Reducing Cycle Time with Negative Equity Transactions: Solution Expedites Lien Payoff Process

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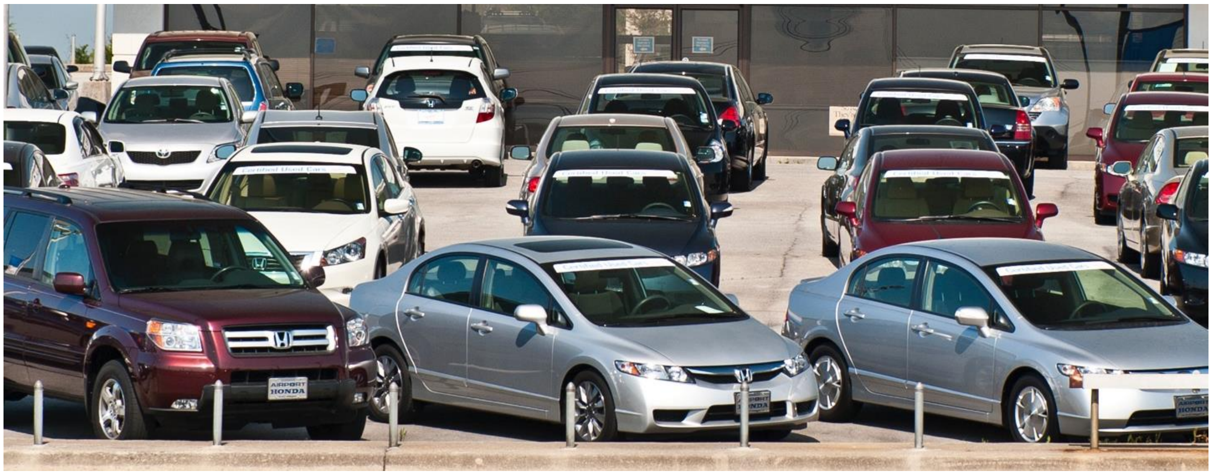
In the current economic climate, automakers are producing vehicles that are increasingly expensive due to technological complexities. Consumers are struggling to make sizeable down payments on these vehicles in hopes of lowering their monthly payments and moving into a positive equity position.

This article will focus on the latest auto industry financing trends and the resulting time-consuming and costly issues affecting consumers, insurance providers and lenders. We will also discuss a key industry solution that delivers efficiencies in claims and cost savings for carriers, lenders and consumers.



The Negative Equity Landscape

Over the past several years, the total loss claims landscape has developed interesting trends that show no signs of reversing themselves. Based on internal analysis and interactions with multiple insurance providers, IAA estimates that there are nearly 5 million cars declared a total loss each year. An estimated 60-70% of total loss vehicles that still have loans to be paid off face negative equity situation. The causals for these trends are driven by multiple factors, including the higher cost of new vehicles as they become increasing more complex, elevated levels of depreciation, an insatiable consumer demand for higher-value vehicles such as SUVs, loan terms that outlive the average vehicle warranty and the fact that consumers have never had so many vehicle financing options. It is estimated that new vehicles lose 20% or more of their value in their first year on the road (Carfax, 2021). Auto loan term lengths have been steadily increasing and show no signs of receding. According to Experian, the average loan term for new-car financing is just under 72 months, which increased by 2 months from Q2 2019 (Experian, 2020). The net result is higher overall loan amounts and auto loans that very often outlive the ownership of the vehicle.

