Been There; Done That: Banks Should Stay Out of Payday Lending

Center for Responsible Lending

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Executive Summary

Banks once drained $500 million from customers annually by trapping them in harmful payday loans. In 2013, six banks were making triple-digit interest payday loans, structured just like loans made by storefront payday lenders. The bank repaid itself the loan in full directly from the borrower's next incoming direct deposit, typically wages or Social Security, along with annual interest averaging 225% to 300%. Like other payday loans, these loans were debt traps, marketed as a quick fix to a financial shortfall. In total, at their peak, these loans—even with only six banks making them—drained roughly half a billion dollars from bank customers annually.[1] These loans caused broad concern, as the payday loan debt trap has been shown to cause severe harm to consumers, including delinquency and default, overdraft and non-sufficient funds fees, increased difficulty paying mortgages, rent, and other bills, loss of checking accounts, and bankruptcy.

Recognizing the harm to consumers, regulators took action protecting bank customers. In 2013, the Office of the Comptroller of the Currency (OCC), the prudential regulator for several of the banks making payday loans, and the Federal Deposit Insurance Corporation (FDIC) took action. Citing concerns about repeat loans and the cumulative cost to consumers, and the safety and soundness risks the product poses to banks, the agencies issued guidance advising that, before making one of these loans, banks determine a customer's ability to repay it based on the customer's income and expenses over a six-month period. The Federal Reserve Board, the prudential regulator for two of the banks making payday loans, issued a supervisory statement emphasizing the "significant consumer risks" bank payday lending poses. These regulatory actions essentially stopped banks from engaging in payday lending.

Industry trade group now pushing for removal of protections. Today, in the current environment of federal deregulation, banks are trying to get back into the same balloon-payment payday loans, despite the extensive documentation of its harms to customers and reputational risks to banks. The American Bankers Association (ABA) submitted a white paper to the U.S. Treasury Department in April of this year calling for repeal of both the OCC/FDIC guidance and the Consumer Financial Protection Bureau (CFPB)'s proposed rule on short- and long-term payday loans, car title loans, and high-cost installment loans.[2]

Allowing high-cost bank installment payday loans would also open the door to predatory products. At the same time, a proposal has emerged calling for federal banking regulators to establish special rules for banks and credit unions that would endorse unaffordable installment payments on payday loans. Some of the largest individual banks supporting this proposal are among the handful of banks that were making payday loans in 2013.[3] The proposal would permit high-cost loans, without any underwriting for affordability, for loans with payments taking up to 5% of the consumer's total (pretax) income (i.e., a payment-to-income (PTI) limit of 5%).[4] With payday installment loans, the loan is repaid over multiple installments instead of in one lump sum, but the lender is still first in line for repayment and thus lacks incentive to ensure the loans are affordable. Unaffordable installment loans, given their longer terms and, often, larger principal amounts, can be as harmful, or more so, than balloon payment payday loans.[5] Critically, and contrary to how it has been promoted, this proposal would *not* require that the installments be affordable.

Recommendations: Been There, Done That – Keep Banks Out of Payday Lending Business

- The OCC/FDIC guidance, which is saving bank customers billions of dollars and protecting them from a debt trap, should remain in effect, and the Federal Reserve should issue the same guidance;
- Federal banking regulators should reject a call to permit installment loans without a meaningful ability-to-repay analysis, and thus should reject a 5% payment-to-income standard;
- The Consumer Financial Protection Bureau (CFPB) should finalize a rule requiring a residual income-based ability-to-repay requirement for both short and longer-term payday and car title loans, incorporating the additional necessary consumer protections we and other groups called for in our comment letter;[6]
- States without interest rate limits of 36% or less, applicable to both short- and longer-term loans, should establish them; and
- Congress should pass a federal interest rate limit of 36% APR or less, applicable to all Americans, as it did for military servicemembers in 2006.

Flashback to 2013

Six Banks Made Abusive Payday Loans Until 2013

Six banks were draining roughly half a billion dollars from bank customers annually before they were stopped in 2013.[7] These loans were designed in such a way that they kept customers in long-term debt, just as storefront payday loans do.

Payday loans are marketed as once-in-a-blue-moon emergency loans to help families short on cash make it to the next payday. The loan is typically a few hundred dollars, for a fee of $15-$20 per $100 borrowed. To obtain the loan, the consumer must provide the lender access to the consumer's bank account, so the lender can withdraw the loan repayment from the account on payday, before the consumer pays for any other expenses.

The problem is that there is no assessment of the family's ability to afford to repay the loan. The typical borrower will be unable to meet his or her most basic obligations and repay the payday loan debt in a two-week period. Within one pay period, families may have enough money to either repay their payday loan or meet basic expenses, but not both. So the lender flips the loan over until the next payday, which costs the borrower another high fee, and families get caught in strings of high-cost, unaffordable loans. For a $350 loan, for example, at a cost of $15 per $100 borrowed—a 391% annual interest rate for a two-week loan—a borrower pays about $52 in fees each time the loan is flipped. A borrower trapped in this cycle for ten pay periods has paid over $520 in fees for a $350 loan.

This cycle, of course, makes the family much worse off than when they took the first loan, and leads to financial—and emotional—devastation. Families often go without necessities, and may lose their bank accounts and/or file

Bank Payday Lenders in 2013

Regardless of the bank's headquarters, these banks generally made payday loans available to customers located in several states—flouting the law in states whose laws clearly prohibit such loans if made by a non-bank.

