't have the money to pay on their current loan and did not want the finance company to institute foreclosure or collection proceedings.

We were also told to target personal loan customers whose terms had less than six months remaining, and customers who owed less than 50% of the original principal balance on their loans. I recall one of my supervisors saying that there is a point in each loan when the customer starts to pay a significant portion of principal instead of mostly interest. We were supposed to try to get the customer to refinance at that point in the loan term.

Flipping loans allows finance companies to charge customers points, that is, a percentage of the amount borrowed, on each real estate loan conversion or renewal. The practice is to charge the maximum number of points legally permissible for each loan and each flip, regardless of how recently the prior loan that was being refinanced had been made. The finance companies I worked for had no limits on how frequently a loan could be flipped, and we were not required to rebate any point income on loans that were flipped.

Insurance Packing - How is it done?

Packing is taking insurance products (as many as you can), putting them on the loan and then trying to cover them up or gloss over them. Packing is shoving as much insurance onto the customer as possible without the customer's knowledge or without the customer's understanding.

We attempted to pack insurance during our very first pitch to a new customer. For example, we were trained to tell a new retail installment customer that we had reviewed the customer's financial situation and could offer the customer a debt consolidation loan that would save the customer money by reducing the customer's monthly payments to creditors. The sales pitch would be substantially similar to the following: "Mr. Smith, in reviewing your loan application, I see that you have a lot of credit card payments. What if I could save you $550 a month through consolidating your debt into one loan?" I was taught that the most effective way to sell insurance was to always include insurance products in this quote without telling the customer that my monthly quote included insurance. I was taught that I should always include as many insurance products as possible in the monthly payment quote so long as I could quote a figure that would be less than the customer's current outstanding debt obligation. Using that method, if the customer did not express interest in my initial quote, I could eliminate one insurance product (without telling the customer that I was doing this) and give a quote for an even larger monthly savings. For example, if the customer rejected my pitch to save him $550 a month, I would eliminate one insurance product and respond "Suppose I could save you $600 per month?" Usually, the more naive the customer, the more insurance I would pack on the loan before I made the initial monthly payment quote. This tactic was very effective with immigrants and non-English speaking people. Don't be fooled by training manuals. The manuals are written for regulators, but finance company employees are trained to ignore the manuals if they expect to make their profit quotas and keep their jobs. For example, even though my training manuals discussed quoting a monthly payment both with, and without insurance, I was trained by my supervisors that unless my conversation was being audited, I should ignore the manuals, and *always* quote the monthly payment on a proposed loan *with* insurance unless the customer specifically asked what the cost would be *without* insurance. The tactic we used at all of the finance companies I worked for was "if they [customers] don't ask, don't tell." I heard this phrase often from many of my managers and supervisors.

The "don't ask, don't tell" policy was successful because customers were not aware, until closing (if at all), that the loan included insurance. Once the customer indicated that we could schedule a closing regarding the loan proposed in the telephone solicitation, we merely presented the loan documents with insurance included, even though insurance had not been discussed previously. Through their training and experience, finance company employees know that customers are often desperate for the money, and usually will not object to the insurance once the loan reaches closing. If customers objected to the insurance at closing, we would add more pressure by telling them that if they wanted the loan without insurance, it would be necessary to re-do their loan documents and the closing would need to be rescheduled for a later date. That was a half-truth. We could re-do the loan documents in a few minutes. It wasn't really necessary to reschedule the closing for a later date, but we knew that customers would be more likely to cave-in and accept the insurance if they thought that they couldn't get the money that day. In my experience, this was usually enough to persuade the customers to go through with the closing and take the insurance.

When insurance was to be included with the loan, our computer programs automatically calculated the maximum amount of insurance as provided by state law. The amount of insurance coverage on the loan was never arrived at through negotiation with a customer.

Why did we pack insurance?

Insurance sales are very important to finance companies. My supervisors often used phrases like, "Insurance drives profits." One of my supervisors said that insurance was more important to our company's profitability than its spread on interest rates.

Because insurance sales are so important to the bottom line, finance companies require that their employees meet goals and quotas regarding insurance. Insurance sales are tracked by dollar volume, penetration rates and premium-to-volume ratios. For example, one of my employers required that its branches maintain an 80% penetration rate for credit life (that is, employees were expected to sell credit life insurance in at least 8 out of every 10 loans). My employers always made it clear that I would not keep my job unless I fulfilled my insurance sales quotas.

Finance companies also provide additional rewards for employees who meet or exceed their insurance sales quotas. All of my finance company employers had a quarterly bonus system. Part of my bonus depended on whether my branch met its insurance sales quotas. All of my finance company employers also ran quarterly insurance sales contests. We would be eligible for contest awards if we exceeded quotas regarding insurance penetration and insurance sales volume.

Conclusion

I am glad that I no longer work for a finance company. If they want to keep their jobs, finance company employees must flip and pack loans. They are under enormous pressure to meet quotas regarding loan volume, repeat business and insurance sales. In fact, the pressure to produce loan volume and insurance sales is so great that on many occasions, I've seen finance company employees commit forgery on a massive scale. These employees have forged everything from insurance forms, RESPA documents, income verification forms, and even entire loan files. These practices have always disturbed me, and I hope that something can be done to make finance company customers more aware of these practices so that they can keep from becoming victims of flipping and packing scams.