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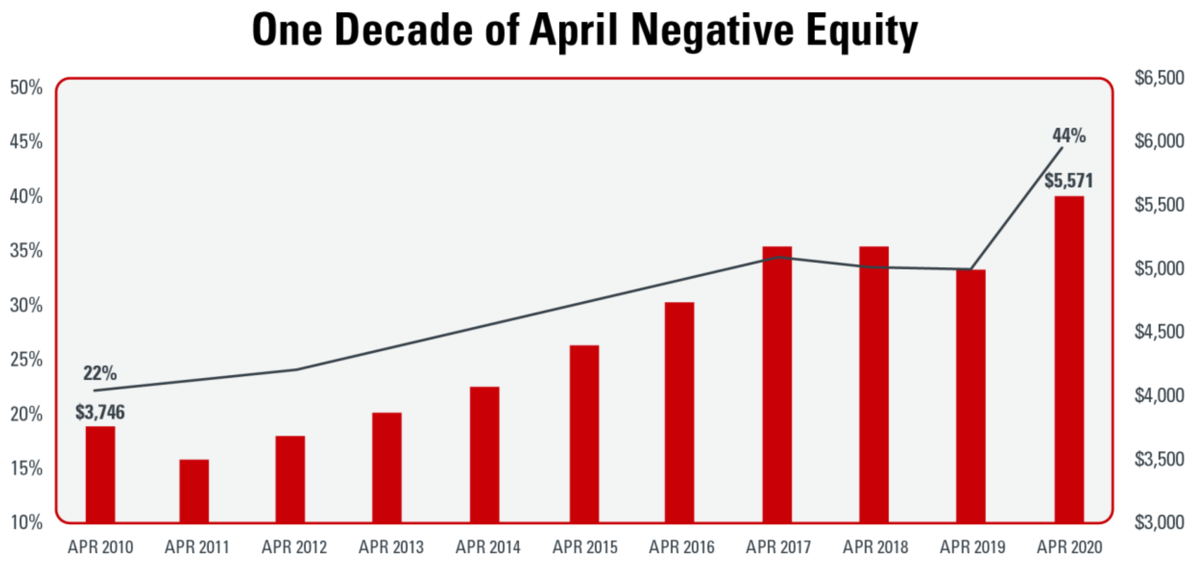
New vehicles lose up to **20%** or more of their value in the first year.

More than **40%** of car loans originated have terms of 6 years or longer.

April 2020 set a record with 0% finance deals accounting for 25.8% of dealership-financed new vehicle purchases, also known as indirect lending or financing. Many of these loans carried a term length of 84 months (Edmunds, 2020). Two other records were broken in April 2020. The share of sales with trade-ins involving negative equity hit 44%, and the average amount of negative equity reached $5,571 (figure 1). Both are new highs. Given the circumstances, it appears that consumers with negative equity fared much better in April 2020 compared to the previous year. This positive trend can be evidenced by a series of metrics. While the average amount financed went up by nearly $5,000, the average loan term stayed flat at 77 months; the average APR decreased from 7.3% to 4.7%, due to more attractive financing offers from automakers; the average total interest paid over the life of a loan financed was approximately $3,000 less compared to April 2019. In the current environment driven by the coronavirus pandemic, automakers have been offering higher than usual financing incentives, which benefits consumers. Many consumers have rolled their negative equity into a new vehicle purchase and automaker incentives, including low interest rates and longer terms, could net them a similar or even lower car payment.

Figure 1: One Decade of April Negative Equity within Auto Industry



Drury, I. (Edmunds, 2020). Negative Equity Is Surging During Coronavirus Generous Financing Offers Could Help Consumers Get Financially Healthy Again.

Negative Equity Poses Real World Challenges for Insurance Providers, Lenders and Consumers

With the previously mentioned factors contributing to negative equity held by consumers, what happens when a major accident causes a total-loss on the vehicle?

When a vehicle carrying negative equity is deemed a total loss by the insurance provider, a string of events are set into motion that affect the consumer, lender and insurance carrier. Assuming the consumer did not have GAP (guaranteed auto protection) insurance, the loan still must be satisfied. Since the loan balance is higher than the insurance company's settlement check, the consumer must either continue to make payments to the lender until the loan is paid off or arrange for additional financing to pay off the balance. In other words, the repayment terms of the loan do not change. The lender would still get paid, but you can imagine many consumers may not want to pay for a car loan with no car attached to it. Insurance carriers also find themselves in a difficult position as they want to retain the policyholder and insure any new car purchased while the consumer (their customer) is trying to get the balance of the loan reduced as much as possible to mitigate their obligation to the lender.