Wells Fargo Headquarters: San Francisco, CA
Prudential regulator: OCC

US Bank Headquarters: Minneapolis, MN
Prudential regulator: OCC

Regions Bank Headquarters: Birmingham, AL
Prudential regulator: Federal Reserve

Fifth Third Bank Headquarters: Cincinnati, OH
Prudential regulator: Federal Reserve

Bank of Oklahoma and affiliates Headquarters: Tulsa, OK; Prudential regulator: OCC

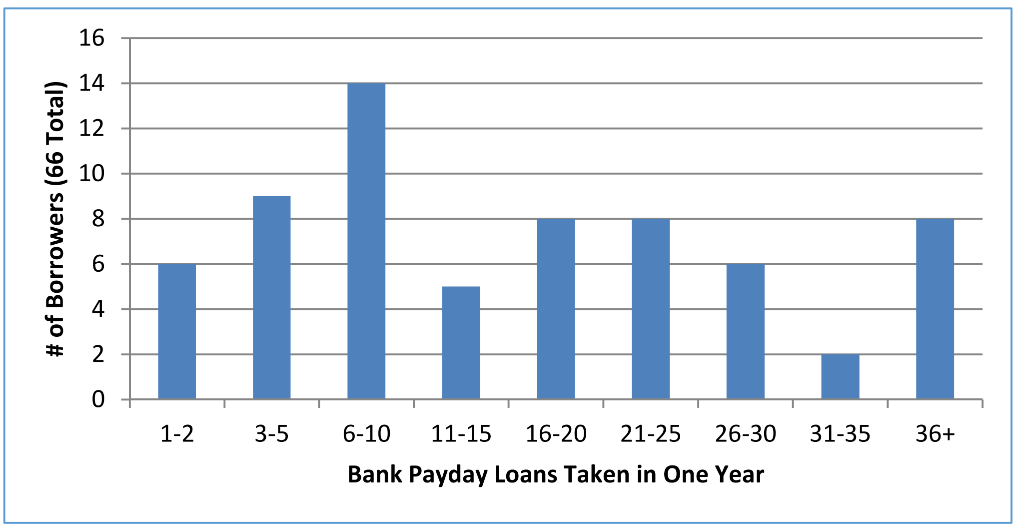
GuarantyBank Headquarters: Milwaukee, WI
Prudential regulator: OCC

bankruptcy. Since the lender has control of the bank account, it gets paid even though the loan is unaffordable for the consumer, and the lender makes most of its revenue from these trapped families.

Bank payday loans worked the same way as loans from payday lenders. And since the bank had full access to the customer's account, it could take payment from the customer's next direct deposit, which routinely left the customer short on cash and then with another triple-digit loan.

In 2011, the Center for Responsible Lending (CRL) published the first data validating that bank payday loans were a debt trap. The median bank payday borrower had 13.5 loans in a year and was in bank payday loan debt at least part of six months annually. The CFPB published its own consistent findings in 2013, showing that borrowers spent an average of 114 days during the year in this triple-digit interest debt. As the following chart based on CRL's data illustrates, over half of borrowers had more than ten loans annually; over 36% had more than 20 loans annually; and over 12% had more than 30 loans annually.

Figure 1: Bank Payday Loans in One Year (2011)



Banks Did Not Determine the Borrower's Ability-to-repay the Loan

The root of the problem with banks' payday loans, as with other payday loans, is that they were made based on the lender's ability to collect, rather than the borrower's ability to repay the loan while continuing to meet ongoing expenses. And in fact, lenders make more money when the borrower cannot afford repayment, while meeting other financial obligations, because the lender makes another triple-digit loan to the borrower to pay those expenses and keeps the borrower stuck in debt.[8] Moreover, a bank has an exceptionally strong ability to collect its own payday loan because the bank has total control over all the funds that flow into the checking account and can repay itself immediately.

The Devastating "Debt Trap"
"Debt trap" has become a common way to describe payday loans, and appropriately so. Yet the label's prevalence shouldn't desensitize us to the profound pain—financial, psychological, emotional—that a debt trap inflicts on one stuck in its grip. This harm can pervade every aspect of a person's finances, every facet of a person's life. Often, the person's family members experience the harm, too. The debt trap, in the words of those who have been there, is a "living hell."

See, e.g., Williams, Diane S. "Getting Out of the Debt: Part 2 of a series." Public Employee Press, District Council 37. (Quoting a payday loan borrower who asked not to be identified.) *http://www.dc37.net/news/pep/3_2012/420_payday_loan.html. Additional examples on file with CRL. (This*

Ineffective "Safeguards" Did Not Prevent a Cycle of Debt

Banks often pointed to what they called "safeguards" on their payday loans, which they claimed prevented customers from becoming stuck in debt. But the data, as shown above, clearly bore out that these features did not prevent a debt trap. Indeed, these "safeguards"—including installment plans and brief "cooling-off periods," when banks would not extend the customer another payday loan for a short period following repayment of one or more loans—were the same "safeguards" that non-bank payday lenders have long touted but that have proven ineffective in that context as well.[9]

Payday Loans by Banks Caused Substantial Harm To Vulnerable Customers

Bank payday loans were proven to operate the same as payday loans by storefronts, which evidence has long demonstrated cause substantial harm to consumers. These harms include the direct financial cost of long-term, high-cost indebtedness, as well as the psychological distress of being trapped in debt with a coercive repayment device for a sustained period of time; the direct harms from delinquency and default, including overdraft and non-sufficient funds fees; and sweeping collateral consequences, including increased difficulty paying mortgages, rent, and utility bills,[10] delinquency on child support payments,[11] delinquency on credit card debt,[12] delaying medical care,[13] loss of checking accounts,[14] and bankruptcy.[15]

The nexus between bank payday loans and high-cost bank overdraft fees is particularly troubling. Overdraft fees are triggered when a customer's checking account lacks sufficient funds for a transaction but the bank pays the transaction anyway, charging a fee averaging about $35 per overdraft. Often, the transactions are small debit card transaction averaging only about $20; the financial institution could easily decline these transactions at no cost to the customer rather than pay them and charge an overdraft penalty fee on each one. The bank repays itself the amount of the overdrafts and the fees in a lump sum—which can easily be hundreds of dollars—from the customer's next incoming deposit, typically about three days later. These fees cost consumers billions of dollars annually, with most disproportionately borne by account holders already struggling to keep their account balances positive. They hit lower income customers hardest and often lead to bank account closure, driving consumers out of the banking system altogether.[16]

Payday lenders, including bank lenders, have promoted payday loans as an alternative to overdraft fees.[17] But rather than bank payday loans having served as a substitute for overdraft fees, data show that customers tended to incur both high interest on bank payday loans *and* high-cost overdraft fees.[18]

The CFPB found that a quarter of the bank payday borrowers most heavily steeped in the cycle of debt incurred an average of 18 or more overdraft or non-sufficient funds fees during the 12-month period.[19] Further, last year, the CFPB published data on overdrafts after discontinuance of most bank payday loans, finding that following discontinuation of the product, former bank payday borrowers, compared to non-bank payday borrowers, did not incur an increase in overdraft or NSF fees or account closure.[20] These findings are consistent with what consultants selling bank payday loan software long promised banks: that payday lending would result in little-to-no "overdraft revenue cannibalization."[21] They also confirm other research finding that non-bank payday loans often exacerbate overdraft fees, leading to checking account closure.[22]

