Center for Responsible Lending
Consumer Federation of America
National Consumer Law Center (on behalf of its low income clients)

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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
People's Action Institute

Comments to the Consumer Financial Protection Bureau Proposed Rule on Payday, Vehicle Title, and Certain High-Cost Installment Loans 12 CFR Part 104, Docket No. CFPB-2016-0025, RIN 3170-AA40

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Submitted electronically
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The **Center for Responsible Lending** (CRL) is a nonprofit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, one of the nation's largest nonprofit community development financial institutions. Over 30 years, Self-Help has provided $6 billion in financing to 70,000 homebuyers, small businesses, and nonprofits. It serves more than 80,000 mostly low-income families through 30 retail credit union branches in North Carolina, California, and Chicago.

The **Consumer Federation of America** is an association of more than 250 non-profit consumer groups that, since 1968, has sought to advance the consumer interest through research, education, and advocacy.

Since 1969, the nonprofit **National Consumer Law Center**® (NCLC®) has used its expertise in consumer law and energy policy to work for consumer justice and economic security for low-income and other disadvantaged people, including older adults, in the United States. NCLC's expertise includes policy analysis and advocacy; consumer law and energy publications; litigation; expert witness services, and training and advice for advocates. NCLC works with nonprofit and legal services organizations, private attorneys, policymakers, and federal and state government and courts across the nation to stop exploitive practices, help financially stressed families build and retain wealth, and advance economic fairness.

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Americans for Financial Reform is a nonpartisan and nonprofit coalition of more than 200 civil rights, consumer, labor, business, investor, faith-based, and civic and community groups. Formed in the wake of the 2008 crisis, we are working to lay the foundation for a strong, stable, and ethical financial system – one that serves the economy and the nation as a whole.

National Coalition for Asian Pacific Americans Community Development (CAPACD) is the first advocacy organization dedicated to the housing and community development needs of the Asian American and Pacific Islander (AAPI) community. Our mission is to improve the quality of life for low-income Asian Americans and Pacific Islanders by promoting economic vitality, civic and political participation and racial equity. We currently have over 100 members in more than 30 metropolitan areas across the country in over 19 states and the Pacific Islands.

The Leadership Conference on Civil and Human Rights is the nation's oldest and most diverse coalition of civil and human rights organizations. Founded in 1950 by Arnold Aronson, A. Philip Randolph, and Roy Wilkins, The Leadership Conference seeks to further the goal of equality under law through legislative advocacy and public education. The Leadership Conference consists of more than 200 national organizations representing persons of color, women, children, organized labor, persons with disabilities, the elderly, gays and lesbians, and major religious groups.

The League of United Latin American Citizens (LULAC) is the oldest and largest Hispanic civil rights organization in the United States. LULAC advances the economic condition, educational attainment, political influence, housing, health and civil rights of Hispanic Americans through community-based programs operating at more than 1,000 LULAC councils nationwide.

Founded in 1909, the **National Association for the Advancement of Colored People (hereinafter NAACP)** is our nation's oldest, largest and most widely known grassroots civil rights organization. The principal objectives of NAACP are to ensure the political, educational, social and economic equality of all citizens; to achieve equality of rights and eliminate racial prejudice among the citizens of the United States; to remove all barriers of racial discrimination through democratic processes; to seek enactment and enforcement of federal, state and local laws securing civil rights; to inform the public of the adverse effects of racial discrimination and to seek its elimination; to educate persons as to their constitutional rights and to take all lawful action to secure the exercise thereof.

The **National Council of La Raza (NCLR)**—the largest national Hispanic civil rights and advocacy organization in the United States—works to improve opportunities for Hispanic Americans. Through its network of nearly 300 affiliated community-based organizations, NCLR reaches millions of Hispanics each year in 41 states, Puerto Rico, and the District of Columbia. To achieve its mission, NCLR conducts applied research, policy analysis, and advocacy, providing a Latino perspective in five key areas—assets/investments, civil rights/immigration, education, employment and economic status, and health. In addition, it provides capacity-building assistance to its Affiliates who work at the state and local level to advance opportunities for individuals and families.

Founded in 1968, NCLR is a private, nonprofit, nonpartisan, tax-exempt organization headquartered in Washington, DC, serving all Hispanic subgroups in all regions of the country. It has state and regional offices in Chicago, Los Angeles, Miami, New York, Phoenix, and San Antonio.

People's Action Institute is dedicated to achieving economic, racial, and gender justice for all people in the United States. With member organizations in 29 states, People's Action Institute helps grassroots leaders shape the decisions that affect their lives and the lives of their communities. Formed by a merger of Alliance for a Just Society, National People's Action, and U.S. Action Education Fund, we provide research, analysis, and strategic support to shape pressing policy issues. People's Action Institute has long called for a financial sector that is accountable to the public and serves the needs of all our communities.

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1. INTRODUCTION AND EXECUTIVE SUMMARY

Arthur, a 69-year-old warehouse worker and grandfather of seven, started with a loan of $200 from Advance America. The loan eventually increased to $300. Every payday, rather than defaulting or coming up short on bill money, Arthur went into the Advance America store and paid a fee of $52.50 so Advance America would not deposit his check for the full loan amount. Advance America flipped the loan over a hundred times, until his total interest paid was an estimated $5,000. The clerks knew him by name and often had his paperwork ready for him when he came in.

Payday lenders have a name for consumers they see every payday: "26ers"—because they pay up every two weeks, 26 times a year. In Arthur's case, they saw him once a month rather than every two weeks, but only because his repayment came from his monthly Social Security check.[1]

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John lived paycheck to paycheck. In December 2013, he took out a car title installment loan with Loan Max for $1,715, requiring 12 monthly payments of $391 each, totaling $2,969 (243% APR). John struggled to make the first two payments and was struggling to make the third. Two months later, in February 2014, he took out a $700 payday installment loan from Check N Go to stay current on his car title loan. The payday loan required 11 biweekly payments of $110 each (247% APR). Of the first payment of $110, only $14 went toward the loan principal. John defaulted on that loan after one payment and was incurring substantial overdraft fees as the bank threatened to close his account. He has no hope of keeping up with his loan payments, much less escaping the debt trap. The extreme stress prevents him from sleeping, and he likely will be forced into bankruptcy.[2]

1.1. Introduction and Overview.

The Consumer Financial Protection Bureau's (CFPB or the Bureau) proposed rule to address payday, vehicle title, and other certain high-cost installment loans marks the culmination of over four years of extensive information gathering and data analysis by the Bureau.[3] We thank and commend the Bureau for this work, which has resulted in a robust record of evidence that strongly supports taking regulatory action to address unfair and abusive practices in this market.

As the Bureau's proposal makes clear, the record supports a rule rooted in the fundamental principle that lenders should make a reasonable determination that a borrower has the ability to repay a loan before making it. But the record also supports a stronger rule in several critical respects; indeed, it provides ample evidence that stronger protections are necessary to prevent unfair and abusive practices.

[1] Loan documents and notes from conversation with borrower on file with CRL.
[2] Loan documents and notes from conversation with borrower on file with CRL.
[3] CFPB, Proposed Rule to Address Payday, Vehicle Title, and Certain High-Cost Installment Loans, 81 Fed. Reg. 47864 (July 22, 2016) ("Proposed Rule).

Our recommendations are informed by five principal evidence-based concerns. Together, these concerns form the lens through which we view each proposed provision. The Bureau shares these concerns, and yet we fear that they are not consistently assigned the weight they warrant.

First, unaffordable payday and vehicle title loans severely harm the communities we represent. "Debt trap" has become a common way to describe these products, and appropriately so. Yet the label's prevalence must not desensitize us to the profound pain—financial, psychological, emotional—that a debt trap inflicts upon 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."[4]

Second, these markets are driven by unique and powerful misaligned incentives between the borrower and the lender. The Bureau's comprehensive presentation of its extensive findings leaves no doubt that payday and vehicle title lenders routinely disregard a borrower's ability to repay because the combination of the loan's high cost and the lender's ability to extract or coerce repayment establishes the incentive to make unaffordable loans. Because the Bureau cannot generally address cost and does not propose prohibiting the extraordinary leverage these lenders have, the rule will not fundamentally alter that perverse incentive. So the substantive restrictions must be strong enough to protect borrowers despite that incentive.

Third, any visible sign of borrower distress is strong evidence that a loan is unaffordable, due to three circumstances combined: (1) the lender's ability to extract repayment; (2) the typical timing of the payment to coincide with the borrower's payday, ahead of the borrower's other obligations and expenses and when a borrower's funds are likely at their *highest*; and (3) the significant chance that the bank will pay the transaction, through overdraft, despite nonsufficient funds. Together, these mean that repayment does not mean affordability, and that a single sign of distress on a loan, like a bounced or late payment, is very often evidence of unaffordability. The Bureau recognizes these realities to varying degrees throughout the proposal, but several of its most critical proposed provisions are not fully consistent with them.

Fourth, lenders are shifting both their short-term loan practices and their short-term loan borrowers to longer-term loans. Short-term borrowers are typically more financially distressed than today's longer-term borrowers. This shift means that tomorrow's longer-term loans carry even greater risk of harm than today's longer-term loans do, warranting more protective rules in that market than the Bureau has proposed.

Fifth, as the Bureau also finds, payday and vehicle title lenders have proven themselves, time and again, shrewd evaders of law and regulation.[5] The only rational expectation is that these lenders will aim to respond to this rule no differently, and indeed there is already evidence to support this expectation. Thus, the proposal must do more to anticipate and prevent predictable evasions. Lenders may object to the complexity of the rule. But attention to detail and to possible evasions is necessary

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[4] 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.

[5] An exception is a fee-inclusive interest rate limit of around 36%, which lenders have not been able to evade, but which the Bureau lacks the statutory authority to establish.

to provide clarity as to what is expected and what is not permitted in an industry that cannot be expected to comply with the spirit of the rule.

Finally, many states do not permit high-cost payday or vehicle title loans at all, enforcing comprehensive state interest rate limits. The Bureau recognizes in its proposal that these interest rate limits, which the Bureau lacks the authority to establish, provide stronger protections than the protections provided by the proposed rule. The Bureau must take great care to avoid putting those strong state laws at risk, even as it seeks to curb abusive and unfair practices in states with little or no protection in place.

With this backdrop, we highlight our highest-priority recommendations, with more detail provided in the remainder of this executive summary:

- **Broader coverage of these high-risk loans, without exclusions or exceptions that lenders will game.** All high-cost loans with leveraged payment mechanisms or other security that coerces repayment should be included. An ability-to-repay determination should be required for all covered loans. Exceptions such as those for credit cards and student loans should be eliminated or narrowed.

- **A meaningful ability-to-repay standard that measures a borrower's actual ability to repay the loan without reborrowing while meeting other expenses.** Lender discretion must be reduced. Loans longer than six months must have an especially robust cushion for income and expense volatility. Any lender with portfolio-wide defaults over 10% should be more highly scrutinized, and high rates of delinquencies or reborrowing should not be tolerated even if they are similar to those of other high-cost lenders.

- **Effective restrictions to prevent flipping of short- or longer-term loans and perpetuation of debt traps.** Borrowers need at least 60 days to recover from the impact of a balloon payment, not just 30. *All* "short"-term loans should be limited to 90 days of indebtedness per year. Each advance on a short-term open-end loan should be treated as a new loan. For longer-term loans, much stronger rules are needed to prevent strings of unaffordable refinancings. A presumption of inability to repay should apply to refinancings before the consumer has made substantial progress in repaying the existing loan (i.e., 75% of principal) and if, in the previous 90 days, the borrower was late, had a failed payment transfer, expressed inability to pay any key expense, if the lender's payment authorization was revoked, or if the credit report shows new delinquencies since the prior loan. Exceptions to the presumption of inability to repay should be removed for loans with smaller payments and for loans with a lower APR, unless the total dollars due on all new payments is lower than the remaining payments on the original loan.

- **Stronger protections against the collateral consequences of unaffordable loans**. Payment authorization should be revoked after a single failed transfer. If the requirement of two consecutive failures is retained, failures in two consecutive months should trigger the revocation, regardless of intervening payments collected, as should any three failures in any 12-month period.

- **More support to protect consumers from illegal loans.** The CFPB should provide that making or collecting a loan that exceeds state usury rates is an unfair, deceptive and abusive practice.

A payment authorization taken for an illegal loan should be viewed as unauthorized under Regulation E, and any attempt to collect such a payment should be deemed an abusive debt collection practice.

1.2. Summary of Recommendations.

1.2.1. The Scope of the Rule is Appropriately Broad But Should Be Broader (Section 4).

The scope of the rule is essential to its success. Payday lenders have proven themselves adept at evading the scope of rules designed to cover them. The proposed scope is strong in that it applies to high-cost payday and car title loans regardless of how large they are or how long their stated term is, and it applies regardless of a lender's status as a government-insured depository institution or a tribe. But in other respects, the scope of the rule is significantly narrower than the evidence suggests it should be, and we urge the Bureau to broaden it accordingly. We make the following recommendations:

- The scope appropriately applies regardless of loan term, size, or issuer.
- Vehicle title loan coverage should not depend on whether the title is a "condition" of the loan.
- *All* high-cost loans with leveraged payment mechanisms or vehicle titles should be included. Lenders will game a rule limiting coverage to mechanisms obtained within 72-hours. Alternatively, the rules should apply to any lender that has obtained a leveraged payment mechanism from at least 25% of its borrowers.
- The 36% fee-inclusive APR must include all ancillary products, and regardless of when their cost is incurred.
- The term "leveraged payment mechanism" should be defined more broadly:
    - Payroll deduction loans should be included whether the payroll deduction is "voluntary" or not.
    - Loans where the lender retains the right to garnish wages should be covered.
    - We agree that coverage should not be limited to repayment tied to payday.
- Certain proposed exclusions from scope should be eliminated or narrowed to prevent foreseeable evasion:
    - The exclusion for credit cards should be eliminated or narrowed to lower-cost mainstream credit cards, consistent with the MLA approach.
    - The exclusion for pawn loans should be narrowed.
    - The exclusion for overdraft lines of credit should be eliminated or narrowed.
    - The exclusion for student loans should be eliminated.
- High-cost loans secured by personal property should be covered, consistent with the long-standing FTC Credit Practices Rule.
- In addition, any high-cost loan should carry an ability-to-repay requirement.

1.2.2. The Ability-to-Repay Determination Requirements Must Be Significantly Strengthened (Section 6).

The Bureau has proposed (with some exceptions) that lenders be required to make a "reasonable determination" of the borrower's ability-to-repay before making a covered loan based on the borrower's income and expenses. We strongly support this residual income approach as most appropriate for the typically lower-income, financially distressed borrower. But we fear that the details of the test leave substantial risk of unreasonable ability-to-repay determinations passing as reasonable.

We evaluate the proposed ability-to-repay test in light of three key factors, among others: (1) virtually every loan covered by this rule is a high-risk loan with extraordinary potential to inflict substantial harm on consumers; (2) lenders lack the incentive to determine ability-to-repay in light of a borrower's other obligations and expenses, given that their super-lien position and high costs will persist under the rule; and (3) many covered lenders have always relentlessly trapped borrowers in unaffordable debt and evaded laws designed to stop them from doing so.

Put another way, the evidence strongly supports that the rule should approach lenders' interest in making genuinely affordable loans, which allow borrowers to meet other obligations and expenses, with great caution. Covered lenders cannot be given the discretion or flexibility that might be appropriate in other regulations.

Relatedly, we expect that lenders will routinely manipulate any provision permitting reliance on borrower self-certification or borrower statements in their efforts to make unaffordable loans. So we oppose, under any circumstances, permitting **borrower certifications** or statements to result in projections of higher income, or lower obligations or expenses, than reliable third-party evidence supports. With that context, our recommendations follow.

We strongly support the requirement that income and major financial obligations be verified using verification evidence. Departures from verification evidence that result in higher income or lower obligations should not be permitted except, in very rare circumstances, with other reliable third-party evidence—not consumer statements. Major financial obligations should generally include payments due on **delinquent debt** that appears on the credit report or registered information system (RIS) unless there has been no activity for at least **365 days**. Claims that a consumer has only partial responsibility for **joint obligations,** other than for rental housing, should be permitted **only with verification evidence**.