For many years, the industry addressed total loss vehicle claims via phone, fax and email. Insurance carriers and lenders had to frequently communicate back and forth throughout the process until a claim was resolved. Many weeks would pass, and the follow-up would leave much to be desired. Insurance carrier customers would frequently go months without a vehicle waiting for their claim to be resolved. The entire total loss claim process put strain on the insurance carriers, auto lenders and frustrated consumers. So, what is the best solution for insurance carriers, lenders and consumers alike?

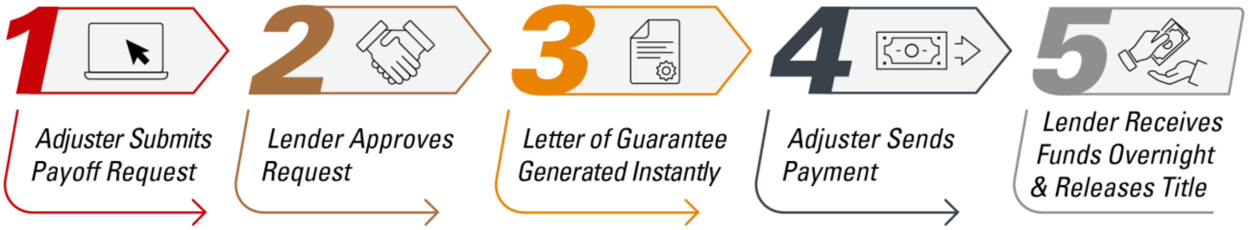
The Opportunity to Improve Efficiencies with Negative (and Positive) Equity Transactions

The glaring opportunity—to create a more efficient process for insurance providers and lenders to resolve negative equity claims—called for enabling connectivity far beyond traditional methods. Creating a bridge between providers and lenders would reduce or eliminate mailing documents, lost checks, endless phone calls and faxes, confusion over where to send titles and documents, uncertain payoff amounts, difficulty in getting a letter of guarantee, and lost time between all these processes. A better way for providers and lenders to communicate and facilitate transactions would deliver efficiencies to all parties. Improving the process for everyone involved would require building and facilitating a digitized communication portal between insurance providers and lenders that would get loans paid faster, creates greater visibility to progress and expedite the settlement process.

How IAA Solved Loan Payoff Challenges

Through their close relationships with insurance providers, lenders and others throughout the automotive industry, IAA (NYSE: IAA) set out to solve the inefficiencies and challenges related to negative equity claims. IAA already possessed the technical expertise to deliver a solution given they connect global vehicle buyers and sellers with their IAA AuctionNow™ digital marketplaceto facilitate the marketing and sale of total loss, damaged and low-value vehicles. So, having the technical expertise and a reputation for being an innovator and industry problem solver, IAA was well positioned to completely transform the processes for handling negative equity claims.

Figure 2: Streamlined Process Flow of the IAA Loan Payoff™ Solution



In 2019, after two years of development and testing, IAA launched Loan Payoff™, an innovative solution that significantly streamlines the loan payoff process and eliminates the challenges and inefficiencies associated with total loss transactions. IAA's solution is easy to use and eliminates excess tasks, inefficient and outdated methods and multiple touchpoints, allowing providers and lenders to expedite the settlement process (figure 2) and reduce costs.

Many of the other lien payoff solutions offered within the industry do not have the comprehensive, multi-tiered lender network as with IAA's, to connect back to the insurance companies.Those products operate as call centers doing manual work for insurance adjusters versus using technology to advance the process. Further, these lien payoff solutions cannot deliver an auto-generated letter of guarantee nor address all payoff types, they simply only address positive equity transactions, ignoring in excess of 63% of the total loss liens in question.