Ultimately, payday loans harm vulnerable populations. CRL's research on bank payday loans in particular found that over one-quarter of bank payday borrowers were Social Security recipients, making these customers over twice as likely to have had a bank payday loan as bank customers as a whole.[23] The CFPB also found that a significant share of payday borrowers—nearly one in four—reported some form of public assistance or other benefits or retirement funds as an income source.[24]

> "[T]he $550 that Wells Fargo took was half of my monthly income… Without it, I couldn't pay my rent and other expenses… A few times I tried to not take out another advance, but to do that I had to let other bills go… I never made it two full months without having to borrow after paying the last advance."
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> *Wells Fargo customer in 2013 testimony before Congress*

One such consumer, a 69-year-old woman who relied on Social Security for her income, testified before Congress in 2013 about her experience with a Wells Fargo payday loan. She noted that "[t]he $550 that Wells Fargo took was half of my monthly income... Without it, I couldn't pay my rent and other expenses... A few times I tried to not take out another advance, but to do that I had to let other bills go... I never made it two full months without having to borrow after paying the last advance."[25]

Payday loans generally also cause particular harm to communities of color, leaving them even more disproportionately underserved by the banking mainstream.[26] Communities of color have historically been disproportionately detached from the traditional banking system, a disparity that persists today. About 18 percent of African American and 16 percent of Latino households are unbanked, compared to 3 percent of white households.[27] And payday loans, with their high association with lost bank accounts,[28] drive families out of the banking system and exacerbate this disparity.

Bank Payday Loans Were Met by Broad, Fierce Opposition

Payday lending by banks was met by fierce opposition from virtually every sphere—the military community,[29] community organizations,[30] civil rights leaders,[31] faith leaders,[32] socially responsible investors,[33] state legislators,[34] and members of Congress.[35] Bank payday lending also motivated "move-your-money" campaigns.[36] It led groups managing programs aiming to bring people into the banking mainstream to establish policy that excludes banks making high-cost payday loans from the program.[37] And multiple lawsuits involving bank payday loans were filed.[38]

States that prohibit or significantly restrict payday lending also strongly opposed payday lending by banks. But banks made payday loans not only in states that permit payday lending but also, through the doctrine of federal preemption and related law, in many of the states that prohibit or meaningfully limit the product from non-bank lenders. In North Carolina, a state that does not permit payday lending, public outcry and state attorney general opposition led Regions Bank to stop making its payday loans there even before federal intervention.[39]

> Rev. DeForest B. Soaries, jointly with nationally prominent African American ministers, called for "an end to usury, an end to 300% interest rates, and an end to enslavement to both payday lenders and the banks now offering equally dangerous products."
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> *An Emancipation Proclamation from Payday Lending, 2013; see note 33 herein.*

Meaningful Reform in 2013 Effectively Ended Payday Lending By Banks, For the Time Being

Banks got out of the payday lending business in 2013, for the most part,[40] following the OCC's and FDIC's guidance and the Federal Reserve Board's supervisory statement. The OCC/FDIC[41] guidance advised banks to assess the ability of their customers to repay the loan based on income and expenses.[42] The Federal Reserve's statement emphasized the consumer risk of bank payday lending, including the risk of unfair and deceptive practices and highlighting the CFPB's findings of sustained and harmful repeat usage.[43] In addition, in 2015, the Department of Defense updated rules under the Military Lending Act that made bank payday loans exceeding 36% annual percentage rate illegal if made to active servicemembers or their dependents.[44]

In 2016, the CFPB proposed rules addressing short- and long-term payday loans, car title loans, and high-cost installment loans (CFPB Proposed Rule), whether made by banks or non-banks, requiring—with certain exceptions that CRL strongly opposes—lenders to determine the borrower's ability to repay before making the loan. Accompanying the proposal, the Bureau released the most extensive record to date on the harms of payday lending.[45] This record included the finding that borrowers of bank payday loans, following the end of bank payday lending, were no more likely than non-borrowers of bank payday loans to experience increased incidences of overdrafts or non-sufficient funds, to use non-bank payday loans, or to experience long-term increases in account charge-offs.[46] This research offers evidence that counters bank claims that bank payday loans protect consumers from overdraft fees and other payday loans.

2017: Banks Push to Make Debt Trap Loans Again

Now, banks and others have renewed efforts to permit unaffordable payday loans by banks. Taking advantage of a trend toward deregulation—and efforts to erode consumer protections—at the federal level, banks are seeking access to their customers' funds through these debt trap loans again. The ABA's white paper to Treasury, calling for repeal of the bank payday guidance and the CFPB Proposed Rule, resurrects long-debunked industry claims touting the "reasonable limits" and "efficient" underwriting of payday loans from banks. And it asserts that, with the end of bank payday lending, "[c]onsumers lost another convenient, fair, and valued source of small dollar credit within the regulated banking industry."[47]

Meanwhile, a separate proposal threatens to open the door for high-cost payday installment loans.

A PTI limit of 5% is not an affordability, or an ability-to-repay, requirement. It excludes the consideration of expenses altogether. Payday installment loans are repaid over multiple installments instead of in one lump sum, but the lender is still first in line for repayment and thus lacks incentive to ensure the loans are affordable. These loans, often made by the same lenders that make lump sum payment payday loans and still carrying triple-digit interest rates, can be as harmful, or even more harmful, than the balloon payday loans.[48]

> Unaffordable installment loans, given their longer terms and, often, larger principal amounts, can be as harmful, or more so, than balloon payment payday loans.

Yet a proposal is calling for federal banking regulators to establish special rules for banks and credit unions that would endorse unaffordable payday installment loans.[49] The proposal would permit high-cost loans, without any underwriting for affordability, for loans with payments taking up to 5% of the consumer's total (pretax) income (i.e., a payment-to-income (PTI) limit of 5%).[50] This proposal has been endorsed by the Pew Charitable Trusts and by some banks, including three of the six that made payday loans.