With respect to rental housing:

- Rental housing should generally be required to be verified using **verification evidence**. In the limited circumstances when verification evidence is not available, the greater of a **reliable locality-based proxy** or borrower statement should be used.
- To assume **shared housing,** lenders must obtain verification evidence or other reliable third- party evidence of the shared arrangement. In addition, supervision guardrails should be established to protect against an unreasonable volume of shared housing in a lender's portfolio.
- At the very least, on any loan where there is a **presumption of inability to repay, and on a second refinance** of a longer-term loan, verification evidence of rental housing should be required in every case. Shared housing in these scenarios should be the greater of that indicated by reliable third-party evidence or a reliable locality-based estimate.

Basic living expenses should not be defined narrowly and unrealistically as only those that are deemed strictly **"necessary**," a term lenders will exploit. Instead, basic living expenses should include all **"typical expenses"** based on income, location, and household size. The examples of "reasonable methods" for projecting basic living expenses should be strengthened:

- With respect to a statistical survey approach, use of a **well-researched government survey** is the preferable approach**.**
- Analysis of **checking account activity** should be included more explicitly as a "reasonable method" **and encouraged.**
- Projections based on statistical data other than government data or based on **"other reliable methods"** should be subject to heightened scrutiny. The method must actually predict expenses, not just collection success.

The examples of "unreasonable methods" of predicting basic living expenses must be strengthened. They must not:

- set the bar too low;
- suggest that a flat percentage of income approach is appropriate no matter how low the family's income or how large the household; or
- provide that the reasonableness of an expense projection can be determined by comparing loan performance to that of similar lenders making loans to similarly situated consumers.

More specificity should be added on the requirement to consider information known to the lender, including a duty to consider:

- Information on the **credit report and registered information system (RIS)** reflecting delinquencies or defaults on covered loans, other forms of credit or debt obligations, or basic living expenses within the past year.
- **A pattern of reborrowing** is information known to the lender that should require consideration.

Short-term open-end loans are virtually always evasion products and should be regulated as such. Each advance on a short-term open-end loan should be treated as a new loan subject to its own ability-to-repay determination.

In addition, all high-cost loans should carry an ability-to-repay requirement.

1.2.3. Reasonable Ability-to-Repay Determinations Require Objectively Low Defaults, Delinquencies and Reborrowing (Section 7).

We strongly support the Bureau's emphasis that a reasonable ability-to-repay determination must be evaluated not only by looking at the lender's front-end determination but also by looking at back-end performance metrics for the lender's portfolio. As the Bureau notes, the aim of this rule is not just "procedural" requirements but success at achieving ability to repay.

The rule should require that lenders design their products, policies, and practices so that the vast majority of a lender's borrowers **actually, in practice, are able to repay** their loans while meeting other expenses without reborrowing. The elements of "while meeting other expenses" and "without reborrowing" should be incorporated more explicitly in the rule.

The success of an ability-to-repay determination should be measured **objectively**, not relative to the performance of other high-cost lenders. It should also be assessed using a number of metrics that indicate high numbers of struggling borrowers.

First, the CFPB should scrutinize closely any lender that has **default rates above a threshold rate**; we **recommend 10%**. The standard should be 5% or even lower for auto title loans and payroll deduction loans, which have extraordinarily little incentive to determine ability-to-repay and inflict especially severe harm upon default.

Second, if a lender's default rates exceed those levels—and even if they do not—the CFPB should consider a variety of factors to assess whether the lender is failing to make reasonable determinations of ability-to-repay. These factors include:

- rates of late payments and delinquencies;
- failed payments;
- reborrowing;
- loans requiring large payments relative to income, and
- the extent to which the lender achieves repayment only due to aggressive debt collection practices.

Both the level of unaffordable loans and the harm from those loans, should be factors in assessing whether the lender is engaging in unfair, deceptive or abusive practices. Harm includes the cost of unaffordable loans that consumers are burdened with and also the impact of particular debt collection practices.

1.2.4. Proposed Anti-Flipping Requirements Could Still Permit Harmful Long-Term Indebtedness in Short-Term Loans (Section 8).

The proposed rule would permit lenders to continue putting borrowers into a more than ten "short-term" loans in a 12-month period, without ever triggering a presumption of inability to repay. That is a red flag about the weaknesses of the proposal. This is largely due to two significant shortcomings addressing repeat lending: (1) the lack of a limit on the cumulative days of annual indebtedness; and (2) the use of only 30 days as the relevant time period to determine what constitutes a renewal/reborrowing/refinance after a short or balloon-payment loan.

***All* short-term loans should be limited to 90 days' indebtedness and six loans in a 12-month period.** The rule recognizes that an upfront ability-to-repay determination is not sufficient to ensure that borrowers do not get stuck in unaffordable loans; thus, it establishes the presumptions framework as well as a hard cooling-off period after three consecutive loans. While we support this approach generally, payday and vehicle title lenders' rich history of debt trap lending and of evading efforts to stop it warrant a fixed outside limit. A 90-day limit has longstanding precedent in FDIC guidelines. A limit of six loans has precedent in the FDIC and OCC's bank payday lending guidance as well as in some state laws. This is a necessary and well-founded protection, with more evidence in favor of including it than excluding it.

Loan sequences should encompass loans made within 60 days of a prior loan, not 30. With a 30-day time period, the Bureau aims to capture a typical expense cycle. But as the evidence we present shows, payday and vehicle title borrowers are likely to have expense cycles significantly longer than 30 days and to need longer than 30 days to recover from the impact of a short or balloon-payment loan. Thus, a 30-day period puts them at significant risk of receiving unaffordable loans on a repeat basis. While most reborrowing today happens in less than 30 days, that is only because it is permitted under today's rules. If the presumption of unaffordability expires after 30 days, lenders will encourage reborrowing at the 31+ day mark, consistent with how they have historically treated cooling-off periods at the state level.

We strongly support loan flipping rules not only for short-term loans but also for longer-term balloon payment loans. But the **definition of balloon payment** should include any payment more than **10% greater** than any other payment, **instead of 200% greater.** We expect this provision as drafted will be evaded. This definition is rooted in mortgage precedent, but state consumer installment laws are the more appropriate precedent, and they support a far broader definition.

In addition, to guard against short-term loan flipping:

- The exception from a presumption of unaffordability for a loan with **smaller payments** should be **eliminated.**
- The duty to consider the impact of **"outstanding loans"** should be expanded to trigger a presumption of unaffordability for defaults in the past 365 days (not 180), and lenders should be prohibited from making a loan if their own loan to the borrower is in default (i.e., +120 days delinquent).
- The presumption of unaffordability should be rebuttable only with **verification evidence.**
- The **prohibition after consecutive loans** should (1) apply after the second consecutive loan, rather than the third; (2) be extended from 30 to 90 days; and (3) apply to any combination of balloon-payment loans whether short-term or longer-term.
- The prohibition after a short-term exemption loan should be extended to **60 days.**
- The proposed **bridge loan requirements** should include all non-covered loans and should reset, rather than toll, the presumption period.
- The rule must close a large loophole that permits flipping through a **short-term open-end line of credit.** Any advance that must be substantially repaid in full within 45 days should be treated as a new loan subject to short-term closed-end flipping rules.

1.2.5. An Exemption from Ability-to-Repay for Any Covered Short-term Loans Will Permit Substantial Harm (Section 9).

We categorically oppose the exemption from an ability-to-repay requirement for certain short-term loans. There is ample precedent for finding that lending without regard to ability-to-repay is abusive and unfair. Yet we are aware of no precedent for exemptions from that standard similar to those the Bureau has proposed, particularly with respect to short-term loans.

If a loan has a cost of $15 per $100, the exemption would permit three consecutive bi-weekly payments averaging $217 each; at a price $25 per $100, the payments would average $250. All the data on short-term payday loans of which we are aware **strongly suggest that these payments will typically be unaffordable**. These data include several studies and analyses, including the Bureau's online payments study, finding that relatively smaller payments are often unaffordable for payday borrowers.

In addition, the Bureau's offered justification for this exemption is unpersuasive in light of other findings central to the rule as a whole. For example, the Bureau generally shows clear appreciation for the difficulty significant payments in short order may pose. It also acknowledges the harm caused by even a relatively short series of short-term loans.

Moreover, the suggestion that, even without an ability-to-repay requirement, lenders will have incentive to screen out borrowers without the ability-to-repay is unconvincing. So long as lenders can collect on payday, borrowers' true ability to repay is not of interest to high-cost lenders.

We support that this exemption has not been provided for vehicle title loans, while noting that the most logical conclusion drawn from the Bureau's rationale for why it has excluded vehicle title loans from the exemption is that there should be no exemption for any loans at all.

The following elements of the exemption make it particularly harmful:

- The first loan in a series as high as $500;
- A loan sequence/reborrowing construct that permits excessive unaffordable lending:
    - Permitting six $500 loans in 12 months if lenders game the insufficient 30-day reset period. A stepdown on every loan within 12 months would be most appropriate.
    - The insufficient 30-day period between a covered (short- or longer-term) balloon loan with an ability-to-repay requirement and a short-term exemption loan;
    - Permitting two series of three consecutive unaffordable loans is particularly unwarranted.
    - A limit of six loans and 90 days is too high, particularly considering it permits additional short-term covered loans outside the exemption.
- The lack of an income verification requirement encourages lax lending and will prevent the Bureau from having supervisory data it should have to analyze lending under the exemption.

1.2.6. Longer-Term Loans Warrant Enhanced Underwriting (Section 10).

High-cost longer-term loans pose particularly high risk of harm to consumers, including particularly high risk of inability to repay. Longer-term loans are not only longer by definition; they are likely to be even longer than the sequences of short-term loans. Longer-term loans are also likely to be much larger. The larger size combined with the longer term make the costs and potential harm much higher. The longer term also increases the risks of both default and collateral harms.

In some ways, the Bureau clearly recognizes these risks, but we fear that in others the proposal does not sufficiently account for them. Particularly concerning are the Bureau's statements that payday lenders can simply move borrowers into longer-term high-cost loans (as permitted by state law) with smaller, purportedly more affordable payments. These statements risk understating the difficulty many borrowers will have *sustaining* payments—even smaller ones—over time. Stronger substantive provisions must more fully recognize that challenge.

Lenders are already shifting to longer-term loans and are pushing for state legislative authorizations for longer-term high-cost loans. In addition, we discuss that evidence suggests that tomorrow's longer-term market will look more like the short-term market than it does today. Short-term covered loan borrowers are even more distressed than longer-term borrowers, and they are the longer-term borrowers of tomorrow.

The harm of longer-term loans must be addressed both with an appropriate ability-to-repay determination and, as addressed in the following section, adequate protections against refinancings that mask inability to repay. Our recommendations on the ability-to-repay determination are discussed below; we discuss refinancings in the following section.

We strongly support requiring a cushion to account for the significant income and expense volatility that should be expected over the course of a longer-term loan. But we urge the following to make the requirement more meaningful:

- Provide that the **"term of the loan"** for determining a cushion includes the actual loan term and the anticipated period by which **refinancings will extend** the original term.
- Require lenders to consider not only volatility experienced by similarly situated consumers, but also other clear indicators of volatility for the particular borrower, including **a credit report showing delinquencies** within the past year.
- Prohibit a cushion of zero and require consideration of seasonal fluctuations.
- For loans longer than six months:
  - Require a cushion based on a **lookback the length of the loan term.**
  - In the alternative, require an additional income **cushion of at least 25%**, a common measure of income volatility.
- When verifying income and major financial obligations, require a **lookback the length of the loan term.**
- Longer-term **balloon loans s**hould be required to be underwritten for **60 days following the last payment**, not 30 days.
- For **open-end lines of credit:**
  - Require **a new determination** before **increasing** a line of credit, and also after 180 days, as proposed.
  - Require lenders to **assume that an indefinite line of credit will be repaid in full within 180 days**, as proposed.
  - View certain new advances as a refinancing (discussed below).

1.2.7. Restrictions on Refinancing Longer-Term Loans Are Far Too Weak (Section 11).

The debt trap caused by unaffordable longer-term loans gets deeper and longer yet when loans are refinanced. Yet the proposed rule's approach to refinancings of longer-term loans is one of the weakest parts of the proposal. Without strengthening, it is likely to permit serial refinancings of these loans that compound and mask the borrower's inability to afford the loan. Weak treatment of refinancings also seriously undermines the rule that lenders must ensure that borrowers have enough residual income to cover basic expenses, and to weather non-catastrophic income dips and expense shocks over the course of the loan, without reborrowing.

Proposed section 1041.10 imposes a presumption on inability to repay in certain reborrowing scenarios and sets the standards for rebutting that presumption. Making a new longer-term loan is prohibited within 30 days of a short-term exemption loan, a provision we strongly support.

The standards in this section are critical to the success of the rule and to compliance with a meaningful ability-to-repay standard. Even if a loan is required to be underwritten based on the highest payment, weaknesses and uncertainties in the ability-to-repay standard may result in unaffordable loans. Refinancing of longer-term loans can mask inability to repay and cause consumer harm just as it can for short-term loans. Consequently, we support the additional protections set forth in this section.

In general, the presumptions for new loans made within 30 days of an underwritten balloon-payment loan are appropriate. However, the presumption period should run 60 days to better capture a typical expense cycle for financially distressed borrowers and to better enable consumers to recover from a balloon payment. A 60-day period is especially critical when a lender is moving a consumer from a balloon-payment loan to a longer-term loan, where there are **fewer limits** on bait-and-switch to **long-term debt**. In addition, we strongly oppose the proposed exemption that would permit a new loan immediately following a balloon loan, without a presumption, if the new loan has substantially **smaller payments, unless it also has lower total dollar costs**. That will encourage weak underwriting of balloon loans and bait-and-switch tactics to move consumers from shorter balloon loans to longer high-cost installment loans.

For non-balloon loans, the refinancing rules need much more substantial strengthening. The scope of the provision should be broadened to apply:

- When the **previous loan was repaid early (in the prior 30 days**), even if it is no longer "outstanding." Otherwise lenders will evade the rules by having borrowers pay off their old loans first and then immediately reborrow, the same or next day.
- **To new lenders,** not just the same lender, when indicia of unaffordability are detectable. If the consumer is delinquent on the prior loan, has had recent bounced payments, or has said she cannot afford the prior loan, the identity of the new lender should not affect whether a presumption of unaffordability should apply.
- To longer-term exemption lenders under § 1041.12 refinancing their **own unaffordable loan.** These loans may be quite large with large fees, and lenders may have an incentive to push refinancing to stay within the 5% default rate limit necessary to qualify for the exemption.

Lenders should be prohibited from refinancing their own delinquent loans, even after 180 days. Otherwise, they can use the debt collection process to push new loans and obtain a new payment authorization.

A broader range of circumstances should trigger the presumption of inability to repay:

- Lenders should be required to look for indicia of unaffordability in the **prior 90 days,** not merely 30. The leveraged payment mechanism will disguise unaffordability in many months, and a recent history of bounced or delinquent payments shows a struggling consumer.
- **A loan that is even one day late in the past 30 days, or more than seven days late in the past 90 days**. Lenders may contact borrowers and push refinancing before day eight to disguise inability to repay.
- **A failed payment transfer** (including failed payroll deductions)**.** A bounced payment is a strong sign of unaffordability.
- Payments **not initiated due to nonsufficient funds**. With new technologies or by taking bank account login information, lenders may learn the consumer does not have enough money to make a payment even if the payment does not bounce.
- **Revocation of payment authorizations**, unless the consumer has since made an on-time payment. The revocation may be triggered by payment failures, and consumers also revoke payment authorizations when they cannot afford the payment.
- An expression of inability to meet **major financial obligations or basic living expenses**, not just the loan payment. Money is fungible, and the ability to repay standard applies to all obligations and expenses, not just the loan payment.
- Reborrowing **before making substantial progress in repaying the loan (i.e., repaying 75% of principal),** not merely receiving a small amount of cash-out. Enforcement of and compliance with a true ability-to-repay without reborrowing test is undermined when borrowers need

more cash early in the loan term. Lenders are able to exploit that need and to extend the debt trap. A cash-out standard also pushes larger loans, a phenomenon that can already be seen in the CFPB's data.