IAA is the Clear Loan Payoff Category Leader

Services to providers and lenders through IAA Loan Payoff are unmatched by any other offering within the category. IAA's Loan Payoff solution offers insurance carriers and lenders an extensive list of transformational advantages:

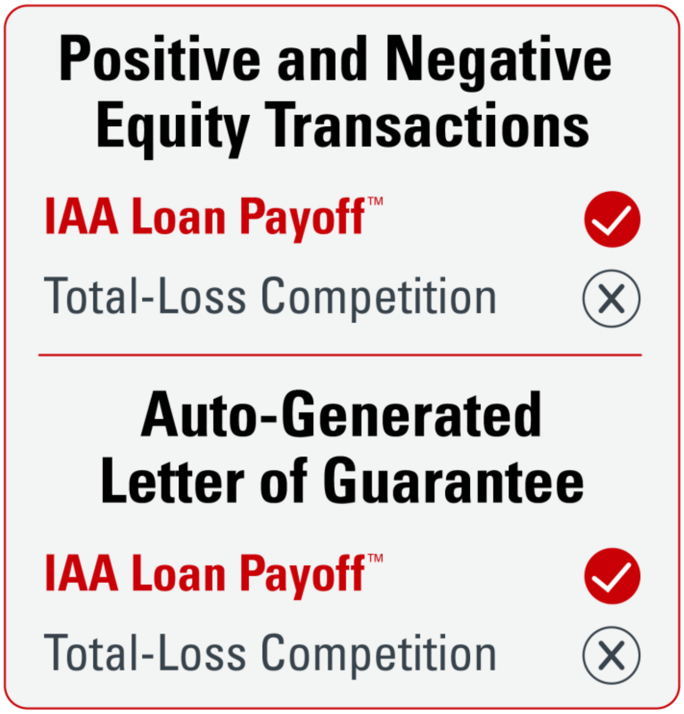
1. Provides a secure online portal that connects insurance carriers and lenders to simplify the vehicle loan payoff process for total loss and delivers actionable transparency by informing lenders of a possible total loss claim and dramatically reduce the need for back-and-forth phone calls, emails and faxes.

2. Enables insurance companies and auto lenders to efficiently process total loss claims in larger volumes, while also reducing operational costs.

3. Is the only total-loss solution available that can handle both negative equity and positive equity transactions – a one stop for all payoff types.

4. Is the only total loss solution that provides an auto-generated Letter of Guarantee for all lenders on the IAA network, saving time and resources for insurance providers and lenders.

5. Can address more complex net payoff transactions, including provider-backed GAP insurance.



Click here to view IAA's Statement Regarding Forward Looking Statements.

6. On average takes under 2 days for insurance carriers to receive a letter of guarantee from the date the record is submitted versus the industry standard of 10+ days based on feedback from lending industry professionals.

7. Delivers significant overall time savings. Data from Q1 2021 shows an average time savings of 12 days from assignment to settlement, on both positive and for negative equity transactions combined.This allows insurance providers and auto lenders to spend more time servicing their customers and to focus on the customer experience instead of communicating back and forth to resolve claims.

An Unparalleled History of Growth and Continued Momentum

IAA's industry expertise, focus on innovation, and problem-solving capabilities allowed them to create the industry's unparalleled total loss solution. Since its introduction IAA Loan Payoff has experienced exponential growth.