For individuals with relatively low incomes—which is typically the case for payday loan borrowers[51]—an assumption that debt is affordable based merely on the ratio of that debt to the borrower's income is not a safe assumption.[52] Consider a family of four at the federal poverty level of $24,300 annually, $2,025 monthly. A 5% PTI standard would assume that the borrower has an extra $101 each month, or $1,215 annually, that he or she can spare toward service of payday loan debt. Even under the best circumstances, this often will not be the reality. And the PTI standard ignores altogether exacerbating factors like the family's existing debt load or challenges meeting regular expenses.

Existing loan performance data also call deeply into question the suitability of a 5% PTI standard. CFPB's research found extraordinarily high default levels on online installment loans even at PTI ratios of 5% or less. For one lender in the Bureau's data whose loans included both storefront and online loans, 28 to 30% of loans with PTI of 5% of less defaulted, excluding loans with first-payment defaults.[53] For all loans for which the origination channel was unknown—about half the dataset, or 1.25 of 2.5 million loans—the Bureau found default rates of 38 to 40% at PTI of 5% or less, including first-payment defaults.[54]

CRL's analysis of checking account data shows that smaller payday loan payments were no less likely to incur overdraft or NSF fees than larger payments. CRL analyzed online payday loan payments from a database of consumer checking account activity for its 2015 paper, *Payday Mayday*.[55] The payday loan payment sizes in this panel were typically much smaller than a typical payday balloon payment, with about 42% of all the payments less than $100. Yet the analysis found that payments even at these smaller dollar amounts were often associated with significant borrower distress, as evidenced by NSF/overdraft activity occurring in the two weeks following a payment. (Fifty percent of such overdrafts occurred the same day as the payday payment, and the average number of days between the payment and the NSF or overdraft was 2.7.) Many of the payday payments that were associated closely in time with an overdraft were for small amounts: Half were $100 or less and over a third were $50 or less.

Figure 2: Distribution of the Payday Payment Amounts Followed Closely by an Overdraft

Range	# of Payments in This Range	Percent of Payments in This Range
$25 or less	29	4.5%
$25.01-50.00	194	29.9%
$50.01-75.00	46	7.1%
$75.01-100.00	59	9.1%
$100.01-150.00	119	18.3%
$150.01-250.00	36	5.5%
$250.01 or more	166	25.6%
Grand Total	**649**	**100.00%**

A PTI limit of 5% for banks with no interest rate limit risks increasing non-bank predatory lending. Even assuming that loans to payday borrowers with 5% PTIs were affordable—again, not a reasonable assumption—there is little indication that banks will actually make these loans. And even if they do make these loans, there is little evidence that more affordable bank-issued products will reduce unaffordable products. To the contrary, they may well bourgeon them.

First, banks have had the option for decades to make more affordable installment loans, but instead they chose high-cost payday loans and high-cost overdraft fees. And indeed, so long as banks can continue to generate $17 billion annually in overdraft and nonsufficient fund fees, much of which is from the same financially vulnerable customers who might take payday installment loans, it is unlikely banks will markedly increase reasonably priced small dollar lending to those customers. (A CFPB rulemaking is needed to address overdraft abuses.)[56]

> "I never considered going to one of those payday loan stores because I knew they had a reputation for charging really high interest rates… I thought that since banks were required to follow certain laws, they couldn't do what those payday loans people were doing."
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> *Wells Fargo customer in 2013 testimony before Congress*

Second, while the ABA endorsed *a* payment-to-income standard, it has expressed substantial doubt that 5% is high enough to induce banks to make the loans.[57] Individual banks that have expressed interest in a 5% PTI standard, as well as other bank trade associations endorsing it, have also hedged, stating that "experience may suggest that a different percentage is appropriate over time."[58]

Further, evidence suggests that competition does not drive out predatory practices. Responsible mortgage loans, which were long being made, did not drive out the predatory subprime loans that lead to the foreclosure crisis. Reasonably priced credit cards did not keep out the abusive subprime fee harvester cards that proliferated prior to 2008 regulatory and Congressional interventions.

And critically, bank loans under a PTI program would not likely have an interest rate limit. Thus, by sanctioning 5% PTI, non-cost restricted loans, regulators would not only permit high-cost unaffordable lending by banks, but they risk *bolstering* predatory lending by non-banks. Over half of states have interest rate limits on longer-term loans, but the sanctioning of a 5% PTI limit would give non-bank lenders a purported rationale to weaken or remove extremely effective interest-rate limits in favor of a weak PTI standard, weakening consumer protections throughout the country.

For the above reasons, a coalition of over 500 civil rights, consumer, labor, faith, veterans, seniors, and community organizations from all 50 states, strongly supported that the CFPB's proposed ability-to-repay requirements for payday loans did not include an exception based on a 5% PTI standard.[59]

Recommendations: Been There, Done That – Keep Banks Out of Payday Lending Business.

To protect consumers from abusive bank payday lending, CRL recommends the following:

- The OCC/FDIC guidance, which is saving bank customers billions of dollars and protecting them from a debt trap, should remain in effect, and the Federal Reserve should issue the same guidance;
- Federal banking regulators should reject a call to permit installment loans without a meaningful ability-to-repay analysis, and thus should reject a 5% payment-to-income standard;
- CFPB should finalize a rule requiring a residual income-based ability-to-repay requirement for both short- and longer-term payday and car title loans, incorporating the additional necessary consumer protections we and other groups called for in our comment letter;
- States without interest rate limits of 36% or less applicable to both short- and longer-term loans should establish them; and
- Congress should pass a federal interest rate limit of 36% APR or less applicable to all Americans, as it did for military service members in 2006.

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[1] CFPB reports that the market was roughly $6.5 billion in advances at its peak in 2013. Bureau of Consumer Protection, 12 CFR Part 1041, Payday, Vehicle Title, and Certain High-Cost Installment Loans; Proposed Rule, 81 Fed. Reg. 47864, 47884 (July 22, 2016), *available at* https://www.gpo.gov/fdsys/pkg/FR-2016-07-22/pdf/2016-13490.pdf (CFPB Proposed Rule). Banks charged from $7.50 to $10.00 per $100 borrowed, computing to a range of $487.5 million (if every customer were charged $7.50) to $650 million (if every customer were charged $10.00).