- **New delinquencies on the credit report.** If new negative information shows that the consumer has not been able to make payments on major financial obligations or basic living expenses since the outstanding loan was taken out, that is powerful evidence of inability to repay.

When indicia of unaffordability are present, there should be **no exception to the presumption** for:

- **Loans with smaller payments.** Smaller payments on the new loan do not change the unaffordability of the previous loan, and permitting lenders to refinance their own unaffordable loans will encourage bait and switch.
- **Loans with a lower APR**, unless the total **dollar amount** of new payments is lower than those remaining. Bigger and longer loans frequently have lower APRs than shorter loans, but if a consumer cannot afford a 300% loan, that does not make a 150% loan affordable.

The term "improvement in financial capacity" should be defined to mean only an improvement in net income or major financial obligations as defined in the ability-to-repay rules. That appears to be the CFPB's intention, but the rule is not clear.

Lenders should not be permitted to use *any* type of non-covered loan as a bridge loan. Permitting any loan to bridge the 30-day cooling off or presumption period will undermine it. Lenders could use balloon loans with no payment mechanism or loans secured by a mobile phone and rely on aggressive debt collection to bring borrowers back. Bridge loans should also **completely restart, not just toll**, the 30-day period.

Only one refinancing should be permitted. There should be a prohibition on a second refinancing. Where permitted, refinancing, particularly early in the loan term, should be an occasional exception to a standard of ability to repay without reborrowing, not a routine pattern of loan flipping that compounds costs extends the debt trap of unaffordable loans secured by leveraged payment mechanisms or vehicle titles.

Open-end credit needs more protection:

- **Increases in credit lines should be viewed as a refinancing** subject to the presumption of inability to repay after a balloon payment or if indicia of unaffordability are present. An increased credit line is just like a new loan.
- In addition, **new advances** on an existing credit line should also be viewed **as refinancings and be subject to the presumption (and a potential freeze on the credit line), if indicia are present showing that the credit line is proving unaffordable.** Especially, but not only, during the periodic review of ability-to-repay, delinquencies, bounced payments, and other indicators of distress show unaffordability that should result in the credit line being frozen until and unless the consumer's financial capacity improves.
- **Advances that are repayable in 45 days** or less should be treated as closed-end short-term loans.

The CFPB should **review portfolio-wide refinancing rates**. High rates of refinancing should be evidence that the lender's underwriting standards are inadequate. The CFPB should also track data on the number of loans that meet the indicia of unaffordability but gain an exemption from it or overcome the presumption. This is especially critical if the rule retains exceptions for loans with smaller payments or lower APRs.

1.2.8. Exemption from Ability-to-Repay for Longer-Term Loans Is Vulnerable to Exploitation (Section 12).

The proposal provides two exemptions from ability-to-repay for longer-term loans. One tracks the National Credit Union Administration's Payday Alternative Loans (PAL) program and exempts loans not exceeding annual interest of 28% and a $20 application fee, up to six times annually (the PAL exemption). The other exempts loans with an APR of 36% or less, fee-inclusive with the exception of an origination fee that can be $50 or a reasonable portion of the lender's origination costs, made up to four times annually per lender, so long as the portfolio-wide default rate does not exceed 5% (the Section 12 exemption).

As proposed, the longer-term exemption loans pose risk of inflicting substantial harm for three primary reasons:

First, any exemption from an ability-to-repay requirement is inconsistent with and undermines the central principle underlying the rule. That principle matters not only for this rule, but for the significance of the ability-to-repay principle in every credit-related context, in every regulatory sphere, going forward. We understand that these exemptions were designed with the intent of excluding products currently issued by credit unions and community banks that have not been a cause for great concern of consumer harm. But the exemptions will be available to all lenders and will be vulnerable to exploitation. **The Bureau should apply the ability-to-repay principle to every covered loan.**

Second, any exemption must not sanction unreasonably high origination fees, lest the risk of substantial harm is too great. The $50 fee sanctioned on each loan in the Section 12 exemption, permitted four times annually, is too high and is not adequately supported by the data the Bureau presents. Moreover, this fee has no clear upper bound, which could result in very costly loans, particularly small ones. A high upfront fee encourages lenders to flip borrowers from one early refinance to another, adding to the risk of the substantial harm. Sanctioning a large origination fee also bolsters lenders' efforts to introduce those fees into state law, without even the limits the Bureau imposed. If this exemption is retained, the rule should limit the fee to **10% of the credit extended up to a maximum of $30 and limit the fee to one per year**. To discourage loan flipping, it should also require a **pro rata refund** of origination fees for early refinancings.

Third, the rule must be carefully designed to ensure that lenders do not use longer-term exemption loans as bridge loans to evade the provisions aimed at preventing flipping for both short- and longer-term loans. As designed, the rule does not prevent lenders from putting borrowers directly into exemption loans following an unaffordable balloon loan or any longer-term loan repaid early. This has the effect of (1) masking the unaffordability of the prior loan by tiding the borrower over until the lender can put the borrower back into a non-exempted covered loan; and (2) ultimately permitting the lender to keep the borrower in unaffordable debt indefinitely, without ever triggering a presumption of inability to repay. Thus, the rule should prohibit longer-term exemption loans from being **used as bridge loans** that have the effect of masking unaffordable loans made by the **same lender.**

In addition, we urge that vehicle title loans not be eligible for these exemptions.

Finally, we support the Bureau's decision **not** to include an exemption based solely on a **5% payment-to-income ratio** as originally included in the preliminary SBREFA outline. There is little reason to presume that a $100 monthly loan payment will be affordable for a typical, already financially distressed borrower earning $24,000 per year. Indeed, the Bureau's more recent data found that default rates on high-cost installment loans, even at payment-to-income ratios not exceeding 5%, reached 28-40%. However, payment size does matter, and we urge the Bureau to closely scrutinize the affordability of loans with large payment-to-income ratios.

1.2.9. Payment Protections Are Warranted and Should Be Stronger (Section 13).

Given the abusive and unfair practices rampant in the payments space for payday and vehicle title loans, we strongly support a failed payment trigger that requires a lender to obtain a new payment authorization.

However, based in part on the Bureau's own recently published online payments data, we urge that the trigger requiring reauthorization be one failed payment rather two. The Bureau's study found that after one payment attempt failed, only 30% of second attempts succeeded—meaning 70% of second attempts failed. The Bureau also found that 36% of borrowers who experienced a bounced payment had their checking account closed.

If the rule retains its limit of two consecutive failed payments rather than one, additional protections are needed:

- View failed payments in **two consecutive months** as consecutive failures, even if the lender was able collect re-initiated payments, fees, or biweekly payments that do not coincide with rent in between.
- An additional trigger of **three cumulative failed payments**, whether consecutive or not**, over a rolling twelve months.**
- After two consecutive failures and then a third **after a new payment authorization, a fourth attempt should not be permitted**. This is especially important after a refinancing.

We support the proposals for notice of upcoming payment transfers and of consumer rights after payment authorization is revoked. We further urge that consumers be informed of a clear **right to revoke authorization**; that **multiple payment channels** not be permitted; and that lenders be required to comply with applicable **payment network rules**.

1.2.10. The Information Furnishing Requirements to Registered Information Systems Are Essential to the Rule As a Whole (Sections 14 and 15).

The requirement to report to registered information systems (RIS) is critical to enable compliance with provisions addressing loan flipping restrictions. The reporting will also provide data on a borrower's loan performance (like delinquencies, defaults, and collections activity) on covered loans that lenders should be required to consider in making a reasonable ability-to-repay determination.

We support requiring lenders to report covered loan information **to every registered information system.** To facilitate the utility of the data across lenders and help ensure accuracy, we urge that CFPB require specific consumer identifying information with strict matching criteria.

We generally support the information the proposal requires lenders to report but urge that it be expanded. The feasibility of including more information is supported by more detailed requirements for existing state databases.

We strongly support the need for the function the registered information systems (RISs) serve in the proposed rule, and if the Bureau does not take on that function itself, we support the RIS approach. But in the interest of best protecting consumers, **we urge the CFPB to consider taking on this role itself (**via a contractor), much as the 14 states with covered loan databases have done.

With respect to RISs, compliance with the **Fair Credit Reporting Act is essential.** The Bureau should mandate the development and use of a s**tandardized data reporting format**.

We strongly urge the Bureau to **prohibit** use of RIS information for **marketing (including prescreened "offers" of credit)** and **non-credit uses such as employment and insurance**. Otherwise, the creation of these new RISs could harm consumers and make them prey to debt settlement and credit repair scams.

1.2.11. Record Retention and Reporting Requirements to the Bureau Should Be Enhanced (Section 16).

We support both the proposed compliance program and record retention requirements. But we urge requiring lenders to **retain records longer than 36 months** when needed to substantiate RIS/CRA reporting.

We also urge the Bureau to require lenders to retain **additional data** and to report it to the Bureau and State enforcement agencies, in order bolster enforcement of the rules and the ability to detect evasions. Particularly critical is reporting on the percentage of a lender's portfolio that:

- Departs from clear verification evidence;
- Has a presumption of inability to repay, relies on an exception to that presumption, or rebuts it;
- Has various metrics of loan performance, including delinquencies, defaults and other indicators that consumers are struggling;
- Results in debt collection or debt sales.

We provide a list of examples of aggregate data that will aid in enforcement of the rule.

We further urge that the Bureau **create a public, searchable database** with key information (such as default and reborrowing rates) **by state and by lender** and **publish an annual report**, including state-level data, based on the data lenders have reported.

1.2.12. The Prohibition Against Evasion Must Be Stronger (Section 17).

We strongly support a general anti-evasion provision, and indeed the history of evasion in these markets demands a strong one. We support a provision along the lines of what the proposal includes, but we urge that the Bureau do the following:

- Address any clearly foreseeable evasions within the substantive provisions of the rule itself.
- Eliminate the "intent" element of the evasion prong that risks gutting it.

- Modify the existing examples in the Commentary to support a stronger interpretation of the anti-evasion provision.
- Include additional examples of evasion.

1.2.13. The Proposed Severability Provision Is Important and Appropriate (Section 18).

We strongly support the rule's proposed severability provision: "The provisions of this rule are separate and severable from one another. If any provision is stayed or determined to be invalid, it is the Bureau's intention that the remaining provisions shall continue to be in effect."

The proposed rule is critical to protect consumers from harm. Should certain provisions be stayed or ruled invalid, there are others that would still provide substantial needed protection to consumers.

1.2.14. The Benefits of the Proposed Rule Far Outweigh Its Costs (Dodd-Frank Act Section 1022(b)(2) Analysis) (Section 19).

The Bureau's cost/benefit analysis required under Dodd-Frank § 1022(b)(2) thoroughly demonstrates that the benefits of the proposed rule far outweigh the costs. The Bureau solicits comment on its preliminary analysis, and we offer some observations, noted here and discussed further below.

First, in connection with the Bureau's duty to consider the impact on access to credit, access is most appropriately construed broadly. Households with lower credit scores are served by a range of credit products. High-cost loans drive out lower-cost ones from responsible lenders. Unaffordable payday and vehicle title loans generate their own demand for reborrowing rather than meeting consumers' credit needs. The 90 million Americans living in states without payday lending deal also with cash shortfalls without unaffordable payday loans and the harms they cause.

Second, the proposed underwriting requirements, with our proposed recommendations, are **not too costly to be feasible.** Fintech companies are eager to develop solutions that will streamline compliance.

Finally, some statements the Bureau makes in the cost/benefit analysis expose vulnerabilities in the rule and reinforce the need to strengthen it.

1.2.15. The Rule Should Make Clear that Offering or Collecting a Loan in Violation of State Law Is an Unfair, Deceptive, and Abusive Practice (Section 20).

A substantial number of states have strong laws in place to protect their residents from the harm of unaffordable payday and vehicle title loans, including usury limits. These states can and do enforce their laws with actions that have resulted in millions of dollars of debt relief and restitution. But payday lenders exploit loopholes in state laws or simply disregard state laws altogether.

The Bureau explicitly recognizes in the proposal that state usury limits are more protective of consumers than the Bureau's proposed rule. While the Bureau does not have authority to enact a usury cap, it has authority to prevent lenders from violating stronger state level protections and making illegal loans.

Even in states that do not have strong laws, licensing requirements generally apply to non-depository lenders and other limits may apply. Unlicensed loans are unlawful and may be void or uncollectible under state law.

The CFPB should protect consumers from illegal loans and strengthen the enforceability of state laws by declaring in this rule that offering, collecting, making, or facilitating loans that violate state usury, licensing or other consumer protection laws is an unfair, deceptive, and abusive act or practice. Collecting of such loans is also an abusive debt collection practice and a violation of the Electronic Fund Transfer Act if collected via electronic fund transfer.

1.2.16. Effective Date (Section 21).

The Bureau has proposed an effective date for the rule of, generally, 15 months after publication of the final rule in the Federal Register. We appreciate that the Bureau aims to balance providing consumers with needed protection while giving covered persons adequate time to comply with the rule.

We urge the Bureau to shorten this effective date to 12 months, in light of the urgent need for protection from the abusive and unfair practices the rule addresses. One year is a reasonable period of time within which to expect lenders to be compliant.

We thank the Bureau for its consideration of these recommendations, which we discuss in more detail throughout these comments. With incorporation of the suggestions we offer, this rule should be expected to significantly curtail the significant harm caused by making high-cost loans with coercive repayment devices without a reasonable determination of the borrower's ability-to-repay. This rule is a critical part of the Bureau's congressionally assigned mission to prevent unfair and abusive practices and to prevent evasions.

2. BACKGROUND

Congress established the CFPB with the intent that the Bureau would identify and prevent unfair, deceptive, and abusive practices, *and* that it would design rules to prevent evasion of those efforts. The Bureau has proposed this rule to prevent practices that the evidence supports are "unfair" and "abusive," as those standards are defined by Congress. A key element of that evidence is substantial harm to consumers, which the Bureau appropriately finds present in both the short-term and longer-term payday and vehicle title markets. (Throughout these comments, unless otherwise specified, we use "payday" and "vehicle title" loans to refer to those loans regardless of their length—i.e., including both the short- and longer-term variety.) In this section, we discuss that harm; its impact on particular communities; the growing recognition of that harm in public policy; the importance of addressing that harm in the longer-term loan market; and payday and vehicle title lenders' history of evasion, warranting a rule carefully crafted to prevent evasions. (We address the specific prongs of the unfairness and abusive tests separately, in section 5 below.)

2.1. Payday and Vehicle Title Lenders Disregard a Borrower's Ability to Repay, Evidenced by Extraordinarily High Rates of Repeat Loans, Defaults, and Overdraft/NSF Activity.

In earlier comments, we might have begun with several pages explaining that payday and vehicle title lenders disregard borrowers' ability to repay, as evidenced by high rates of repeat loans, defaults, and overdraft/non-sufficient funds activity. But that is less necessary here, as the Bureau's compilation of existing evidence, and the addition of its own extensive research, establish the most robust record to date demonstrating this pervasive practice.[6]

Instead we present a summary table of data based on the Bureau's findings as presented throughout the proposed rule. We note that in every case, the Bureau cites to broadly consistent findings from third-party research.

