CALIFORNIA LEGISLATURE

STATE CAPITOL
SACRAMENTO, CALIFORNIA
95814

October 6, 2016

The Honorable Richard Cordray
Director
Consumer Financial Protection Bureau
1700 G Street NW
Washington, DC 20552

Re: Comments on proposed rulemaking on payday, vehicle title, and certain high-cost installment loans; Docket number CFPB-2016-0025 or RIN 3170-AA40

Dear Director Cordray:

As elected representatives, we respectfully urge the Consumer Financial Protection Bureau (CFPB) to issue a strong federal payday lending rule that puts an end to the payday, car title, and high-cost installment loan debt trap nationwide. We appreciate the Bureau's efforts to curb these predatory practices, and we recognize that this is not an easy task.

In California, payday lenders charge on average 366% APR.[1] Annually, these high cost lenders drain $507,873,939 in payday fees and $239,339,250 in car title fees, a significant loss both to borrowers and to the overall state economy.[2] Furthermore, the majority of payday loans are made to repeat borrowers, as 67% of California payday loans are taken out on the same day that a previous loan is repaid, and 90% are taken out within 60 days of repayment of the previous loan.[3]

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1 California Department of Business Oversight, "California Deferred Deposit Transaction Law – Annual Report and Industry Survey," 2016, http://www.dbo.ca.gov/Licensees/payday_Lenders/payday_lenders.asp
2 Center for Responsible Lending, "Payday and Car Title Lenders Drain $8 Billion in Fees Every Year", 2016, http://www.responsiblelending.org/research-publication/payday-and-car-title-lenders-drain-8-billion-fees-every-year
3 Table 21, page 108, CFPB SUPPLEMENTAL FINDINGS ON PAYDAY, PAYDAY INSTALLMENT, AND VEHICLE TITLE LOANS, AND DEPOSIT ADVANCE PRODUCTS, http://files.consumerfinance.gov/f/documents/Supplemental_Report_060116.pdf

Additionally, payday and car title lenders in our state have been migrating to larger loan amounts, offering abusive high-cost longer-term loans over $2,500, structured with terms that last months to years and have no limit on interest rates.[4] A recent report by the California Department of Business Oversight found that in 2015, nearly 55% of loans between $2,500 - $4,999 had APRs of 100% or higher.[5] At these high rates, lenders have little incentive to underwrite – often leading to high rates of default - and they continue to profit despite making loans that ultimately harm borrowers.

Payday lenders' ability to seize money directly out of borrowers' bank accounts and car title lenders' ability to threaten repossession of a borrower's car means that lenders exert extraordinary leverage over borrowers to collect payments, causing borrowers to re-borrow or default on other bills such as a rent or medical care. These high-cost unaffordable loans are detrimental to any community, but have a disproportionate impact on our African American and Latino neighborhoods. In California, payday lenders are twice as likely to be located in communities of color than in white communities, even after accounting for income.[6]
Also at risk are the state's more than 1.8 million veterans. Unlike our active duty military, our veteran families are not protected by the 36% rate limit under the Military Lending Act.

The core principle of the CFPB's proposal is the right approach – requiring lenders to ensure that a loan is affordable without having to re-borrow or default on other expenses. However, some of the details must be strengthened in order for this approach to truly work and protect Californians from predatory lenders. Specifically, the rule should apply that ability to repay standard to every, single loan where a lender can take control over a borrower's personal property – be it the borrower's checking account, car or paycheck. There should not be any exceptions. Additionally, the rule should include protections to ensure that borrowers can't be stuck in so-called two-week loans for three months or more. Finally, for the rule to be effective it must protect against repeat refinancing and other tricks and traps that are really just taking out new loans to pay off old loans.

We look forward to seeing a final rule that is as strong as necessary to protect all Californians and we appreciate the chance to offer this comment.