[2] American Bankers Association White Paper, Small Dollar Credit (April 2017), *available at* http://www.aba.com/Advocacy/Documents/SmallDollarWhitePaper2017Apr.pdf. The Consumer Bankers Association (CBA) also continues to tout that "deposit advance products were carefully designed to ensure strong safeguards at reasonable prices." CBA comment to CFPB on CFPB Proposed Rule (Oct. 7, 2016), *available at* http://consumerbankers.com/sites/default/files/CBA%20Small%20Dollar%20Comment%20-%20CFPB-2016-0025%20RIN3170%E2%80%93AA40.pdf.

[3] Letter to CFPB endorsing a 5% PTI standard signed by Guaranty Bank, Regions Bank, and Fifth Third Bank, and The Pew Charitable Trusts, among others (Oct. 6, 2017), *available at* https://www.regulations.gov/document?D=CFPB-2016-0025-142119

[4] The Pew Charitable Trusts, A Year After CFPB Proposed a Rule for Small Loans, Borrowers Still Await Reform (June 9, 2017), http://www.pewtrusts.org/en/research-and-analysis/analysis/2017/06/09/a-year-after-cfpb-proposed-a-rule-for-small-loans-borrowers-still-await-reform.

[5] Diane Standaert and Peter Smith, *Payday and Car Title Lenders' Migration to Unsafe Installment Loans*, Center for Responsible Lending at 1 (Oct. 2015) *available at* http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_brief_cartitle_lenders_migrate_to_installmentloans.pdf (CRL, *Migration*); CRL, Consumer Federation of America (CFA), and National Consumer Law Center (NCLC) (on behalf of its low income clients), joined by Americans for Financial Reform, National Coalition for Asian Pacific American Community Development (CAPACD), The Leadership Conference on Civil and Human Rights, League of United Latin American Citizens (LULAC), NAACP, National Council of La Raza, and People's Action Institute, to the Consumer Financial Protection Bureau (CFPB) on its Proposed Rule on Payday, Vehicle Title, and Certain High-Cost Installment Loans at 165 *et seq.* (Oct. 7, 2016), *available at* http://www.responsiblelending.org/research-publication/comment-cfpbs-proposed-rule-payday-and-car-title-lending (CRL/CFA/NCLC Comments on CFPB Proposed Rule); *see also* CFPB Proposed Rule, Market Concerns—Longer-Term Loans.

[6] CRL/CFA/NCLC Comments on CFPB Proposed Rule.

[7] CFPB reports that the market was roughly $6.5 billion in advances at its peak in 2013. Bureau of Consumer Protection, 12 CFR Part 1041, Payday, Vehicle Title, and Certain High-Cost Installment Loans; Proposed Rule, 81 Fed. Reg. 47864, 47884 (July 22, 2016) (CFPB Proposed Rule), *available at* https://www.gpo.gov/fdsys/pkg/FR-2016-07-22/pdf/2016-13490.pdf. Banks charged from $7.50 to $10.00 per $100 borrowed, computing to a range of $487.5 million (if every customer were charged $7.50) to $650 million (if every customer were charged $10.00).

[8] See description of this cycle at CFPB Proposed Rule, Market Concerns—Short-Term Loans, "Lender practices" section, 81 Fed. Reg. 47922-23.

[9] See Uriah King and Leslie Parrish, *Springing the Debt Trap: Rate caps are the only proven reform*, Center for Responsible Lending (Dec. 2007), *available at* http://www.responsiblelending.org/payday-lending/research-analysis/springing-the-debt-trap.pdf. CRL examined millions of loans across several states that adopted so-called "best practices" to ostensibly reform payday loans. Nevertheless, there was no measurable reduction in repeat borrowing. For example, over 60 percent of all loans from these states went to borrowers with 12 or more transactions in a year. *See also* CFPB Proposed Rule discussion of the ineffectiveness of existing cooling off periods and installment off-ramps, 81 Fed. Reg. 47931-32, 47975.

[10] B. Melzer, *The Real Costs of Credit Access: Evidence from the Payday Lending Market*, (2011), Oxford University Press (Melzer, 2011), *available at* http://bit.ly/10M01tZ.

[11] B. Melzer, *Spillovers from Costly Credit* (2010), *available at* http://bit.ly/10FsYmE.

[12] Agarwal, S., Skiba, P. M., & Tobacman, J., *Payday loans and credit cards: New liquidity and credit scoring puzzles?* NBER Working Paper (2009), *available at* http://bit.ly/RtDsXx.

[13] Melzer, 2011.

[14] Research has shown that payday lending is linked with increased rates of involuntary bank account closures, which makes routine financial transactions more expensive and risky. *See* D. Campbell, A.S. Jerez, & P. *Tufano*, *Bouncing Out of the Banking System: An empirical analysis of involuntary bank account closures,* Harvard Business School (2011), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1335873.

[15] One study found that payday borrowers nearly doubled their chances of filing for bankruptcy compared with households of similar financial status who were denied a payday loan. P.M. Skiba & J. Tobacman, *Do Payday Loans Cause Bankruptcy?* (2008) SSRN working paper, *available at* http://bit.ly/UhdRNJ.

[16] *See*, *generally*, Rebecca Borné, Peter Smith, and Rachel Anderson, *Broken Banking*: *How Overdraft Fees Harm Consumers and Discourage Responsible Banking Products*, Center for Responsible Lending (May 24, 2016), *available at* http://www.responsiblelending.org/research-publication/how-overdraft-fees-harm-consumers-and-discourage-responsible-bank-products (CRL, *Broken Banking*).

[17] For example, Wells Fargo noted its payday loans were less expensive than overdrafts (i.e., its own overdraft fees that it charged). *See*, *e.g*., Kevin Burbach et. al., *Big Banks' quick-cash deals: Another form of predatory lending?*, MinnPost, (Feb.

4, 2013) ("In their defense, banks said the emergency loans are less expensive than overdrafts."); Wells Fargo's Direct Deposit Advance Service Agreement and Product Guide, Effective May 14, 2012 (providing a chart comparing borrowing $300 for 30 days as costing $22.50 with the deposit advance (payday loan) product versus $70 with overdraft (assuming two overdraft items at $35 each) and also stating: "If you find yourself in a situation where the funds in your . . . checking account may be insufficient to cover checks or other items that will post to your deposit account, you may choose to advance from [the direct deposit advance] service to avoid the overdraft . . . . The Direct Deposit Advance service is an expensive form of credit, and while the advance fee may be lower than an overdraft or insufficient funds fee, you may want to consider speaking with a banker regarding overdraft protection options that may be available to you.")