Summary Data Demonstrating Lending Without Regard to Ability-to-Repay

	Short-term Payday	**Short-term Vehicle Title**	**Longer-term Payday**	**Longer-term Vehicle Title**
Repeat loans:				
-% of loans reborrowed within 30 days	82%[7]	85%[8]	37%[9]	20%[10]
-Avg loan sequence length	>50% are 10 loans; 14% are 20+ loans[11]	56% are 4+ loans; 23% are 10+ loans[12]	--	--
Default rates, loan sequence (proxy for per borrower)	20%[13]	33%[14]	38%[15]	31%[16]
Repossession, loan sequence (proxy for per borrower)	n/a	20%[17]	n/a	11%[18]

The Bureau cites to similar findings by others for each data point above: repeat short-term payday loans;[19] repeat short-term vehicle title loans;[20] high refinancing rates for longer-term payday loans;[21]

[6] We include as **Appendix C** to these comments an index and summary of the research that CRL, CFA, and NCLC have conducted on payday and vehicle title lending and their impact on consumers.
[7] CFPB, Supplemental Findings on Payday, Payday Installment, and Vehicle Title Loans, and Deposit Advance Products (2016), at 103, ("Supplemental Findings").
[8] CFPB, Single-Payment Vehicle Title Lending (2015), at 10.
[9] Supplemental Findings at 15 (35% for storefront, 22% for online).
[10] Supplemental Findings at 15.
[11] CFPB White Paper, Payday Loans and Deposit Advance Products (2013), at 22 (showing the total number of transactions per borrower over 12 months) ("CFB White Paper).
[12] CFPB Single-Payment Vehicle Title Lending at 7.
[13] 81 Fed. Reg. 47930 (using 30-day definition of loan sequence, with 69% of these defaults occur in loan sequences where the borrower has reborrowed at least once).
[14] CFPB Single-Payment Vehicle Title Lending at 23.
[15] Supplemental Data at 22 (55% for online; 34% for storefront). On a per-loan basis, the default rate is 24%.
[16] Supplemental Data at 22. On a per-loan basis, the default rate is 22%.
[17] CFPB Single-Payment Vehicle Title Lending at 23.
[18] Supplemental Data at 22. 11% at both the loan and sequence level; 35% of all defaults at both loan and sequence level resulted in repossession.
[19] 81 Fed. Reg. 47926.
[20] 81 Fed. Reg. 47926.
[21] 81 Fed. Reg. 47886.

high refinancing rates for longer-term vehicle title loans;[22] loan sequence default rates for each type of loan;[23] and repossession rates.[24]

2.2. Unaffordable Payday and Vehicle Title Loans Cause Substantial Harm.

Unaffordable payday and vehicle title loans cause substantial harm. The Bureau identifies and describes this harm at length.[25] The Bureau finds that making payday and vehicle title loans without ability-to-repay causes or is likely to cause "a substantial number of consumers a high degree of harm, and a large number of consumers . . . a lower but still meaningful degree of harm."[26]

We walk through the prongs of the abusive and unfair standards at section 5 below. But we discuss harm briefly here, applying the Bureau's categorization of harms: (1) harms from long sequences of loans, (2) harms stemming from delinquency and default, and (3) collateral harms from making unaffordable payments. In addition, at **Appendix A** to our comments, over 100 borrower experiences with payday or vehicle title loans are documented. Each is coded according to the categories of harm the loan has caused. In many cases, a single loan or loan sequence causes harms in more than one category.

2.2.1. Long-term indebtedness in high-cost loans.

The Bureau recognizes the harm of long-term indebtedness in high-cost loans, even when those loan sequences do not result in default. It cites the harm of "exceedingly long loan sequences,"[27] as well as those that are relatively shorter,[28] and particularly when there is not substantial reduction of principal despite paying high costs over an extended period of time.[29]

These harms occur with short-term loans, where long loan sequences are the norm. Consumers are stuck in a debt trap, paying fee after fee with no meaningful reduction in principal. Because borrowers cannot typically afford to repay the principal, the alternative to paying the fee would be default.

These harms also occur with longer-term loans. Indeed, longer-term loans, as discussed at sections 10.2 and 10.3, can create their own debt traps that can be larger and longer than those caused by short-term loans. Repeated refinances, particularly without reduction of principal, are also a sign that the loan is unaffordable.

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[22] 81 Fed. Reg. 47888.
[23] 81 Fed. Reg. 47930 (short-term payday), 81 Fed. Reg. 47990 (longer-term payday), 81 Fed. Reg. 47991 (short-term and longer-term vehicle title).
[24] 81 Fed. Reg. 57991.
[25] Proposed Rule, particularly Market Concerns sections and the Bureau's application of the abusive and unfair practices standards.
[26] As the Bureau notes, longstanding precedent provides that substantial injury may consist of a small amount of harm to a large number of individuals *or* a larger amount of harm to a smaller number of individuals; in this case, both are present. See section 5.5 of our comments. 81 Fed. Reg. 47936.
[27] 81 Fed. Reg. 47936.
[28] Id.
[29] 81 Fed. Reg. 47974.

These harms take the form of virtually inescapable debt that drains significant funds from every paycheck and hundreds or thousands of dollars over time, as well as the psychological distress of being trapped in debt with a coercive repayment device for a sustained period of time.

2.2.2. Delinquency and default.

The Bureau also recognizes the harm stemming from delinquency and default. With short-term loans, default often occurs when the borrower is no longer able to sustain even rollover fees—far smaller than the principal amount. On a longer-term loan, default can occur when the payment becomes so unmanageable that it cannot be sustained. Default also occurs after payments start bouncing even despite bank overdraft programs that typically cover unaffordable payments in exchange for a high fee.

Direct harms from delinquency and default include (1) lender fees for bounced and late payments; (2) bank fees for bounced payments; (3) loss of one's checking account; (4) aggressive debt collection tactics; and (5) for vehicle title loans, repossession of one's car. As discussed in the next section, there are also a number of indirect harms.

The Bureau has 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.[30] These borrowers paid an average of $185 in such fees, while 10% paid at least $432.[31] It further found that 36% of borrowers with a bounced payday payment later had their checking accounts closed involuntarily by the bank.[32] The Bureau notes that other borrowers close their accounts themselves as it seems the only way to stop the payday lender's collection attempts.[33]

CRL's 2015 published study of checking account activity supports the Bureau's findings. One-third of borrowers experienced at least one incident in which their account was overdrawn on the same day that the payday lender withdrew a payment,[34] even though the payment itself did not bounce. For these borrowers, their banks honored the payday lender's debit, but the bank charged an overdraft fee for that payment and/or other debits paid during the day. We term these overdrafts "invisible defaults" because, from the payday lender's perspective, they are a successful payment, even while they signal distress for the borrower. The study further found that nearly half of payday borrowers incurred an overdraft or NSF fee in the two weeks after a payday loan transaction, and 64% paid overdraft or NSF fees at some point.

The Bureau also finds that covered loan borrowers are likely to be subject to debt collection efforts. Indeed, more than 10% of all collection-related complaints the Bureau receives relate to payday loans. Aggressive debt collection, as the Bureau notes, can jeopardize employment and future earnings and inflict psychological distress and anxiety for borrowers who are already financially distressed.[35]

[30] CFPB, Online Payday Loan Payments (April 2016).
[31] Id.
[32] Id.
[33] 81 Fed. Reg. at 47990.
[34] Susanna Montezemolo & Sarah Wolff, *Payday Mayday: Visible and Invisible Payday Lending Defaults*, Center for Responsible Lending (2015), http://www.responsiblelending.org/research-publication/payday-mayday-visible-and.
[35] 81 Fed. Reg. at 47991.

Often, the collection activities payday lenders engage in are illegal. Recent CFPB enforcement actions illustrate the abusive debt collection practices of many payday and vehicle title lenders. The Bureau found that ACE Cash Express engaged in harassing phone calls, including calling the borrower's employee or relatives; false threats to sue or criminally prosecute overdue borrowers to pressure them into additional, unaffordable loans; false threats of physical harm; and false threats to charge extra fees and report consumers to credit reporting agencies if borrowers failed to repay their loans.[36] The Bureau found that EZCORP unlawfully visited delinquent borrowers at their homes and workplaces; illegally contacted third parties, such as supervisors, references, and landlords, about borrowers' debts; called borrowers at their workplaces despite being told to stop calling; threatened borrowers with legal action despite having no intention to take that legal action; and lied to consumers that they could not stop collection calls.[37] The Bureau found that vehicle title lender TMX Finance LLC illegally exposed information about consumer debts to co-workers, neighbors, and family members, and made illegal in-person debt collection visits despite knowing that visitors were not allowed at the consumer's workplace.[38]

In addition to aggressive and often abusive debt collection, of course vehicle title borrowers lose their cars at astounding rates (the Bureau's data show 1 in 5). The Bureau appropriately describes the harm from losing one's car as "dire," noting that it "not only leads to the loss of a valuable asset but can also disrupt consumers' lives and put at risk their ability to remain employed."[39]

Appendix A includes examples of borrowers who have experienced these harms.

2.2.3. Collateral harms from making unaffordable payments.

The consequences of sustained unaffordable payments on payday and car title loans are sweeping. The Bureau acknowledges but notes that it is "unable to quantify" the extent to which a leveraged payment mechanism causes collateral injury, in terms of the borrower's ability to meet other obligations or basic living expenses.[40] Indeed, to the extent the collateral harms do not lend themselves to ready quantification, it is in large part because they are so far-reaching. They are cascading, spiraling harms. Unaffordable payments, made nonetheless because of a coercive payment device or car title, can lead to overdraft fees or late bill payments. Those can lead to additional overdraft and late fees, and perhaps a penalty rate on a credit card balance, which will likely lead to a reduced credit score. Late rent payments can lead to eviction. And these harms are just from a loan that *is repaid*.

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[36] In the Matter of ACE Cash Express, Inc., Consent Order 2014-CFPB-0008 (July 10, 2014), http://files.consumerfinance.gov/f/201407_cfpb_consent-order_ace-cash-express.pdf.

[37] In the Matter of EZCORP, Inc., Consent Order 2015-CFPB-0031 (Dec. 16, 2015), http://files.consumerfinance.gov/f/201512_cfpb_ezcorp-inc-consent-order.pdf.

[38] In the Matter of TMX Finance LLC, Consent Order, 2016-CFPB-0022 (Sept. 26, 2016), http://files.consumerfinance.gov/f/documents/092016_cfpb_TitleMaxConsentOrder.pdf. In addition to these examples, we note that CFPB sued Cash Call for collecting loans that were made in violation of state law, which were thus void under state law; see section 20 below for our recommendation that the Bureau declare it a UDAAP to collect a loan that violates state law.

[39] 81 Fed. Reg. at 47930 (citing two surveys finding that 15% of borrowers said they would have no way to get to work or school if they lost their vehicle, and a survey finding that more than 35% of borrowers were pledging the only vehicle in the household).

[40] 81 Fed. Reg. at 47995.

Nonetheless, there are numerous studies that have measured the impact of payday loans and provide insight into the effects that these loans have on borrower's broader finances. These include increased difficulty paying mortgages, rent, and utility bills,[41] delinquency on child support payments,[42] delinquency on credit card debt,[43] delaying medical care,[44] loss of checking accounts,[45] and bankruptcy.[46]

We emphasize the importance not only of all quantifiable evidence of harm, but also of the qualitative evidence the Bureau already has through the complaints database and other borrower accounts, and the additional qualitative evidence it will collect from public comments. This evidence speaks strongly to the extent to which unaffordable payments cause collateral harm, on both short-term and longer-term loans, and should be given great weight.

2.3. Payday and Vehicle Title Loans Cause Particular Harm to Financially Vulnerable Communities.

Payday and vehicle title loans typically prey upon those with few resources struggling to make ends meet. As discussed in the proposal, median incomes for these borrowers are in the $25,000-$30,000 range, while closer to $35,000 for online borrowers. Median credit scores are deep subprime or subprime, ranging from 525 to 580.[47]

These loans have a particularly harsh impact on communities of color and older Americans, as discussed below.

2.3.1. Payday and vehicle title lending disproportionately harm communities of color.

Payday and vehicle title loans cause particular harm to communities of color, which several of the undersigned groups represent. Lenders heavily market to these communities and leave them even more disproportionately underserved by the financial mainstream.

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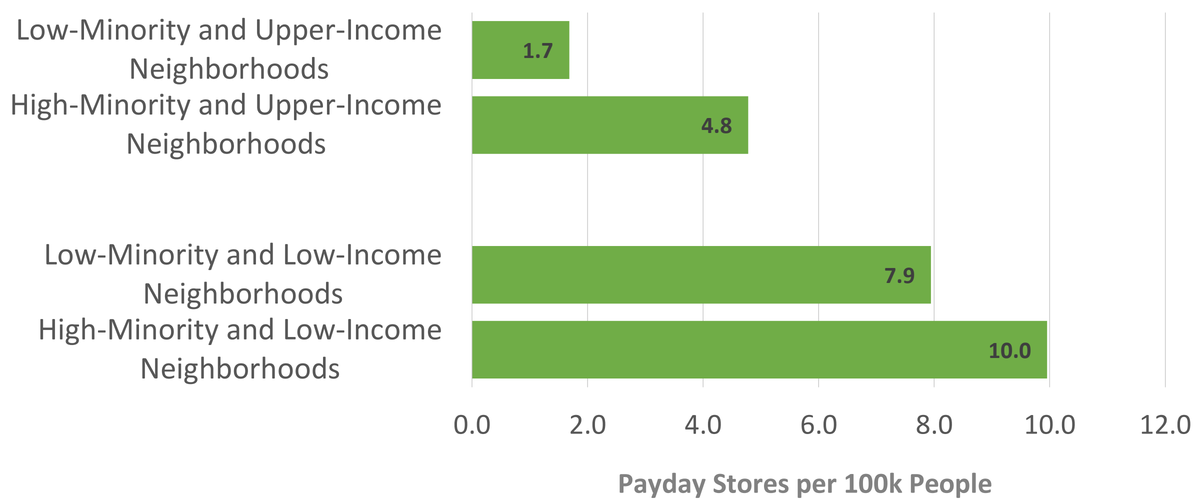
[41] B. Melzer, *The Real Costs of Credit Access: Evidence from the Payday Lending Market*, (2011), Oxford University Press, *available at* http://bit.ly/10M01tZ.
[42] B. Melzer, *Spillovers from Costly Credit* (2010), *available at* http://bit.ly/10FsYmE.
[43] Agarwal, S., Skiba, P. M., & Tobacman, J., *Payday loans and credit cards: New liquidity and credit scoring puzzles?* NBER Working Paper (2009), *available at* http://bit.ly/RtDsXx.
[44] Melzer, 2011.
[45] 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.
[46] 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.
[47] As the Bureau notes, nonprime 101 has found median VantageScore 3.0 scores of 525 for online borrowers and 532 for storefront borrowers. 81 Fed. Reg. 47921. Nonprime 101 has also found a median score of 580 for online installment borrowers. Nonprime101 Report 8. *Can Storefront Payday Borrowers Become Installment Loan Borrowers?* (Dec. 2015), https://www.nonprime101.com/wp-content/uploads/2015/12/Report-8-Can-Storefront-Payday-Borrowers-Become-Installment-Loan-Borrowers-Web-61.pdf.

Research has repeatedly found that payday lenders concentrate in communities of color.[48] Payday lenders in California were found 2.4 times more concentrated in African American and Latino communities, *even after controlling for income and a variety of other factors*.[49] Payday lenders in Florida were also more concentrated in majority black and Latino communities, even after controlling for income, as shown in the following chart.

Florida Payday Store Concentrations By Race and Income, Combined:[50]



In light of this concentration, it is unsurprising that a disproportionate share of payday borrowers come from communities of color, even after controlling for income.[51] This disparity is even more significant

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[48] Delvin Davis, Keith Ernst, Uriah King, and Wei Li. *Race Matters: The Concentration of Payday Lenders in African-American Communities in North Carolina.* Center for Responsible Lending (March 2005) *available at* http://www.responsiblelending.org/north-carolina/nc-payday/research-analysis/racematters/rr006-Race_Matters_Payday_in_NC-0305.pdf (finding that, even when controlling for a variety of other factors, African-American neighborhoods had three times as many payday lending stores per capita as white neighborhoods in North Carolina in 2005); Assaf Oron. *Easy Prey: Evidence for Race and Military Related Targeting in the Distribution of Payday Loan Branches in Washington State*, Department of Statistics, University of Washington (March 2006) (concluding based on a study of Washington State payday lenders that "payday businesses do intentionally target localities with a high percentage of African Americans.").