Sincerely,

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4 Center for Responsible Lending, "Predatory Payday and Larger Installment Loans Overshadow Emerging Market for Smaller, Less Expensive Installment Loans in California," December 2015, http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_california_payday_dec2015.pdf

5 California Department of Business Oversight, "Annual Report, Operation of Finance Companies Licensed Under the California Finance Lenders Law," 2016, http://www.dbo.ca.gov/Licensees/Finance_Lenders/pdf/2015_CFLL_Aggregated_Annual_Report_FINAL.pdf

6 Center for Responsible Lending, "Predatory Profiling: The Role of Race and Ethnicity in the Location of Payday Lenders in California," 2009, http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/predatory-profiling.pdf

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STATE OF CALIFORNIA
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October 7, 2016

The Honorable Richard Cordray, Director
Monica Jackson, Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street, N.W.
Washington, D.C. 20552

RE: Comments on Proposed Rule for Payday, Vehicle-Title, and Certain High-Cost Installment Loans; Docket No. CFPB-2016-0025 / RIN 3170-AA40

Dear Director Cordray and Ms. Jackson:

I write to support the proposed rule published by the Consumer Financial Protection Bureau (Bureau) to strengthen protections against harmful payday and small-dollar lending practices. This rule will create the first nationwide regulatory floor for the payday lending industry, while maintaining the prerogative of states to further strengthen their consumer protection laws and regulations as they see fit. I strongly support the Bureau's proposal to require a meaningful "ability-to-repay" standard and to curb collection abuses, as well as its proposals for structural protections to help protect consumers from being trapped in long-term, unaffordable debt. Together with California's lending laws, the Bureau's proposed rule will bring needed protections to vulnerable California consumers who take out small-dollar loans, which too often are predatory and create a debt trap for fixed- and low-income consumers.

Payday and Small-Dollar Lending in California

Payday loans are prevalent in California, and many consumers fall into debt traps similar to those seen throughout the country. Californians who need short-term emergency access to cash are getting stuck in a destructive and unaffordable cycle of repeat high-interest loans that they cannot afford to repay. The average annual percentage rate (APR) for payday loans in California is 366 percent.[1] In 2015, more than 1.8 million California consumers took out

[1] California Department of Business Oversight, *Summary Report: California Deferred Deposit Transaction Law – Annual Report and Industry Survey* 7 (2015).

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12.3 million payday loans at an average loan amount of $237; this represents a total of almost $4.2 billion, a 32 percent increase in aggregate dollar amount from 2013.[2] As the California Department of Business Oversight's 2015 survey report on payday lending shows, most payday loans in California are made to repeat borrowers. Over 95 percent of payday loans were made to repeat borrowers, with consumers taking an average of 6.5 loans. The number of consumers who obtained ten payday loans was 40 percent greater than the number of consumers who obtained just one payday loan during the year (462,334 compared to 323,870 consumers). About 90 percent of the fees collected from payday loans came from consumers who took out three or more payday loans during the year, and more than 60 percent of the fees came from consumers who borrowed seven or more times during the year.[3] Roughly 60 percent of consumers for these loans had average annual incomes of $30,000 or less.[4] There are nearly 2,000 licensed payday loan locations in California[5] (substantially more than the number of McDonald's restaurants), with many of these locations in counties with high poverty rates and low education levels.[6] Put simply, short-term loans with triple-digit interest rates are trapping vulnerable Californians in a crippling cycle of long-term, unaffordable debt.

California law provides some protections for consumers who take out loans up to $2,500. In California, payday lenders can lend up to $300, including a maximum 15 percent fee, for a maximum 31-day term. (Cal. Fin. Code §§ 23035-23036.)[7] Lenders typically make loans for a two-week term, and consumers pay a fee that can amount to an APR as high as 459 percent. Some structural protections exist for these loans. Lenders are prohibited from providing a payday loan to a consumer if the consumer has an earlier payday loan in effect (Cal. Fin. Code § 23036(c)), and lenders may not permit a consumer to pay off all or a portion of one payday loan with the proceeds of another (Cal. Fin. Code § 23037(a)). There is a maximum $15 fee for a dishonored check. (Cal. Fin. Code § 23036(e).) Additional restrictions and disclosures are required. (*See* Cal. Fin. Code § 23035 et seq.) Separately, under California's Finance Lenders Law, a graduated scale of interest-rate caps applies to non-payday loans up to $2,500. (Cal. Fin. Code § 22303 et seq.)