[18] CRL found that nearly two-thirds of bank payday borrowers incurred overdraft fees, and these borrowers were three times as likely to incur overdraft fees as bank customers as a whole. Rebecca Borné and Peter Smith, *Triple Digit Danger: Bank Payday Lending Persists*, Center for Responsible Lending (March 2013), *available at* http://www.responsiblelending.org/payday-lending/research-analysis/Triple-Digit-Bank-Payday-Loans.pdf (CRL, *Triple Digit Danger*). The CFPB's analysis found similar results, with 65 percent of bank payday borrowers incurring overdraft fees, which was more than three-and-a-half times the portion of customers eligible for a bank payday loan who did not take one out. CFPB White Paper, Payday Loans and Deposit Advance Products at 41 (2013), *available at* http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf.

[19] CFPB White Paper, Payday Loans and Deposit Advance Products at 42 (2013), *available at* http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf.

[20] CFPB Supplemental Findings on Payday, Payday Installment, and Vehicle Title Loans, and Deposit Advance Products at 39 (June 2016) (CFPB Supplemental Findings), *available at* http://files.consumerfinance.gov/f/documents/Supplemental_Report_060116.pdf.

[21] Fiserv, Relationship Advance program description, retrieved from http://www.relationshipadvance.com/ in August 2011, on file with the Center for Responsible Lending.

[22] Susanna Montezemolo & Sarah Wolff, *Payday Mayday: Visible and Invisible Payday Lending Defaults*, Center for Responsible Lending (March 2015), http://www.responsiblelending.org/research-publication/payday-mayday-visible-and (CRL, *Payday Mayday*); CFPB Online Payday Loan Payments (April 2016), *available at* http://files.consumerfinance.gov/f/201604_cfpb_online-payday-loan-payments.pdf. The Bureau quantified bank fees triggered when funds were insufficient on longer-term loans, as well as subsequent lost bank accounts. It found that about half of borrowers paid a nonsufficient funds (NSF) or overdraft fee. These borrowers paid an average of $185 in such fees, while 10% paid at least $432. It further found that 36% of borrowers with a bounced payday payment later had their checking accounts closed involuntarily by the bank.

[23] CRL, *Triple Digit Danger*; analysis on file with CRL. These findings, based on 2011 checking account data, are consistent with our analysis of 2010 data, which found that nearly one-quarter of all bank payday borrowers were Social Security recipients, who were 2.6 times as likely to have a bank payday loan as bank customers as a whole. R. Borné, J. Frank, P. Smith, and E. Schloemer, *Big Bank Payday Loans: High interest loans through checking accounts keep customers in long-term debt* (2011), Center for Responsible Lending, *available at* http://www.responsiblelending.org/payday-lending/research-analysis/big-bank-payday-loans.pdf.

[24] CFPB White Paper, Payday Loans and Deposit Advance Products at 18 (2013), *available at* http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf.

[25] Chris Morran, *Wells Fargo Customer Explains How $500 Loan Resulted In $3,000 In Fees*, The Consumerist (July 26, 2013), https://consumerist.com/2013/07/26/wells-fargo-customer-explains-how-500-loan-resulted-in-3000-in-fees/ (quoting Annette Smith).

[26] CRL/CFA/NCLC Comment to CFPB at 22.

[27] 2015 FDIC National Survey of Unbanked and Underbanked Households at 15, *available at* https://www.fdic.gov/householdsurvey/2015/2015report.pdf.

[28] CFPB Online Payday Loan Payments at 23.

[29] *See*, *e.g.*, Testimony of Steve Abbot, former President of the Navy-Marine Corps Relief Society, Before the U.S. Committee on Banking, Housing and Urban Affairs (Nov. 3, 2011) (noting bank payday loans among the "most egregious trends"); Comments of Michael Archer, Director of Military Legal Assistance, Marine Corps Installations East, to CFPB (April 4, 2012): "Most ominously, a few large banks have gotten into the business of payday loans through the artifice of calling the loans open ended credit," http://www.regulations.gov/#!documentDetail;D=CFPB-2012-0009-0056.

[30] Hundreds of groups urged the prudential regulators to stop banks from trapping borrowers in payday loans. Letters from approximately 250 groups to FDIC, OCC, FRB and CFPB, March 13, 2013 (http://ourfinancialsecurity.org/blogs/wp-content/ourfinancialsecurity.org/uploads/2013/03/Bank-Payday-Sign-On-Letter-3-13-13-Final.pdf) and February 22, 2012 (http://www.responsiblelending.org/payday-lending/policy-legislation/regulators/Dear-Regulators.pdf). Thousands of individuals and many community groups filed comments with the OCC urging that Wells Fargo's Community Reinvestment Act rating be negatively impacted because it makes payday loans. The comment filed by CRL and NCLC is available here: http://www.responsiblelending.org/payday-lending/policy-legislation/regulators/cra-comment_wells-nov-29-2012_final.pdf.

[31] *See*, *e.g.*, Letter from Benjamin Todd Jealous, President and Chief Executive Officer, NAACP, to FDIC, OCC, FRB, and CFPB opposing bank payday lending (Feb. 21, 2013), *available at* http://www.responsiblelending.org/payday-lending/policy-legislation/regulators/NAACP-redatory-Pay-Day-Loans-to-regulators-BTJ.pdf.

[32] *See*, *e.g.*, Elaina Ramsey, Faith Groups Take On Payday Lenders, Sojourners, *available at* https://sojo.net/magazine/stub/faith-groups-take-payday-lenders (discussing a National Day of Action among faith leaders in early 2013 to address payday lending). In connection with this National Day of Action, Rev. DeForest B. Soaries, jointly with other nationally prominent African American ministers, called for "an end to usury, an end to 300% interest rates, and an end to enslavement to both payday lenders and the banks now offering equally dangerous products" in *An Emancipation Proclamation from Payday Lending.* Center for Responsible Lending, *Bank Payday Lending: Overview of Media Coverage and Public Concerns*, CRL Issue Brief, March 7, 2013, *available at* http://www.responsiblelending.org/payday-lending/tools-resources/BPD-media-coverage-3-7-13.pdf.