[49] Wei Li, Leslie Parrish, Keith Ernst, and Delvin Davis, *Predatory Profiling: The Role of Race and Ethnicity in the Location of Payday Lenders in California,* Center for Responsible Lending (March 26, 2009), *available at*: http://www.responsiblelending.org/payday-lending/research-analysis/predatory-profiling.pdf.

[50] Replicated from Brandon Coleman and Delvin Davis, P*erfect Storm: Payday Lenders Harm Florida Consumers Despite State Law*, Center for Responsible Lending (March 2016), at 7, Chart 2. The analysis is based on payday loan locations provided by the Florida Office of Financial Regulation, as of January 2016, reflecting more than 1,100 stores. Two payday lenders—Amscot and Advance America—own nearly 500 of these stores. By comparison, Starbucks has 642 Florida locations.

[51] The Pew Charitable Trusts, Safe Small-Dollar Loans Research Project, *Payday Lending in America: Who Borrows, Where They Borrow, and Why* at 9 (July 2012) (finding that, after controlling for other characteristics including income, payday loan usage was 105% higher for African Americans than for other races/ethnicities). Other studies that do not control for income also show disproportionalities. Amanda Logan and Christian E. Weller, *EZ Payday Loans: Who Borrows From Payday Lenders? An Analysis of Newly Available Data*, Center for American Progress (March 2009), summary of findings at page 1 (finding, based on the FRB's Survey of Consumer Finances conducted in 2007 and released in 2009 payday borrowers are more likely to be minorities); California

since African Americans and Latinos are much less likely to have checking accounts than whites;[52] since a checking account is typically required to get a payday loan, one might expect the concentration of payday lenders to be lower than in white neighborhoods.

Communities of color have historically been disproportionately detached from the traditional banking system, a disparity that persists today. About 21 percent of African American and 18 percent of Latino households are unbanked, compared to 4 percent of white households.[53] And payday and vehicle title loans, with their high association with lost bank accounts,[54] drive borrowers out of the banking system and exacerbate this disparity.

Payday and vehicle title lenders have promoted their products as providing access to credit in communities that have few other options. But in reality, these predatory products strip borrowers of assets, leaving them worse off, while stifling the development of responsible products—a double-edged sword. Permitting their unfair and abusive practices unfettered entrenches a two-tier financial system. One group of consumers has access to the mainstream financial system, while another is further marginalized, relegated to predatory lenders pushing debt traps, reinforcing a history of financial exploitation.[55]

2.3.2. Older Americans are particularly attractive to high-cost lenders and especially vulnerable to the harms the loans cause.

Older Americans are particularly attractive to payday and vehicle lenders and especially vulnerable to the harm the loans cause. Older Americans show greater signs of financial hardship than other age

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Department of Corporations, *Payday Loan Study* (updated June 2008), *available at* http://www.dbo.ca.gov/Licensees/Payday_Lenders/Archives/pdfs/PDLStudy07.pdf (finding that, although they represent about one-third of the overall state population, over half of California payday borrowers are African American and Latino); Skiba and Tobacman, Do Payday Loans Cause Bankruptcy?, *supra* (analysis of a database of a large Texas-based payday lender finding that African Americans (who make up approximately 11 percent of the total adult population) made up 43 percent of payday borrowers and Latinos (who make up approximately 29 percent of the total adult population) made up 34 percent of payday borrowers).

[52] 2013 FDIC National Survey of Unbanked and Underbanked Households, *available at* https://www.economicinclusion.gov/surveys/2013household/banking-status-findings/.

[53] Id. Seventeen percent of American Indian/Alaskan households and 6% of Hawaiian/Pacific Islander households are unbanked.

[54] CFPB Online Payday Loan Payments at 23.

[55] For further on our concerns about the harm payday and vehicle title loans cause communities of color, and the efforts we have long made to stop that harm, see the sampling of references cited here: http://stopthedebttrap.org/wp-content/uploads/2014/11/PayDay-loans.7-2016.pdf; http://stopthedebttrap.org/wp-content/uploads/2014/11/PayDay-loans.7-2016.pdf; http://www.civilrights.org/press/2014/payday-lending-resolution.html?referrer=https://www.google.com/; http://publications.nclr.org/bitstream/handle/123456789/1595/stop_payday_predators.pdf?sequence=1&isAllowed=y; http://blog.nclr.org/2014/04/03/avoiding-debt-cycle-problems-payday-loans/; http://lulac.org/news/pr/dont-get-caught-in-a-debt-trap/; http://lulac.org/assets/pdfs/10_Financial_Literacy_Payday_loan_case.pdf, http://stopthedebttrap.org/wp-content/uploads/2015/08/naacp_letter_obama_payday_15december2014.pdf, http://stopthedebttrap.org/wp-content/uploads/2015/08/lcchr_resolution_payday_deposit_advance_lending_12dec2015.pdf; http://ourfinancialsecurity.org/2011/04/hilary-shelton-cfpb-testimony/; http://www.responsiblelending.org/payday-lending/policy-legislation/states/Letter-JBond_Rendell-012306.pdf; http://archives.financialservices.house.gov/media/pdf/012804hs.pdf.

groups and are often less able to recover from financial distress. Coupled with recent dramatic declines in the value of their largest assets—homes and retirement assets—many older Americans also struggle with limited incomes. Nearly half of all older Americans are considered economically insecure, living on $29,425 per year or less.[56] Forty-seven percent of seniors depend on Social Security for 90% or more of their income.[57] Senior women in particular face diminished incomes because of lower lifetime earnings and Social Security and pension benefits. Not only are these incomes limited, but they are also fixed, meaning seniors are particularly unlikely to be able to address financial shortfalls by working extra hours or otherwise earning extra income.

Facing these financial hardships, older Americans are particularly vulnerable to payday and vehicle title lenders' claims of quick cash. And they are particularly attractive to lenders because Social Security benefits provide a steady source of repayment. As one payday lender described federal benefits recipients:

> *"These people always get paid, rain or shine . . . [They] will always have money, every 30 days."*—former manager of payday loan stores[58]

As another put it:

> *"[Borrowers receiving Social Security or disability] payments would come in for a small loan and write a check to the company dated the 3rd of the month, when their government checks would arrive. All the Advance America employees were required to come in early on that day, so we could quickly cash their checks and wipe out their checking accounts."*—former Advance America employee[59]

Indeed, an analysis by one researcher found that payday lender storefronts cluster around government-subsidized housing for seniors and the disabled in a number of states across the country.[60]

It is unsurprising, then, that significant numbers of older Americans become trapped in payday loans. Moreover, recent trends show that older Americans comprise a growing share of payday borrowers. The share of payday borrowers in Florida age 65 and older more than doubled over the past decade—increasing from 3.4% of borrowers in 2005 to 8.6% in 2015 (a 152.9% increase), while the share of

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[56] National Council on Aging, age 60+, 25 million out of 53 million. https://www.ncoa.org/news/resources-for-reporters/get-the-facts/economic-security-facts/.

[57] Id.

[58] Ellen E. Schultz and Theo Francis, High-Interest Lenders Tap Elderly, Disabled, *Wall Street Journal* (Feb. 12, 2008), *available at* http://online.wsj.com/article/SB120277630957260703.html [Wall Street Journal, 2008].

[59] *Bailed-Out Banks Finance Predatory Payday Lenders*, Center for Media and Democracy (Sept 16, 2010) (reporting from a GRO-MO action, September 16, St. Louis, MO, and quoting a former Advance America employee who remained anonymous because he was reportedly forced to sign a confidentiality agreement upon leaving the firm), *available at* http://www.prwatch.org/node/9456.

[60] Wall Street Journal, 2008. An analysis of data from the U.S. Department of Housing and Urban Development showed that many payday lenders are clustered around government-subsidized housing for seniors and the disabled. The research was done by Steven Graves, a geographer at California State University at Northridge, at The Wall Street Journal's request.

Florida's overall population comprised of that age group grew by only 9.7%.[61] Borrowers 65 and older were the fastest growing age group of borrowers over this period.[62] In California, nearly a third of borrowers are age 52 and over;[63] the portion of borrowers age 62 and over grew steadily from 12.8% in 2013, to 13.2% in 2014, to 13.9% in 2015.[64] The senior program manager at a community organization that aids lower-income people in Nevada recently stated: "I see about 80 to 100 seniors per week . . . . at least half have taken out a payday loan." [65] Many go on to default and become victim to harassing phone calls.[66]

CRL's research on bank payday loans found that over one-quarter of bank payday borrowers were Social Security recipients, making these borrowers 2.2 times as likely to have had a bank payday loan as bank customers as a whole.[67] 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.[68]

In loan data the Bureau analyzed, 58% of payday borrowers with loans due monthly were recipients of government benefits.[69] The Bureau notes that such borrowers are particularly financially vulnerable, concentrated at the lower end of the income range.[70] And the debt trap for these borrowers appears to be particularly deep. The Bureau found that monthly borrowers have more repeat loans than those paid more frequently: approximately 20% of such borrowers averaged at least one loan per pay period over the course of a year,[71] and over 40% of all monthly loans were in sequences that persisted for the rest of the year studied.[72]

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[61] Florida's senior population increased from 16.6% of the population in 2005 to 18.2% of the population in 2014. American Fact Finder, United States Census Bureau, *available at* http://factfinder.census.gov/faces/nav/jsf/pages/index.xhtml.

[62] *Perfect Storm*, CRL at 8.

[63] In 2015, the figure was 31.1%. California Department of Business Oversight, "Summary Report: California Deferred Deposit Transaction Law – Annual Report and Industry Survey" (2014-2016). http://www.dbo.ca.gov/Licensees/Payday_Lenders/Publications.asp.

[64] Id.

[65] Michael Lyle, *Seniors often pay hefty price for relying on payday loans*, Las Vegas Review Journal, Sept. 1, 2016 (quoting Don Miller, seniors program manager for HopeLink, 178 Westminster Way, which provides assistance and resources to low-income people and families in the Las Vegas area), *available at* http://www.reviewjournal.com/view/seniors-often-pay-hefty-price-relying-payday-loans.

[66] Id.

[67] CRL, 2013; 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.

[68] CFPB White Paper at 18.

[69] 81 Fed. Reg. at 47981 (citing CFPB Data Point).

[70] 81 Fed. Reg. at 47981. The Bureau notes that nearly 90% of borrowers receiving public benefits reported annual incomes of less than $20,000, whereas less than 30% of employed borrowers reported annual incomes of less than $20,000.

[71] Id (citing Supplemental Findings at 121).

[72] Id (citing Supplemental Findings at 131).

Payday loans to seniors are particularly troubling because lenders routinely seize Social Security funds that are protected from creditors in other contexts. Congress has long sought to protect Social Security funds and other public benefits intended for necessities from the unilateral reach of creditors.[73] The Social Security Act prohibits collection of Social Security benefits through assignment, garnishment, or other legal process. The policy underlying this legal protection is to ensure the debtor a minimum subsistence income—for essential needs like food, shelter, and medicine—and courts have repeatedly upheld it.[74]

Payday lenders grossly undermine this critical protection by requiring Social Security recipients to provide direct access to their bank accounts and immediately taking the income for repayment. CRL research found that bank payday lenders took an average of 33% of the recipient's next Social Security check to repay a bank payday loan.[75] The Treasury Department recently made significant strides in protecting Social Security funds in checking accounts from bank freezes in response to garnishment orders,[76] but these rules do not address the informal wage assignment routine to the payday lending model.[77]

The threat payday loans pose to Social Security recipients became more pronounced in 2013, when electronic distribution of government benefits became mandatory.[78] Benefits that have been distributed by paper check, often to those most financially vulnerable, are now directly deposited to checking accounts or prepaid cards. As part of the new rule, the Treasury Department prohibited government deposits to prepaid cards that allow payday loans out of concern that credit products would siphon off exempt benefits.[79] However, benefits deposited into traditional checking accounts remain at risk to payday loans.[80]

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[73] *See*, *e.g.*, Social Security Act, at 42 U.S.C. § 407(a).

[74] For further discussion and detail, see Testimony of Margot Saunders, National Consumer Law Center (on behalf of its low income clients) before the Subcommittee on Social Security, Committee on Ways and Means, U.S. House of Representatives, June 24, 2008, *available at* http://www.nclc.org/images/pdf/other_consumer_issues/exempt_public_benefits/NCLC_exemptBenefitsTestimony_House_June2008.pdf.

[75] CRL, Big Bank Payday Loans, supra.

[76] 31 C.F.R. § 212.1.

[77] They also do not apply to the practice whereby a depository institution repays itself as creditor, as with bank payday loans. 76 Fed. Reg. 9947.

[78] U.S. Department of the Treasury, Interim Final Rule, Federal Government Participation in the Automated Clearing House, 75 Fed. Reg. 80335, amending 31 CFR Part 208 (2010).

[79] "In order to prevent Federal payments from being delivered to prepaid cards that have payday lending or 'account advance' features, we are prohibiting prepaid cards from having an attached line of credit if the credit agreement allows for automatic repayment of a loan from a card account triggered by the delivery of the Federal payment into the account. Our intention is that this restriction will prevent arrangements in which a bank or creditor 'advances' funds to a cardholder's account, and then repays itself for the advance and any related fees by taking some or all of the cardholder's next deposit." 75 Fed. Reg. at 80338.

[80] In its discussion, Treasury cited Regulation E's prohibition on compulsory electronic repayments as the comparable protection on traditional checking accounts, id., but this prohibition is typically not read to apply to single-payment loans, as bank payday loans typically are. Thus, federal benefits direct deposited to traditional checking accounts remain vulnerable to bank payday loans.

2.4. Policy Makers and the Public Are Increasingly Recognizing the Harm Caused by Payday Lending.

At both the state and federal level, policymakers have increasingly recognized the harm caused by payday and car title loans, and laws and regulations clearly reflect this trend.

2.4.1. State laws are trending against payday lending.

In the last ten years, no state has opened its borders to high-cost payday or car title loans, and many states have strengthened their protections by enacting rate caps.[81]

As the Bureau notes, the last state authorizations for payday lending were in 2005.[82] Since then, state regulatory trend has been to rein in payday lenders' debt trap practices. In 2007, the District of Columbia set its 24% rate cap. In 2008, Arizona and Ohio's voters overwhelmingly supported ballot initiatives in support of interest rate caps in those state, and Montana voters did the same in 2010. In 2009, the New Hampshire legislature enacted its rate cap, and an Arkansas Supreme Court decision clearly applied the state's 17% constitutional rate cap to payday loans. Those changes created the current landscape, where 14 states plus the District of Columbia have interest rate limits that keep short-term payday and car title lenders out of their states.

Other states have implemented more limited reforms to curb the harm from payday loans. In 2006, Oregon passed its law to reduce the cost of payday loans and curb renewals. In 2009, Washington limited payday loans to eight loans per 12-month period, and Colorado enacted a minimum six-month loan term along with moderate price restrictions. In 2013, Delaware limited payday loans to five per year.