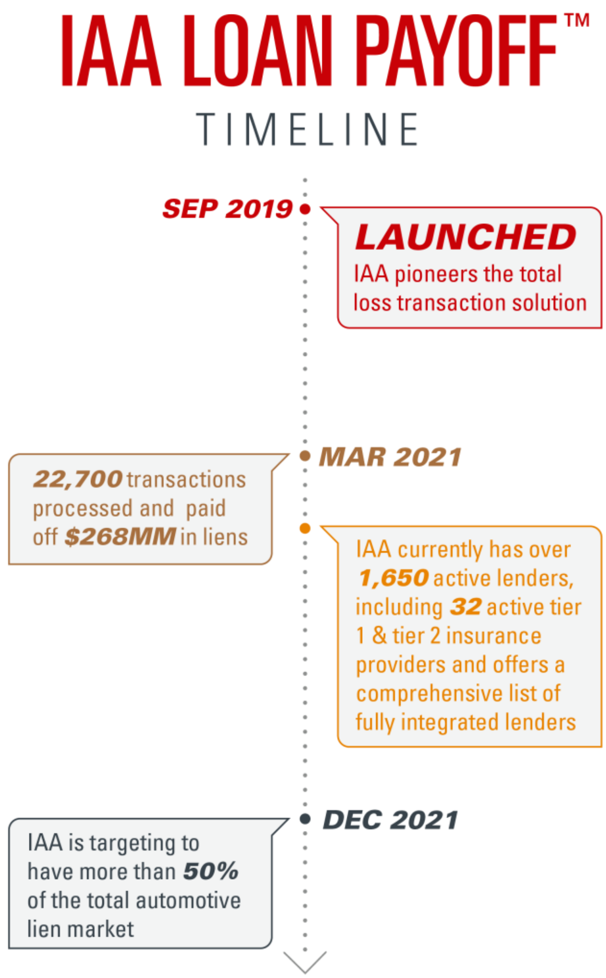
When IAA Loan Payoff was released in September of 2019, they processed more than $1M in loans the first week.

In 2020, IAA completed over 56,000 transactions and paid off over $495MM in liens.

IAA has already paid off $268MM in liens paid off and 22,700 transactions through March 26, 2021.

IAA Loan Payoff has over 1,650 active lenders and includes 32 active tier 1 and tier 2 insurance providers.

IAA is continually onboarding new lenders and insurers to expand the network of users. IAA Loan Payoff continues to grow because IAA pioneered and perfected the loan payoff solution and is delivering top-notch service and customer experience.



High Levels of Value and Service Drive Customer Loyalty for IAA Loan Payoff™

IAA Loan Payoff has experienced unprecedented growth over the years and the unrivaled benefits of IAA Loan Payoff provide a clear path toward insurance provider and lender industry solutions.

Delivering measurable and tangible results to customers can be considered the truest test for IAA Loan Payoff. What do IAA Loan Payoff customers have to say about their experience with the product?

> *As an early adopter of IAA Loan Payoff™, we continue to see*
> **IMPROVED EFFICIENCY FOR OUR CLAIMS TEAMS.**
> *This has streamlined our total loss process; and, as portal participation grows, we expect to see even further reduction in our overall timeline processing salvage.*
>
> *– Top Tier Insurance Company*

Future Auto Lending Industry and Negative Equity Trends

Rising levels of negative equity may continue at least into the near term. There are several economic factors that could affect current negative equity trends including, consumer demand for new or used vehicles, interest rates, access to financing, future automaker incentives, and auto loan terms. Increased auto loan terms for example, are a major contributor to the negative equity trends, and according to Experian the average auto loan term in Q3 of 2020 was 69.68 months for new vehicles and 65.15 months for used.

Automotive consumers are becoming increasingly more comfortable with online purchases. An ever-increasing consumer sentiment for digital sales interactions is about twice that of traditional models (McKinsey & Company, 2020). Industries in general recognize that remote selling models are becoming the next normal, and some are already preparing for that in response to consumer demand (McKinsey & Company, 2020). Digital solutions in an ever-increasing digital world will continue to be a critical part of addressing negative equity loans. IAA's Loan Payoff™ solution is positioned well to serve insurance providers and lenders in the future digital landscape, alleviating hardship and potential downtime, while also helping lenders and insurance carriers effectively manage their customer relationships.

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