[33] For proxy year 2013, investors filed shareholder resolutions with the four largest banks making payday loans expressing concern about the product and requesting data, which none of the banks agreed to provide. Wells Fargo (http://www.onlineethicalinvestor.org/eidb/wc.dll?eidbproc~reso~10525); Fifth Third Bank (http://www.trilliuminvest.com/resolutions/payday-lending-fifth-third-bancorp-2013/); Regions Bank; (https://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2013/dominisocial012513-14a8.pdf); and U.S. Bank and U.S. Bank (https://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2013/congregationsisters011413-14a8.pdf).

[34] *See*, *e.g.*, "Legislative Black Caucus slams Regions Bank over payday-style loans," Raleigh News and Observer "Under the Dome," Oct. 11, 2012, *available at* http://www.cashcowadvances.com/paydayblog/legislative-black-caucus-slams-regions-bank-over-payday-style-loans.html (quoting letter from N.C. Senator Floyd McKissick, Jr., chairman of the N.C. Legislative Black Caucus, to Regions Bank, which stated: "We are deeply concerned about recent reports of Regions Bank offering its 'Ready Advance' payday loans in North Carolina . . . . High-cost, short-term balloon loans like these sharply increase the financial distress of families under economic strain"); Letter from Arizona Democratic Caucus to the prudential banking regulators, February 2012 (noting that Arizona "has spent countless state resources to study and understand the effects of [payday lending], and ultimately outlaw payday lending entirely" and calling on federal regulators to "take immediate action so that meaningful reforms taking place in Arizona and throughout the country in the name of consumer protection will not be undermined.").

[35] In January 2013, several Senators wrote the FRB, OCC, and FDIC urging action to address bank payday lending (http://www.blumenthal.senate.gov/newsroom/press/release/blumenthal-calls-on-regulators-to-act-to-stop-abusive-bank-payday-lending). In April 2013, House members did the same. For further documentation of opposition to bank payday lending, *see* Center for Responsible Lending, *Bank Payday Lending: Overview of Media Coverage and Public Concerns* at 10, CRL Issue Brief, March 7, 2013, *available at* http://www.responsiblelending.org/payday-lending/tools-resources/BPD-media-coverage-3-7-13.pdf.

[36] *See*, *e.g.*, Green America's "Break up with your mega bank" campaign focused on bank payday lending: http://breakupwithyourmegabank.org/. In addition, a 2012 North Carolina poll found that 93 percent of respondents were less likely to use a bank that makes payday loans that violate North Carolina law. North Carolina Justice Center, *Regions Bank Halts Illegal Payday Lending in North Carolina* (Jan. 16, 2013), *available at* http://www.ncjustice.org/?q=consumer-and-housing/media-release-regions-bank-halts-illegal-payday-lending-north-carolina (citing Public Policy Polling poll conducted on behalf of CRL, Sept. 2012).

[37] In 2012, "Bank On" Savannah (Ga.) adopted as policy that participating banks may not make deposit advance products in excess of 36% APR. Relatedly, Cities for Financial Empowerment, the organization that supports cities in implementing "Bank On" programs to bring people into the banking mainstream, wrote to the prudential regulators expressing serious concerns about bank deposit advance programs (https://www.fdic.gov/regulations/laws/federal/2013/2013-deposit_advance_products-c_61.pdf).

[38] For example, the following class action lawsuits were filed against Fifth Third Bank: *Klopfenstein v. Fifth Third Bank*, S.D. Ohio (Aug. 3, 2012); *Laskaris v. Fifth Third Bank*, S.D.Ca. (Feb. 12, 2013); *Jesse McQuillen v. Fifth Third Bank*, W.D. Ky. (May 7, 2013). Another was filed against Bank of Oklahoma and its affiliates (*Leland Small v. BOKF, N.A.*, 13-cv-01125), which resulted in a $1.8 million settlement, http://fastloansettlement.com/Home/FAQ.

[39] NC Justice Center, Media Release, Regions Bank Halts Illegal Payday Lending in North Carolina (Jan. 16, 2013), http://www.ncjustice.org/?q=consumer-and-housing/media-release-regions-bank-halts-illegal-payday-lending-north-carolina.

[40] Fifth Third Bank's materials state that it continues to make its loans available to those borrowers already enrolled in the product as of January 31, 2014, at a cost of $3 per $100 borrowed. https://www.53.com/doc/pe/pe-eax-faq.pdf. This equates to an excessive APR of approximately 100%.

[41] Importantly, the FDIC's guidance supplemented its existing guidelines advising banks to limit loans to 36% APR. Financial Institution Letters, *Affordable Small Dollar Loan Products, Final Guidelines*, FIL-50-2007, *available at* http://www.fdic.gov/news/news/financial/2007/fil07050a.html.

[42] OCC, Guidance on Supervisory Concerns and Expectations Regarding Deposit Advance Products (Nov. 26, 2013), *available at* https://www.occ.gov/news-issuances/federal-register/78fr70624.pdf; FDIC, Guidance on Supervisory Concerns and Expectations Regarding Deposit Advance Products (Nov. 26, 2013), *available at* https://www.gpo.gov/fdsys/pkg/FR-2013-11-26/pdf/2013-28306.pdf.

[43] Federal Reserve Board, Statement on deposit advance products (2013), *available at* https://www.federalreserve.gov/supervisionreg/caletters/CA13-07attachment.pdf.

[44] 80 FR 43560 (July 22, 2015).

[45] *See generally* CFPB Proposed Rule and in particular the following: Market Concerns—Short-Term Loans, Market Concerns—Longer-Term Loans, and the applications of the "unfairness" and "abusive" standards.

[46] CFPB Supplemental Findings at 39.

[47] American Bankers Association White Paper, Small Dollar Credit (April 2017), *available at* http://www.aba.com/Advocacy/Documents/SmallDollarWhitePaper2017Apr.pdf. The Consumer Bankers Association (CBA) also continues to tout that "deposit advance products were carefully designed to ensure strong safeguards at reasonable prices." CBA comment to CFPB on CFPB Proposed Rule (Oct. 7, 2016), *available at* http://consumerbankers.com/sites/default/files/CBA%20Small%20Dollar%20Comment%20-%20CFPB-2016-0025%20RIN3170%E2%80%93AA40.pdf.