In addition, since 2005, the following states have rejected lender attempts to expand high-cost loans into their states: Arizona, North Carolina, New York, New Hampshire, Georgia, Pennsylvania, and Maine.[83] And no state that once permitted payday lending, but now does not, has reversed course.[84] A number of states have also entered enforcement actions against payday and car title lenders to protect their states' strong laws.[85]

2.4.2. Federal law and regulation.

Trends at the federal level are consistent. The Bureau's proposal discusses these in detail;[86] key highlights are noted here. In the early 2000s, the federal prudential regulators shut down bank/payday

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[81] The Bureau's discussion of the regulatory landscape reflects these trends. See 81 Fed. Reg. 47875 et. seq. We note that although some states have recently permitted an extension of the types of high-cost loans they permit (Mississippi, Tennessee, and New Hampshire) by authorizing high-cost longer-term loans, they already permitted other forms of high-cost payday and car title loans in their state. See section 2.5.4 below for further discussion.
[82] 81 Fed. Reg. at 47875, noting Alaska and Michigan.
[83] Details on file with CRL.
[84] Details on file with CRL.
[85] See Diane Standaert and Brandon Coleman, *Ending the Cycle of Evasion: Effective State and Federal Payday Lending Enforcement* (2015), Center for Responsible Lending, *available at* http://www.responsiblelending.org/payday-lending/research-analysis/crl_payday_enforcement_brief_nov2015.pdf.
[86] 81 Fed. Reg. at 47883-84.

lender partnerships whereby payday lenders were renting bank charters to take advantage of bank preemption and related laws to evade state law.[87] The FDIC's 2005 payday lending guidelines advised that lenders should not keep payday loan borrowers in payday loans for more than three months in a twelve month-period, across all lenders.[88] The FDIC's 2007 affordable small loan guidelines advised that interest on small dollar loans should be limited to 36%.[89] And the OCC and FDIC's 2013 guidance addressing high-cost payday loans made directly by banks resulted in the discontinuance of these products by the handful of those agencies' supervisee banks that were making these loans.[90]

In addition, in 2006, Congress passed the Military Lending Act after the Department of Defense found that predatory lending was harming service members' finances, which was affecting security clearances and ultimately reducing the nation's military readiness.[91] This Act limited the cost of credit on covered loans to military servicemembers and their dependents to 36% on an annual basis, including fees that are not included in the Truth in Lending Act (TILA) annual percentage rate (APR). The Department of Defense's initial regulations under the law covered most payday and car title loans on the market at the time. Congress then directed DoD to revisit the rules, which DoD significantly strengthened in 2015 (effective 2016) to include all payday and car title loans, whether short- or longer-term, as well as, generally, all credit currently subject to TILA.[92]

Further, a number of enforcement actions by the Federal Trade Commission and CFPB have cracked down on unfair and abusive practices by payday and car title lenders.[93]

Finally, as noted in section 2.3.2 above, the Treasury Department has prohibited government deposits to prepaid cards that allow payday loans out of concern that credit products would siphon off exempt benefits.[94]

Meanwhile, there have been *zero* federal actions of which we are aware that have, to the contrary, signaled appropriateness of high-cost payday, car title, or similar loans.

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[87] See Comments of CRL to the OCC on Marketplace Lending, October 2015, at II., *available at*. http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_comment_treasury_marketplacelending_sept2015_final.pdf.

[88] FDIC Financial Institution Letters, Guidelines for Payday Lending, FIL 14-2005, February 2005, *available at* http://www.fdic.gov/news/news/financial/2005/fil1405a.html.

[89] FDIC Financial Institution Letters, *Affordable Small Dollar Loan Products, Final Guidelines*, FIL-50-2007 (June 19, 2007), *available at* http://www.fdic.gov/news/news/financial/2007/fil07050a.html.

[90] 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 [OCC/FDIC Deposit Advance Guidance].

[91] U.S. Department of Defense, *Report on Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents* (2006), *available at* www.defense.gov/pubs/pdfs/Report_to_Congress_final.pdf.

[92] 80 FR 43560 (July 22, 2015).

[93] Press Release, FTC, "Online Payday Lending Companies to Pay $21 Million to Settle Federal Trade Commission Charges that they Deceived Consumers Nationwide," (Jan. 16, 2015); for examples of CFPB actions, see n. 36-38 above.

[94] For the Treasury Department's rationale, see n.79 above.

2.4.3. Other policy trends.

The policy landscape increasingly reflects a rejection of unaffordable payday and vehicle title lending in a host of other ways. Earlier this year, Google announced that it will prohibit ads for payday loans and other related loans, banning ads in the U.S. for loans with an APR exceeding 36% and worldwide for loans due within 60 days. The company noted particular concerns about unaffordable payments and high default rates on payday loans in its announcement.[95] It collaborated with the civil rights community in the development of this policy.[96]

Also this year, New Jersey's pension fund divested from a large payday lender,[97] joining North Carolina's, which has had a policy against investing in payday lenders for several years.[98] Other actions include socially responsible investors filing shareholder resolutions against the largest banks making payday loans in 2013;[99] elected officials rejecting campaign contributions from payday lenders,[100] and public polling that shows overwhelming opposition to unaffordable payday lending.[101]

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[95] David Graff, Director of Global Product Policy, Google, "An Update to our AdWords Policy on Lending Products," Google Public Policy Blog, May 11, 2016, https://publicpolicy.googleblog.com/2016/05/an-update-to-our-adwords-policy-on.html.

[96] Press Release, "Advocates Applaud Google's Ban on Payday Loan Advertisements," The Leadership Conference on Civil and Human Rights, May 11, 2016, http://www.civilrights.org/press/2016/google-payday-ads.html.

[97] Shawn Aiken, "New Jersey Divests from Payday Lending," yes! Magazine, Mar. 26, 2016, http://www.yesmagazine.org/new-economy/new-jersey-divests-from-payday-lending-20160326.

[98] North Carolina Department of State Treasurer, Investment Policy: Payday Lending Divestment Policy, Approved March 2007, Amended July 2012, *available at* https://www.nctreasurer.com/inv/Policies/Payday%20Lending%20Divestment%20Policy%20-%20enacted%202012-07-19.pdf.

[99] 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. Resolutions filed with 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 and U.S. Bank (http://www.calvert.com/sri-resolutions.html).

[100] John Ellis, "Assembly hopefuls clash over contributions from payday lenders," Fresno Bee, Jan.11, 2016 http://www.fresnobee.com/news/politics-government/politics-columns-blogs/political-notebook/article54206090.html#storylink=cpy ("As for Arambula, McIntyre says he won't return the contributions – $1,500 from Axcess Financial Services and $1,500 from Check into Cash of California Inc. What Arambula is instead doing, McIntyre says, is writing a check to Poverello House for $3,000, the total amount of the contributions." Poverello House is a non-profit focused on hunger and homelessness. http://www.poverellohouse.org/.

[101] Mark Pattison, "Iowa caucuses, lawmakers getting payday lending issue on their radar," Catholic News Services, http://catholicphilly.com/2016/01/news/national-news/iowa-caucuses-lawmakers-getting-payday-lending-issue-on-their-radar/ (noting poll findings that 78 percent supported requiring payday loan lenders to first determine whether a borrower can repay the loan before issuing it); CEDAM, "Poll: Michigan Voters Oppose Expansion of Payday Lending," http://cedam.info/wp-content/files/PaydayPoll_Release_2-16-16.pdf (noting 70% support requiring payday lenders to determine a borrower's ability to repay the loan); Stop the Debt Trap Campaign, "National Survey Results: Overwhelming Support for CFPB's Payday Lending Rule," June 2016 (finding that voters support regulations that "requires payday lenders to verify—in advance of making a loan—that people applying for a loan have the ability to repay the full amount of the loan"), http://stopthedebttrap.org/wp-content/uploads/2016/06/Payday-Lending-Poll-Memo-June-2016.pdf.

2.5. Payday Lenders are Morphing to Particularly Harmful Longer-Term Loans in Anticipation of CFPB Rules.

2.5.1. Overview.

Though often forgotten in today's policy debates, it bears underscoring that payday lenders convinced states to authorize high rates in the 1990s based on the claim that the loans were for very short-term, relatively small loans intended to address an "emergency." The lenders often promoted the loan as a check-cashing fee. In those days, lenders did not even attempt to justify triple-digit interest rates for loans at the larger sizes and longer terms where high rates are charged today.

Likewise, in most cases, an authorization for a lender to hold a post-dated check written on the borrower's checking account, effectively as a condition of obtaining the loan, was only provided in the context of these short-term loans. And the authorizations likely rarely even contemplated the notion of a lender's electronic access to the account.

This history is notable because, among other things, it demonstrates that public policy has not historically sanctioned high-cost longer-term lending—including payday and car title lending—even to the limited extent it has sanctioned high-cost payday lending. The most likely explanation is this: High rates and a coercive repayment device are more likely to cause a borrower harm the longer the borrower is subjected to them. Put another way, both loan features carry extraordinary risk—not to mention the psychological impact on a borrower of an effective wage assignment—and they have never before been sanctioned as a prolonged scenario to which any person should be subjected.

As a point of comparison for what public policy generally supports on longer-term loans, we note that Congress was driven to enact significant reforms to the credit card market due to the widespread harm caused by penalty rates that averaged *27%* in 2008—far lower than the typical cost of covered longer-term loans.[102]

2.5.2. Longer-term loans can be particularly harmful.

The harm from traditional two-week payday loans comes not only from their high rate but also their very short term and balloon payment structure. The CFPB has rightly focused many of its proposed protections on the particular problems that are triggered by short terms and by balloon payments.

But as the scope of the proposed rule appropriately reflects, severe consumer injury is also caused by unaffordable longer-term installment loans, even if they lack balloon payments. Indeed, in many ways, longer-term high-cost loans pose even greater risk of harm than short-term loans.

[102] "2008 Credit Card Survey." Consumer Action, July 23, 2008. http://www.consumer-action.org/downloads/english/2008_Summary.pdf.

Longer-term loans vary widely in size and loan term, ranging from three-payment payday installment loans that effectively function as short-term balloon loans with two rollovers, to car title loans with two-year terms.[103] At least five states also have longer-term open-end loans.[104]

We discuss why high-cost longer-term loans can be particularly harmful in detail at 10.2 and 10.3, as an introduction to our discussion of the ability-to-repay determination and refinancing concerns unique to these loans. We provide a summary list of those reasons here:

Harms and dangers caused by all high-cost longer-term loans:

- Longer term loans tend to be larger than short-term loans.
- Longer-term loans can result in a longer high-cost debt trap.
- Larger and/or longer loans can mean higher overall costs taken from the budgets of struggling families.
- The high interest rates on longer-term loans compound when the loan is delinquent or defaults.
- A longer, multi-payment loan means longer exposure to the harms of a repeatedly-used leveraged payment device.

Additional harms and dangers caused by high-cost loans with especially long terms (i.e., more than six months):

- The longer the loan term, the greater the likelihood of significant income or expense volatility that may inhibit the borrower's ability to repay.
- Larger and longer loans are more likely to have payments for many months that cumulatively exceed the loan amount and yet do not significantly reduce the loan balance.
- Loans with terms longer than six months are more likely to default.
- The longer the term of the loan, the greater the likelihood that the consumer will, at some point, become delinquent and suffer from aggressive debt collection practices.
- Longer terms increase the chance of other collateral consequences of unaffordable payments.
- Long terms increase misaligned incentives because there is a higher possibility that the lender will recover the loan amount, and maybe a profit, even if the consumer eventually defaults.
- Small loans with disproportionately long terms put consumers in an extended debt trap with potential harm that likely outweighs the possible benefit.
- Small but long loans have an especially high potential for profitable defaults and weak underwriting.

Narratives of complaints filed with the Bureau provide further evidence of the collateral harms that high-cost longer-term loans cause, including trouble meeting other expenses, overdraft fees, and aggressive debt collection.[105]

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[103] Diane Standaert and Peter Smith, *Payday and Car Title Lenders' Migration to Unsafe Installment Loans*, Center for Responsible Lending at 1(Oct. 2015) (noting a 45-day loan from Check Into Cash in Ohio and a TitleMax car title loan in Missouri), *available at* http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_brief_cartitle_lenders_migrate_to_installmentloans.pdf [CRL, *Migration*].
[104] Id.
[105] Id. at 5, citing individual complaints filed with the Bureau at n. 45-48.

2.5.3. Lenders are already shifting to longer-term loans.

As the Bureau notes, some lenders are already shifting to longer-term loans. They are making these loans in a growing number of states, and these loans are becoming a larger portion of their overall portfolios. (In some cases, shifts to longer-term loans are clear efforts to evade laws aimed at shorter-term loans; those efforts are discussed primarily at section 2.6 below. This current section focuses on shifts more generally, which are largely in anticipation of CFPB rules expected to bring contraction to the short-term market.)

A majority of states—roughly 30—currently have laws with cost limits that have prevented or sufficiently discouraged payday and car title lenders from expanding into longer-term loans there.[106] But CRL estimates that longer-term payday and/or vehicle title loans are being offered in 23 states by large licensed lenders.[107]

Further, as the Bureau notes, the Online Lenders Alliance member survey found that installment loan volume is growing while balloon loan volume is shrinking,[108] a trend consistent with industry analyst reports[109] as well as the public filings of individual large lenders.[110]

2.5.4. Payday and vehicle title lenders are pushing for legislative authorizations for longer-term high-cost loans.

Payday and car title lenders are also pushing legislative proposals for high-cost longer-term loans—both closed-end and open-end—in a number of states. In Arizona, California, Georgia, Indiana, Iowa, Michigan, New York, Oklahoma, Pennsylvania, and Washington, efforts to authorize longer-term closed-end products have thus far been defeated;[111] in Mississippi and New Hampshire in 2016, though, lenders obtained authorization.[112] The proposals have varied in the details of their generally

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[106] As the Bureau notes, NCLC found that eight states have no rate or fee limits for closed-end loans of $500, and 11 have no rate or fee limits for closed-end loans of $2,000. For open-end loans, 14 states do not limit rates on lines of $500; 16 do not limit rates on lines of $2,000. 81 Fed. Reg. 47885 (citing Lauren Saunders, Margot Saunders, Carolyn Carter and Andrew Pizor, *Installment Loans: Will States Protect Borrowers from a New Wave of Predatory Lending?* (July 2015), *available at* http://www.nclc.org/images/pdf/pr-reports/report-installment-loans.pdf [NCLC, Installment Loans]).

[107] CRL, *Migration,* at 1 and Table 1, noting 20 states, in addition to New Hampshire, Mississippi, and Louisiana. In two states, Colorado and Illinois, a shift to longer-term has been in response to explicit authorizations for high-cost longer-term loans. In most states, though, the shift has possible because of state laws that do not have explicit rates limits for longer-term loans.

[108] 81 Fed. Reg. at 47885, n.231 (citing Online Lenders Alliance survey finding that the volume of longer-term loans was growing while balloon loans was contracting).

[109] 81 Fed. Reg. at 47885, n.232 (citing Hecht, which notes that the continuing trend is for installment loans to take market share away from balloon loans).

[110] *See, e.g.*, CashAmerica, Annual Report (Form 10-K), at 47 (Feb. 26, 2016) (noting that unsecured installment loan product offering was expanded in 2015). Loan fee revenues for CashAmerica's installment loans comprised 31% of total fee revenue in 2015, up from 14% in 2014, while fee revenue from short-term loan products comprised 69% of total fee revenue for the company, compared to 86% in 2014. *See also*, Annamaria Andriotis, "A Payday-Loan Rival Gains Ground", *The Wall Street Journal* (Aug. 7, 2016), http://www.wsj.com/articles/a-payday-loan-alternative-gains-ground-1470603307 (noting 78% rise in installment loan volume in 2015 versus 2014).

[111] CRL, *Migration*, at 5, n. 39. Bill numbers on file with authors.

[112] Mississippi: SB2409 (closed-end); New Hampshire: SB 308 (closed-end car title).

complicated fee structures and repayment terms. But the proposals typically authorize high rates, access to the borrower's checking account, and incentives for lenders to encourage repeated refinancing. In at least some instances, lenders have pitched these proposals as in anticipation of the CFPB's pending rules.[113]

High-cost open-end products have been pushed in a number of states as well. Lenders succeeded in Tennessee in 2014, where Enova International (dba CashNetUSA) is now offering a 273% APR line of credit.[114] In Arizona and Texas in 2015, and in Alabama, Kentucky, and South Dakota in 2016, similar lender efforts failed. Like closed-end loans that encourage repeated refinancing, these open-end proposals are so laden with fees as to make progress toward principal extraordinarily difficult. The proposal pushed in Arizona provided for the borrower to pay $4,900 on a $3,000 loan before having paid down even half of principal.[115]

2.5.5. Evidence suggests that tomorrow's longer-term market will look more like the current short-term market than it does today.

The Bureau's analysis of the longer-term loan market is, naturally, a study of the existing market, not the future one. Yet this research already shows that both payday lenders making longer-term loans and more traditional consumer finance lenders, have a business model built on keeping borrowers in long-term indebtedness.