California's Department of Business Oversight has also developed an innovative pilot program to increase consumer access to responsible installment loans of $300 to $2,499 as an alternative to predatory small-dollar loans. The "Pilot Program for Increased Access to Responsible Small Dollar Loans," which took effect on January 1, 2014, encourages innovation by allowing participating lenders to charge marginally higher interest rates than otherwise

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[2] *Id.* at 6, 11.
[3] *Id.* at 6, 7, 30, 39.
[4] *Id.* at 8.
[5] *Id.* at 10.
[6] James R. Barth et al., Milken Institute, *Where Banks Are Few, Payday Lenders Thrive: What Can Be Done About Costly Loans* 7 (2013).
[7] Payday loans are referred to as "deferred deposit transactions" under California's Deferred Deposit Transaction Law, and are secured by the consumer's personal check. (*See* Cal. Fin. Code § 23035 et seq.)

allowed under California law and requiring them to underwrite loans to determine ability and willingness to repay, report loans to credit bureaus, provide some financial education to consumers, and adhere to other provisions designed to protect consumers.

<u>Comments on Proposed Rule</u>

I support the Bureau's proposed rule, which will provide important consumer protections for payday, vehicle title, and certain high-cost installment loans. The Bureau's proposed rule will complement California's existing small-dollar lending laws and create a regulatory floor upon which California may build to better curb small-dollar lending abuses and protect California consumers against predatory lending practices. As discussed below, I support the Bureau's proposals and encourage the Bureau to strengthen its provisions to further protect consumers.

- **Require a meaningful "ability-to-repay" standard.**
  Consumers often cannot afford to both repay their loan and meet ongoing financial obligations, leading them to fall into a debt trap. I strongly support the Bureau's proposed "full-payment" test. This test will require lenders to determine whether the consumer can afford the full amount of each payment when it is due and still meet basic living expenses and major financial obligations without re-borrowing or defaulting. Requiring lenders to determine ability to repay a loan is important to protect consumers and promote responsible lending. I also agree with the proposal to require lenders, for short-term loans, to determine whether a consumer has the ability both to make the payments on the loan and to meet his or her basic living expenses and major financial obligations for a period of time beyond the term of the loan without needing to re-borrow and, for longer-term loans, to account for the possibility of volatility in the consumer's income, obligations, or basic living expenses during the term of the loan.

  I suggest a change, however, to proposed comment 5(b)-2.iii to the ability-to-repay standard. This proposed comment would provide that evidence of whether a lender's ability-to-repay determinations are reasonable may include the extent to which the lender's determinations result in delinquency, default, and re-borrowing and, notably, how these rates compare to those of other lenders. To avoid perpetuating high default and delinquency rates across the industry, and also to avoid unintentionally incentivizing aggressive collection tactics and other means to artificially lower default rates compared to other lenders, I recommend that the Bureau not use comparison with other lenders as a formal factor to establish whether a lender's determination of ability to repay is reasonable.

- **Include meaningful structural protections, and increase "cooling off" periods.**
  The Bureau's proposed rule will permit lenders the option of making certain loans under alternative standards without conducting a "full-payment" test. I believe requiring an ability-to-repay analysis for all payday and small-dollar loans would better protect consumers by setting a clear regulatory expectation that lenders provide safer loans that

consumers can afford. If, however, the Bureau allows alternatives to its ability-to-repay requirements, I strongly support the proposed structural protections and further encourage the Bureau to consider additional or increased protections for vulnerable consumers.

In particular, I support the Bureau's proposed structural protections for alternative short-term and longer-term loans, including presumptions of inability to repay, mandatory "cooling off" periods, and maximum limits of indebtedness per six-month or 12-month periods. These requirements will help prevent long-term debt created by repeat, unaffordable loans.