[48] CRL, *Migration* at 1; CRL/CFA/NCLC Comments on CFPB Proposed Rule, Sec. 10, p. 165 and following; CFPB Proposed Rule, Market Concerns—Longer-Term Loans.

[49] Letter to CFPB endorsing a 5% PTI standard signed by Guaranty Bank, Regions Bank, and Fifth Third Bank, and Pew, among others, Oct. 6, 2017, *available at* https://www.regulations.gov/document?D=CFPB-2016-0025-142119

[50] The Pew Charitable Trusts, A Year After CFPB Proposed a Rule for Small Loans, Borrowers Still Await Reform (June 9, 2017), http://www.pewtrusts.org/en/research-and-analysis/analysis/2017/06/09/a-year-after-cfpb-proposed-a-rule-for-small-loans-borrowers-still-await-reform.

[51] As discussed in the CFPB's Proposed Payday Loan Rule, median incomes for these borrowers are in the $25,000-$30,000 range, while closer to $35,000 for online borrowers.

[52] The CFPB, which chose a residual income (income and expenses-based) approach rather than a debt-to-income (DTI) approach to its ability-to-repay rule, discusses related concerns about a DTI approach in the Proposed Rule: "DTI tests generally rest on the assumption that so long as a consumer's debt burden does not exceed a certain threshold percentage of the consumer's income, the remaining share of income will be sufficient for a consumer to be able meet non-debt obligations and other expenses. However, for low-and moderate-income consumers, the Bureau believes that assumption is less likely to be true: a DTI ratio that might seem quite reasonable for the 'average' consumer can be quite unmanageable for a consumer at the lower end of the income spectrum and the higher end of the debt burden range [citation omitted]. Ultimately, whether a particular loan is affordable will depend upon how much money the consumer will have left after paying existing obligations and whether that amount is sufficient to cover the proposed new obligation while still meeting basic living expenses." 81 Fed. Reg. 47941.

[53] CFPB Supplemental Findings at 17 (Figure 6), 22 (Figure 9) and n.31 at 24. CFPB's analysis of a large dataset uses a conservative definition of default, counting as defaulted loans only those charged off. *Id*. at 19. In addition, the Bureau excluded from this analysis loans with defaults before the first payment. This results in a conservative defaults figure, particularly considering that some portion of first payment defaults are due to inability to repay. At the same time, we note, as the Bureau does, that a nonprime 101 study found that the statistical correlation between PTI and defaults was substantially mitigated or eliminated when first-payment defaults were eliminated.

[54] CFPB Supplemental Findings at 18, 23, 24.

[55] CRL, *Payday Mayday*. To conduct this analysis, we used a national sample of checking account transaction data. We identified instances where accountholders had overdraft fees assessed within two weeks of a payday payment and isolated the payday payment that fell closest in time to the overdraft (in some cases accountholders had either multiple payday payments or multiple overdrafts in this period). We then looked at the distribution of the amounts of the payments.

[56] For further discussion on overdraft fees, including quantification of the $17 billion estimate and policy recommendations, *see, generally, CRL, Broken Banking*.

Notably, the 5% PTI proposal as presented to CFPB in October 2016 would permit banks to sweep consumers' accounts to a negative balance to repay the loan, just as they did with previous bank payday loans, subjecting the borrower to overdraft or non-sufficient funds fees triggered by any subsequent transaction before the account is brought to negative: "f) Do not prohibit deposit account sweeping or taking deposit account balances negative, provided that no lender-originated penalty fees apply for incurring a negative balance on payments (e.g. overdraft or NSF fees charged by the lender). i) Being able to collect payments in a simple and automated manner is critical to a bank's ability to provide small credit at a fair price. ii) Any potential risk to consumers would be more than offset by ensuring that lender-originated penalty fees would not apply." Letter to CFPB endorsing a 5% PTI standard signed by Guaranty Bank, Regions Bank, and Fifth Third Bank, and Pew, among others, Oct. 6, 2017, *available at* https://www.regulations.gov/document?D=CFPB-2016-0025-142119

[57] *See* ABA Comment to CFPB on CFPB Proposed Rule (Oct. 7, 2016), http://www.aba.com/Advocacy/commentletters/Documents/cl-SmallDollar-2016.pdf: "It is not clear, however, whether a 5% PTI standard would allow banks to earn a reasonable return on the small dollar loans made under this framework, sufficient to justify expanded bank offerings. Further market testing may help identify the level of such a PTI standard that would elicit the optimal supply of small dollar credit. Any rules ultimately adopted should afford interested market participants with room to experiment with a PTI approach. Moreover, because of the variability of cost structures, operating efficiencies, and customer default risk, we believe that rules should permit variability in the payment to income ratio."

Notably, one of the banks most out-front urging more permissive rules in this space is Fifth Third, one of only six banks that made payday loans, and the only bank to continue to make these loans after the 2013 guidance, at a cost of $3 per $100 to customers already enrolled in the product as of Jan. 31, 2014. *See* Yuka Hayashi, *Banks Want a Piece of the Payday-Loan Pie*, Wall Street Journal (May 20, 2017) *available at* https://www.wsj.com/article_email/banks-want-a-piece-of-the-payday-loan-pie-1495281601-lMyQjAxMTE3MjI0MDEyNjA1Wj/?mg=prod/accounts-wsj.

[58] Letter to CFPB endorsing a 5% PTI standard signed by Guaranty Bank, Regions Bank, and Fifth Third Bank, and Pew, among others, Oct. 6, 2017, *available at* https://www.regulations.gov/document?D=CFPB-2016-0025-142119 (noting "[a]vailable evidence suggests that a 5 percent payment-to-income ratio is suitable from the borrower's and the lender's perspectives, but these are new products and experience may suggest that a different percentage is appropriate over time.")

[59] *See* Stop the Debt Trap Campaign, *CFPB's Proposed Payday Rule Is Better Without Loophole Based Solely on a Borrower's Income* (June 2016), *available at* http://stopthedebttrap.org/wp-content/uploads/2016/06/stdt_5percent_jun2016.pdf; http://ourfinancialsecurity.org/wp-content/uploads/2016/06/Grouprelease.pdf; CRL/CFA/NCLC Comments on CFPB Proposed Rule at 248.