As short-term lenders continue their shift to the longer-term market, we should expect both their practices and their borrowers to shift there as well. Payday and vehicle title lenders are purveyors of unaffordable loans and always have been. There is no reason to believe that these traditional debt-trap lenders will relinquish their basic business model when they move to the installment market. In fact, as discussed in section 2.6.5 below, evidence shows that, to the contrary, they are already planning ways to preserve it.

Evidence also suggests that today's short-term loan borrowers are more financially vulnerable than today's longer-term loan borrowers, with research showing they have significantly lower credit scores. Nonprime 101 found that storefront payday borrowers had an average Vantage Score of 532, compared to 581 for storefront installment borrowers.[116]

Moving these particularly vulnerable short-term borrowers into a high cost longer-term loan market creates an especially high risk of harm. This combination—more traditional debt-trap lenders making

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[113] *See, e.g.*, Hearing on S.B. 842 and S.B. 843 Before the S. Comm. On Banking and Fin. Inst., 2015-16 Sess. (Mich. 2016) (testimony of Ron Hicks, Senior Dir. For Gov't Aff. And Community Outreach, Advance America), *available at* http://www.senate.michigan.gov/committees/files/2016-SCT-BANK-03-08-1-10.PDF; Hearing on S.B. 842 and S.B. 843 Before the S. Comm. On Banking and Fin. Inst., 2015-16 Sess. (Mich. 2016) (testimony of Christopher Henn, Executive V. Pres. of NCP Finance), *available at* http://www.senate.michigan.gov/committees/files/2016-SCT-BANK-03-08-1-02.PDF; Hearing on S.B. 842 and S.B. 843 Before the S. Comm. On Banking and Fin. Inst., 2015-16 Sess. (Mich. 2016) (testimony of Joanne Needleman, Clark Hill PLC), *available at* http://www.senate.michigan.gov/committees/files/2016-SCT-BANK-03-08-1-04.PDF).

[114] CRL, *Migration*, at 5, n. 41-42.

[115] This and similar analyses of proposals in Alabama, Kentucky, and South Carolina, on file with authors.

[116] Nonprime101 Report 8. *Can Storefront Payday Borrowers Become Installment Loan Borrowers?* (Dec. 2015), https://www.nonprime101.com/wp-content/uploads/2015/12/Report-8-Can-Storefront-Payday-Borrowers-Become-Installment-Loan-Borrowers-Web-61.pdf.

loans to borrowers more financially vulnerable than those in the longer-term market today—means that tomorrow's longer-term loan market carries an even greater risk of consumer harm than do the longer-term loans on the market today. This expectation should inform more protective rules in the longer-term market than the Bureau has proposed.

2.6. Payday Lenders' Proven Response to Regulation Is To Attempt to Evade It.

Payday lenders have proven themselves eager and able to evade the law time and again. Clear examples are their morphing to avoid original regulations under the Military Lending Act; their morphing to evade entire state regulatory regimes intended to cover them; their more routine evasion of individual provisions aimed to curb their abusive practices; and their claiming affiliation with bank, tribal, or offshore entities to claim exemption from the law. And there is already evidence that payday lenders plan to evade the CFPB's rule as well.

2.6.1. Payday and vehicle title lenders morphed to evade the Military Lending Act.

It is well documented that payday and vehicle title lenders shifted their products to evade the original regulations under the Military Lending Act. The Bureau notes that some high-cost longer term products likely originally developed in response to the original MLA regulations, which covered only loans 90 days or less.[117] As the Bureau notes, the 2015 revisions to the regulations—which significantly expanded the credit products subject to the rule—were informed by evasions of the original regulations and were made largely to prevent future evasions.[118]

In light of the DoD's experiences regulating payday and vehicle title loans, the updated DoD regulations should be highly instructive for the Bureau's proposed rule. Yet there are several elements of those revised regulations that are better designed to prevent evasion than the Bureau's proposed rule, as noted at sections 3.9 (definition of "total cost of credit"), 4.7.1 (credit cards), and 4.7.3 (overdraft lines of credit) below. We urge the Bureau to model its regulation more closely on the DoD regulations in those respects.

2.6.2. Payday lenders morph to evade state law.

As the Bureau describes, payday lenders have responded to several state regulatory changes by shifting their models or products. Through these "shifts," they have continued to make substantially similar loans, thereby continuing to cause the harm that the regulatory interventions were intended to prevent.[119]

As the Bureau notes, in Ohio, lenders responded to a 2008 legislative fee-inclusive 28% rate cap aimed at payday loans, affirmed by a ballot referendum, by shifting to vehicle title loans, using a credit service

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[117] 81 Fed. Reg. at 47885.

[118] 81 Fed. Reg. at 48112, n.906 (noting that the revised MLA rule's preamble discusses a letter from 40 Senators who noted the revisions were "essential to prevent future evasions).

[119] We note that state laws with comprehensive interest rate caps have generally proven themselves evasion-proof, particularly those that also address fees that may not be considered interest, with sufficiently broad scopes. In addition, Washington State's 2009 annual loan limit of eight loans across all lenders, enforceable with a database, also appears to be working as intended, though it does not eliminate the harm caused by unaffordable payday loans.

organization model, and lending under the state's mortgage lender law. Today, there are 836 storefronts in Ohio making payday or car title loans; the majority (59%) make both. These loans exceed 300% APR, with some payday loans reaching as high as 600% APR. These lenders drain more than $502 million in predatory loan fees from Ohioans annually, twice what payday lenders drained in 2005.[120] In more recent years, lenders have expanded to longer-term, larger loans as well.[121]

In Arizona, lenders responded to a 2008 ballot initiative bringing an end to payday lending by shifting to 204% APR "vehicle title" loans, many of which are in fact merely holding the registrations of encumbered vehicles.[122]

In Virginia, lenders responded to a law placing restrictions on closed-end loans by shifting to open-end loans, which are not subject to state licensing or regulation. Today, as the Bureau notes, even lenders who previously made closed-end loans in Virginia, and who make closed-end loans everywhere else they lend, make open-end loans in Virginia.

In Delaware, some lenders responded to a law limiting loans due within 60 days to five per year by shifting to longer-term loans with several interest-only payments followed by a balloon—effectively a string of payday loans.[123]

In California, a lender made larger loans than consumers sought in order to evade the interest rate caps on smaller loans, telling consumers they could prepay what they did not want.[124]

Payday lenders also pose as brokers to evade state law. Under this scheme, lenders position themselves as credit service organizations (CSOs) or credit access businesses (CABs) and broker loans to borrowers. They charge a large brokerage fee for arranging the loan between the borrower and the technical lender. The interest rate on the loan is low enough to comply with state interest rate limits, while the large brokerage fee—which often pushes the true annual cost of credit up to 500% or higher—is not included in the calculation of interest. This scheme has been attempted but shut down in many states, including California, Maryland, Florida, and Michigan. It persists in Texas and Ohio.[125]

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[120] Diane Standaert and Delvin Davis, *The Buckeye Burden: An Analysis of Payday and Car Title Lending in Ohio*, Center for Responsible Lending (Nov. 2015), *available at* http://www.responsiblelending.org/research-publication/buckeye-burden-analysis-payday-and-car-title-lending-ohio.

[121] See Letter from 100+ Ohio groups to Director Richard Cordray, Consumer Financial Protection Bureau (Aug. 11, 2015), *available at* http://www.cohhio.org/files/Cordray%20letter%20stronger%20rules.pdf.

[122] Jean Ann Fox, Kelly Griffith, Tom Feltner, Consumer Fed'n of America and Ctr. for Econ. Integrity, Wrong Way: Wrecked by Debt (2016), *available at* http://consumerfed.org/wp-content/uploads/2016/01/160126_wrongway_report_cfa-cei.pdf.

[123] 81 Fed. Reg. at 47876. The Bureau cites a Delaware example of a $200, 12-month installment loan with interest-only payments followed by a balloon, with an APR of 838%, which a Delaware court recently found was unconscionable because its purpose and effect was to evade state law. 81 Fed. Reg. at 48111 at n.905, citing *James v. National Financial, LLC*, 132 A.3d 799, 834 (Del. Ch. 216).

[124] Calif. Dept. of Bus. Oversight, Press Release, "CashCall Pays Nearly $1 Million of Restitution to California Borrowers Under DBO Settlement" (July 10, 2015), http://www.dbo.ca.gov/Press/press_releases/2015/CashCall%20Restitution%20Announcement%2011-18-15.asp.

[125] Diane Standaert and Sara Weed, *Payday Lenders Pose as Brokers to Evade Interest Rate Caps: The next chapter in payday lender subterfuge*, Center for Responsible Lending (July 2010), *available at* http://www.responsiblelending.org/payday-lending/policy-legislation/states/CRL-CSO-Issue-Brief-FINAL.pdf [CRL, *Payday Lenders Pose*].

Payday lenders have also been known to disguise their loans as something other than payday or car title loans altogether, in the following ways:[126]

- Payday loans disguised as car title loans despite lack of a free and clear title;[127]
- Payday loans disguised as pawn loans for near-worthless items;[128]
- Payday loans disguised as gift card sales;[129]
- Payday loans disguised as sales, leases, or other services (including advertising space, telephone cards, and Internet service), with cash back;[130]
- Payday loans from employers to employees at relatively low interest rates but an annual administration fee that amounts to one week's pay;[131]

Finally, payday lenders evade a variety of elements of state and federal laws by making high-cost open-end lines of credit. For discussion of how they do so, examples of these evasions, and the harm they pose to borrowers, see section 10.6. See also section 6.3.2.1 describing how virtually all short-term open-end lines of credit are evasion products.

2.6.3. Lender practices have consistently rendered individual provisions that would appear to curb abusive practices virtually ineffective.

Lender practices have also consistently rendered individual provisions that would appear to curb abusive practices virtually ineffective. Bans on renewals, short cooling off periods between loans, and extended repayment plans, or "off-ramps," which would provide borrowers more time to repay their loans, have all done little or nothing to protect borrowers. Ultimately, where states have adopted these provisions, they have made no meaningful dent in the debt trap business model, permitting continued substantial harm to borrowers.

Most states have renewal bans in place, which either prohibit or limit the number of times a lender can extend the loan by having the borrower pay only a renewal fee.[132] Lenders render these ineffective,

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[126] Some of the examples below and additional examples are provided in NCLC, Consumer Credit Regulation § 9.6.6. (2nd ed. 2015).
[127] See note 122, supra.
[128] For example, one attorney in Georgia recently relayed that, in a state that prohibits payday loans, a lender extended his client a $300 payday loan in exchange for the pawn of costume jewelry likely worth $10 or $12. Email from David Addleton to Lauren Saunders re Grier v Hendrix, No. CAFN 2014-V-110112-L, Houston (Georgia) Superior Court (Aug. 22, 2016), on file with authors.
[129] Cash1, LLC disguised small-dollar consumer loans to Washington State and Arizona consumers as "retail installment sales transactions" involving the sale of gift cards issued by large retailers such as Walmart, Target, Fry's, and others on a credit basis, charging consumers interest with a typical APR of 360 percent. *See* Complaint, Spring v. Cash1, LLC, (King. Co., WA Sup. Ct. Jan. 27, 2011), on file at NCLC. The Arizona Attorney General obtained a consent judgment the company. "Judgement entered in gift card scheme," KPHO (Apr. 19, 2013), http://www.kpho.com/story/17353850/judg.
[130] Some of the examples below and additional examples are provided in NCLC, Consumer Credit Regulation § 9.6.6. (2nd ed. 2015).
[131] In one Georgia case, the employer charged the employee 29% interest with an annual "administrative fee" of $500. Answer, Logging v. Colbert, No. 16-762CS (Peach Co. Mag. Ct., Georgia Aug. 19, 2016) .
[132] The Bureau reports that seventeen prohibit lenders from rolling over loans and twelve more limit rollovers. 81 Fed. Reg. at 47870.

making back-to-back transactions instead, which are, in substance, essentially rollovers. The Bureau's recent data confirms that states with rollover bans have close to the same reborrowing rates as those without them.[133]

A smaller number of states have implemented cooling off periods between loans. The most common period is one day, and other states have longer periods following a certain number of loans in close succession.[134] These, too, have proven ineffective. In 2007, CRL found that in two states with cooling off periods, 90% of new loans were still made during the same pay period during which the previous loan was repaid.[135] The Bureau's recent research is consistent, finding that once one-day cooling off periods in Florida expire, reborrowing rates are about the same or exceed those in four states with fewer restrictions on reborrowing.[136] Over 80% of loans are reborrowed within 14 days, and nearly 90% are reborrowed within 30 days.

Extended repayment plans are nominally available in 20 states. These would give borrowers who are having trouble repaying additional time to do so. They have notoriously low take-up rates. CRL has reported on the participation rates of four states with such plans, finding that payment plans comprised no more than 1.5% of total payday transactions in any state.[137] CRL more recently found that, in Florida, where 84% of loans are made to borrowers with seven or more loans per year, fewer than one-half of one percent (0.5%) of all loans were given a cost-free off-ramp, available when a borrower indicates an inability to repay.[138] The Bureau's compilation of state data also finds low participation rates.[139]

The data are not surprising considering lenders' efforts to keep borrowers out of these plans. An industry trade association's best practices advise that it be available only if the borrower's request is one day prior to the loan due date—a very high bar—and the Bureau found that training manuals advise lenders not to mention the availability of the plan unless the borrower mentions it first.[140] The Bureau also found that in Colorado, under its previous law, lenders imposed a short cooling-off period in order to avoid triggering the off-ramp. The Colorado AG's office even reported that lenders would provide a third loan interest-free, in order to reset the consecutive loan sequence (which only included loans with a finance charge) before it reached four loans, thereby avoiding the off-ramp.[141]

[133] Supplemental Findings at 103 (finding that within two weeks, 75% of loans in states that prohibit rollovers have been reborrowed, versus 80% in states that permit at least one rollover (and 82% for all loans in the Bureau's data)).
[134] 81 Fed. Reg. 47870.
[135] See Uriah King and Leslie Parrish, *Springing the Debt Trap: Rate caps are the only proven reform*, December 13, 2007, *available at* http://www.responsiblelending.org/payday-lending/research-analysis/springing-the-debt-trap.pdf [CRL, *Springing the Debt Trap*].
[136] Supplemental Findings at 104-05.
[137] CRL, *Springing the Debt Trap*, at Table 8.
[138] CRL, *Perfect Storm*, at 4, as cited at 81 Fed. Reg. 47925, n.465.
[139] 81 Fed. Reg. at 47925, n.465.
[140] 81 Fed. Reg. 47873.
[141] CRL, *Springing the Debt Trap*, at n.49.

2.6.4. Payday lenders have arranged partnerships with banks or Indian tribes or gone off-shore to claim exemption from state law altogether.

Payday lenders have put together one scheme after another in an effort to claim exemption from state law altogether, including partnerships with banks and Indian tribes and going offshore. Rent-a-bank schemes, where lenders use federal bank preemption and related laws to claim exemption from state usury limits, were largely shut down by federal banking regulators in the early-to-mid-2000s.[142] But they are again rearing their heads.[143] Partnerships with Indian tribes, where lenders claim tribal sovereign immunity, have often been found to be ruses, where the payday lender has the predominant economic interest in the transaction and is thus the true lender.[144] And CFPB has recently sued an offshore lender for, among other things, collecting loans consumers did not owe because they were made in violation of state law.[145]

2.6.5. Payday lenders are planning to evade the CFPB's rule.

Evidence shows that payday lenders are making plans to evade the CFPB's rule, as they have evaded so many other laws. A transcript obtained by a news organization from the March 2016 annual conference of the industry trade group, Community Financial Services Association (CFSA) offers insights into these plans.[146] They include consideration of:

1. ***Avoiding the scope in its entirety by:***
    a. claiming the loan is a retail installment sale, potentially using kiosks in stores for borrowers to purchase products. This "product" could even be a prepaid card, whereby the consumer buys money on credit.
    b. partnering with large employers that can offer cash advances as a consumer benefit and assert the product is not "consumer lending."
    c. "grandfathering in" longer-term lines of credit by establishing them before the effective date of the rule.