As part of the process under the Small Business Regulatory Enforcement and Fairness Act (SBREFA), the Bureau previously proposed treating a short-term alternative loan taken out within 60 days of a prior short-term loan as part of the same loan sequence, with a rebuttable presumption of inability to repay the subsequent loan unless the consumer could show improved financial circumstances, and proposed a mandatory 60-day cooling-off period after three loans in a sequence. In the proposed rule, however, the Bureau shortened both of these time periods from 60 days to 30 days. I believe the prior 60-day proposals would provide greater consumer protection and therefore encourage the Bureau to use a 60-day definition of a loan sequence and 60-day cooling-off period for alternative short-term loans. Re-borrowing within a 60-day period often will indicate that the previous loan and the current loan are beyond the consumer's ability to repay while meeting the consumer's other major financial obligations and basic living expenses. A 60-day period would better reflect the likely impact of the recent loan on the consumer's finances and is appropriate for purposes of a presumption before a lender can extend another loan without verifying a change in circumstances. The prohibition on making additional covered short-term loans after the third loan in a sequence similarly should be returned to 60 days, since a 60-day "cooling off" period better addresses the Bureau's concerns about a consumer's inability to repay a covered loan causing the need for successive covered loans and would provide greater consumer protection against cycles of unaffordable debt.

- **Curb harmful collection practices.**
  Reforms to lender collection practices are critical. I strongly support the Bureau's proposed provisions requiring notification before attempting to collect payment from consumers' accounts and limiting lenders to two attempts to collect payment unless they obtain new authorization. These provisions will limit unsuccessful withdrawal attempts, which result in excessive account fees and other harmful repercussions.

- **Prevent lender evasion.**
  I support the Bureau's proposed anti-evasion provision and applaud the Bureau for including such a provision. The anti-evasion provision is necessary to effectuate the purpose of the proposed rule, and is necessary for law enforcement to ensure consumer protection. The Bureau's example in proposed comment 19-2.i is illustrative of the need for such a provision. The Bureau's proposed rule will cover longer-term loans with an

APR over 36 percent if the lender obtains a "leveraged payment mechanism" (such as vehicle title or electronic debit authorization) within 72 hours after disbursement of the loan. A strong anti-evasion provision is necessary to prevent lenders from evading coverage under the proposed rule by routinely incentivizing consumers to agree to a leveraged-payment mechanism more than 72 hours after disbursement. Because it is difficult to anticipate all the ways in which unscrupulous lenders may seek to evade the requirements of the proposed rule, I encourage the Bureau to enact a broad, flexible anti-evasion provision.

- **Protect consumer privacy.**
  I encourage the Bureau to continue to consider consumer privacy, particularly in connection with the proposed commercially available reporting systems that contain information about consumer-borrowing history on covered loans across lenders.
  I commend the Bureau for requiring lenders to comply with the Fair Credit Reporting Act when furnishing information, and requiring lenders to comply with the Federal Trade Commission's Safeguards Rule to protect the security, confidentiality, and integrity of consumer information. Because amassing and sharing sensitive, confidential consumer information could lead to abusive lender practices and other misconduct, I encourage the Bureau to consider additional limitations on the information collected, as well as on access to and use of the registered reporting systems and consumer reports, to better protect consumers' privacy.

- **Permit states to adopt more restrictive laws and regulations.**
  The Bureau has made clear that the proposed rule does not preempt or undermine state and local laws that provide additional protections regarding payday and small-dollar loans. To the contrary, the Bureau's proposed rule preserves the ability of state and local governments to innovate and enact further measures in their jurisdictions as they deem necessary. The proposed rule does not address all harmful practices, such as triple-digit interest rates, and further state action to protect consumers from predatory lending continues to be necessary. The full range of legislative and regulatory options, including outright bans, rate caps and other consumer-protection regulations of small-dollar loans, will remain available to the states and local jurisdictions to further protect consumers.

Thank you for your continuing efforts to protect consumers. I strongly support the Bureau's proposed rule to implement meaningful reforms in the payday and small-dollar loan market.

Sincerely,

Kamala D. Harris

KAMALA D. HARRIS
California Attorney General