2. ***Evading the ability-to-repay determination requirements by:***
    a. misrepresenting recurring utility costs thanks to "wiggle room" in the proposal; for example, the lender could have the borrower sign an affidavit saying they will

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[142] *See* Marketplace comments for a recent discussion of rent-a-bank

[143] For example, Elevate uses a partnership with Republic Bank & Trust Co. to originate the Elastic credit advances, circumventing state usury caps. See http://www.risecredit.com; Elevate Credit, Inc., Securities and Exchange Commission Form S-1, Registration Statement at 27 (Nov. 9, 2015) ("Elevate SEC Form S-1"), https://www.sec.gov/Archives/edgar/data/1651094/000119312515371673/d83122ds1.htm. For example, Elastic is available in Arkansas, which caps interest at 17%. Arkansas Const'n, Amend. 89. 16. A $380 Elevate loan with monthly minimum payments would cost $480 to repay over four months, See https://www.elastic.com/what-it-costs/, with an APR of about 120%.

[144] CFPB v. CashCall, 2016 WL 4820635 (C.D. Cal. Aug. 31, 2016); FTC, v. AMG Svcs., Inc., et al., 2016 WL 5791416 (D. Nev. Sept. 30, 2016); see generally NCLC, Consumer Credit Regulation § 9.6.3 (2d ed. 2015), update at nclc.org/library.

[145] See press release announcing CFPB's suit against NDG Enterprise and complaint here: http://www.consumerfinance.gov/about-us/newsroom/cfpb-sues-offshore-payday-lender/.

[146] Dayen, David. "How Predatory Payday Lenders Plot to Fight Government Regulation." Vice News. August 18, 2016. http://www.vice.com/read/payday-lenders-consumer-protection-strategy-atlantis-bahamas [Vice 2016]. The examples provided in the list were drawn from the Vice article or directly from the transcript.

cancel their $150 cable bill as soon as he leaves the store, and then remove that $150 costs in the ability-to-repay determination.

   b. renting out co-signers, whereby the lender establishes an affiliated third-party that serves as a guarantor on the loan, in exchange for a fee from the borrower.
   c. encouraging borrowers to find individuals as co-signers; it is unclear to what extent lenders expect to have to determine those co-signers' ability-to-repay.

3. ***Evading the provisions for short-term loans by shifting to longer-term loans***, noting that profits will take a little longer, but lenders will make a similar product.

4. ***Shifting to other products like pawn and rent-to-own.***

For additional examples of payday and vehicle title lenders' evasion practices, see CRL's 2010 issue brief.[147]

As noted above, Congress gave the Bureau explicit authority to prescribe rules and to prevent evasion thereof. The payday and vehicle title industries' record of evasion informs a number of our substantive recommendations on the proposal, as well our recommendations to the more general anti-evasion provision, discussed at section 17 below. We urge the Bureau to use its anti-evasion authority more robustly to limit the industry's ability to evade the protections.

3. SEVERAL DEFINITIONS SHOULD BE MODIFIED TO ENSURE THE RULE ACCOMPLISHES ITS AIMS: § 1041.2.

We support the Bureau's general approach to expand or modify existing definitions to ensure the rule has its intended effect. Yet we are concerned that certain definitions leave the rule vulnerable to foreseeable evasions, and thus consumers vulnerable to continued substantial harm.

The defined terms about which we have concerns are discussed below. In some cases, we elaborate on those concerns later in our comments in the context of the substantive provisions they most impact.

3.1. "Account": § 1041.2(a)(1).

Proposed § 1041.2(a)(1) gives the term "account" the same meaning as in Regulation E. We generally support this definition with some caveats. In particular, the term should be expanded to include a "general-use prepaid card" as defined in 12 C.F.R. § §1005.20(a)(3), regardless of whether it is labeled or marketed as a gift card.

We note that the term "account" under Regulation E does not presently include prepaid accounts and other newer types of accounts that hold consumer funds beyond traditional checking and savings accounts. However, we expect that by the time these rules are in effect, the Bureau's final rule adding prepaid accounts to Regulation E will also be in effect and those accounts will be included. We have not had the opportunity to review those rules in detail and urge the Bureau to take care to ensure that there are no gaps that will lead to evasions.

[147] CRL, *Payday Lenders Pose*, supra.

We agree with the Bureau's approach of incorporating already-defined terms from other statutes or regulations and allowing the meanings to change automatically as those statutes are modernized. This simplifies compliance as terms have the same meaning whenever possible. It also allows the regulation to stay up-to-date without the need for additional rulemakings as products, practices, and technology evolved.

Nonetheless, as we discuss in section 3.4 with respect to "lender," there are times when an existing definition (i.e., TILA's definition of "creditor") is not well suited to this rulemaking and poses a risk of evasion. Therefore, a preference for using pre-existing definitions should not be a hard rule.

We also note that the term "account" under Regulation E does not now include gift cards,[148] and we believe still will not even after the prepaid account rules are in effect.[149] Under the proposed prepaid rules, the term "account" did not even include general-use prepaid cards if they were *both* marketed and labeled as a gift card. We assume the same is true of the final rule.

This could prove an avenue for evasion. Payday lenders sell prepaid cards that consumers use to hold their funds and secure their payday loans.[150] Lenders could start adding the term "gift card" in order to take those loans out of this rule. A card could be marketed as "give the gift of a bank account card" with the label in fine print. Despite gift card labeling and marketing, the card might function like a traditional network-branded prepaid card and hold consumer funds that could be accessed through a leveraged payment device. Simply because a consumer's account carries the word "gift" should not deprive the consumer of the protections of this rule if that account is used to secure a covered loan.

Consequently, we urge the CFPB to expand the definition of "account" to a "general-use prepaid card" as defined in 12 C.F.R. § §1005.20(a)(3). Even if this term encompasses legitimate gift cards, it does no harm to include it within "account." Doing so adds no burdens to the card issuer and prevents payday lenders from using these types of accounts to evade the rule. Indeed, payday lenders have been known to use gift cards as a form of evasion, as noted in section 2.6.2. Alternatively, the CFPB could add a Comment to the anti-evasion provision with a gift card evasion. But it is clearer and more enforceable to simply expand the definition of "account."

3.2. "Covered longer-term balloon payment loan"

The definition of "covered longer-term balloon payment loan" determines which longer-term loans are subject to the stronger rollover provisions applicable to short-term loans. In defining this term, the Bureau has proposed that a balloon payment be considered a payment more than twice the amount of any other payment.

We understand that the proposed definition generally tracks Regulation Z § 1026.32(d)(1).[151] But Regulation Z's definition was aimed at a history of balloon payments on high-cost mortgage loans at

[148] 12 C.F.R. § 1005.20(b)(2).
[149] Proposed 12 C.F.R. § 1005.2(b)(3)(i)(C).
[150] NCLC, Payday Lender Prepaid Cards (July 2015), http://www.nclc.org/issues/payday-lender-prepaid-cards.html (NCLC, Payday Lender Prepaid Cards)..
[151] The Bureau notes that the two definitions differ in that the proposed definition compares the payment to any other payment rather than other "regular periodic payments" as Regulation Z does. We agree with the Bureau's proposal that for these purposes each payment should include principal and interest while excluding charges such

the end of 10- or 15-year terms. A balloon payment that is double the regular payment is a much higher percentage of the principal on a 6-month loan than on a 10- or 15-year loan.

If the purpose of the definition of a balloon payment is to identify loans that are being reborrowed because a payment larger than other payments inflicted payment shock, the proposed definition is underinclusive.

Under the proposed definition, a four-payment, 60-day loan with payments of $100, $100, $100, and $199 would not be considered a balloon loan, even though the $199 should be expected to cause payment shock for a financially distressed borrower. A consumer who is so strapped that she borrows $500 at 398% with biweekly payments of $90.78 is very likely to have trouble making a payment of 199% of that amount.

The definition in this context is also predictably vulnerable to evasion of the proposed protections for short-term loans and longer-term loans with balloon payments. While most loans on the market today with balloon payments may meet the definition of balloon loan as proposed, this could easily change as lenders attempt to evade the reborrowing restrictions applicable only to balloon loans.

In fact, the mortgage rule was substantially tightened by Dodd-Frank to largely eliminate balloon payments on HOEPA loans. In the current context, the balloon definition would not prohibit balloon loans but only subject them to tighter anti-flipping rules, which also supports a tighter definition.

An appropriate definition of "balloon payment" in the context of relatively small dollar installment loans to distressed borrowers can be found in the North Carolina Retail Installment Sales Act (RISA), which defines balloon as more than 10% above other payments, except for the final payment, which is 25% above.[152] For these particularly high-risk loans made to particularly financially distressed borrowers, we urge that any payment that is 10% greater than any other payment be considered a balloon payment.

3.3. "Credit": § 1041.2(a)(5).

Proposed § 1041.2(a)(5) assigns "credit" the same meaning as in Regulation Z, 12 CFR 1026.2(a)(14). We support this approach.

We note, however, that the proposed rule's definitions section uses but does not define the term "loan." Several of the other definitions incorporate the word "loan" in contexts that do not necessarily include the well-defined categories of covered loans. These include § 1041.2(a)(5) ("consummation"), (11) ("lender"), (15) ("outstanding loan"), and (18)(i) ("total cost of credit"). Indeed, some of these terms are used in contexts in which they extend to non-covered loans.

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at late fees and payments accelerated upon the consumer's default, but that they should include changed payment amounts due to rate adjustments or other payment changes permitted or required under the loan. (Comment 2(7)-2. and 2(7)-3.)

[152] § 25A-34. Balloon payments. With respect to a consumer credit sale, other than one pursuant to a revolving charge account, no scheduled payment may be more than ten percent (10%) (except the final payment may be twenty-five percent (25%)) larger than the average of earlier scheduled payments. This provision does not apply when the payment schedule is adjusted to the seasonal or irregular income of the buyer. (1971, c. 796, s. 1.)

While the meaning of the term "loan" may seem obvious, in common parlance it is often used to refer only to closed-end credit rather than open-end credit. In addition, courts might strain to understand why the CFPB used a term other than "credit," which it did define. Principles of statutory construction might lead a court to conclude the CFPB intended a different meaning.

Consequently, we urge the CFPB either to replace the term "loan" in the sections listed above with "credit," or to define "loan" as "an extension of either closed-end or open-end credit."

3.4. "Lender": § 1041.2(a)(11).

We support the Bureau's general approach to defining "lender." But as discussed below, we urge that:

- the term include service providers like credit service organizations (CSOs); and
- the Bureau clarify that the term includes those who provide credit through early access to wages.

3.4.1. We support a broader definition of "lender" than the "creditors" covered under Regulation Z, but it should reference "credit," not "loans."

Proposed § 1041.2(11) would define lender as "a person who regularly extends loans to a consumer primarily for personal, family, or household purposes." As the Bureau notes, this proposed definition is broader than the general definition of creditor under Regulation Z. Regulation Z applies to a creditor only if the creditor extends credit that is subject to a "finance charge" or is payable by written agreement in more than four installments.[153]

We support the proposed approach and agree with the Bureau that a broader definition is necessary to prevent evasions. Lenders will certainly design their fee structures to evade Regulation Z, as they have in the past (see section 3.9 on the "total cost of credit" definition). Many covered lenders make loans that are repayable in a single payment, so they would not meet the prong of Regulation Z that covers credit payable in more than four installments. Lenders could also attempt to disguise their finance charges as fees for noncredit services to evade coverage, as discussed in section 3.4.3.3. As discussed above, the proposed definition covers lenders that regularly make "loans" but provides no definition of that term. We recommend that the definition instead include a person who regularly extends "credit," which is defined in proposed § 1041.2(9), following the Regulation Z definition. Unlike the definition of "creditor" under Regulation Z, the definition of "credit" does not turn on the fee structure.

3.4.2. The term "lender" should include service providers such as credit services organizations.

As the CFPB is aware and as discussed above at section 2.6.2, one method that payday lenders have used to evade state interest rate caps is the CSO or CAB model. A separate organization, often an affiliate, purports to merely be a loan broker, charging a fee for the service of "finding" a loan that is provided by another organization. The CSO thus claims not to be making a loan.

The CFPB has appropriately made clear that fees charged by service providers such as CSOs are counted for purposes of determining rule coverage. Similarly, a loan has a leveraged payment mechanism or

[153] 12 C.F.R. § 1026.2(a)(17)(i).

vehicle security even if that mechanism or security is held by a CSO or other service provider and not the lender. And the rule has included CSOs and CABs in its definition of "service provider."

However, the proposed rule does not appear to include service providers in the definition of "lender" or to impose any obligations or prohibitions on them. All of the requirements of the rule are applied to the "lender." Thus, it is not clear if a CSO could be held accountable, despite the fact that in the existing CSO models the CSO is often the lender in all but name, and the CSO could be the one responsible for a reasonable ability-to-repay determination and debiting the consumer's account.

Another problem is that several requirements of the proposed rule are different if the same lender or an affiliate is involved. The provisions implicated include those providing indicia of unaffordability on loans outstanding with the same lender or its affiliate for both short- and longer-term loans (§ 1041.6(d) and § 1041.10(c)); any provision addressing non-covered bridge loans (§ 1041.6(h), § 1041.7(d), § 1041.10(f)); other rollover restrictions at § 1041.10(e); and the limits on the number of exemption loans permitted in 12 months from the same lender or its affiliate for the longer-term exemption loans (§ 1041.11(c) and § 1041.12(c)).

Yet if the affiliate is a CSO and not a "lender"—or if the CSO is not even an affiliate—[154]the rules may not apply as intended. The rule does not readily seem to account for loans made by unaffiliated lenders but through the same or an affiliated service provider, like a CSO or CAB.

To fix both of these problems, we urge that CFPB add to the definition of lender:

> *The term lender also includes a service provider to a lender that provides a material service to lenders in connection with the lender's offering or provision of covered loans.*

Alternatively, the CFPB could include a more specific provision such as those in some state laws.[155]

In addition to clearly covering service providers, the CFPB should also add a comment that explains that a lender is considered to be the same lender or affiliate (for purposes of the provisions where that is relevant) if the second lender is a service provider to the first lender or if the two lenders use the same or affiliated service provider.

3.4.3. The term "lender" does, and should, include those who offer credit through early access to wages.

3.4.3.1. Early access to wages is credit.

The CFPB has asked whether the term "lender" does, or should, include some new services that allow consumers to draw on money they have earned but not yet been paid or that offer to help consumers to smooth income. Some of these services rely on "voluntary" tips, some charge for each transfer, while others are compensated through a monthly or weekly fee that may also cover other services potentially unrelated to the usage of credit. Some are integrated with the employer, but some are not.

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[154] *Affiliate* has the same meaning as in 12 U.S.C. 5481(1). The Dodd-Frank Act defines affiliate as any person that controls, is controlled by, or is under common control with another person.
[155] *See, e.g.*, N.H. Rev. Stat. § 399-A:1(XII).

The primary question is whether the service offers credit. If it does, then the service would generally fall under the definition of covered short-term loan regardless of pricing or repayment mechanism. These services, to our knowledge, are all repaid through a leveraged payment mechanism (either EFT or payroll deduction) in less than 45 days. Since there is no exemption in the proposed rules for short-term credit that charges no or low fees, the providers of these products meet the proposed rule's definition of "lender" regardless of their cost. The next question then is whether there should be an exemption for any of these services, which we address in section 3.4.3.4 below.

The proposed rules (other than the definition of "lender," which section 3.4 of these comments urges the Bureau to revise) rely on the Regulation Z definition of "credit," which is "the right to defer payment of debt or to incur debt and defer its payment."

A small number of services may not meet this definition. For example, some services may arrange for a split direct deposit directly from the employer to the employee, with part of the wages deposited early and the rest on the regular payday. These services may not involve credit if the employer pays the wages early and thus a third party does not advance the wages and defer repayment. However, we do have some concerns about these products, and the CFPB should not make a definitive conclusion now as to whether or not they are credit.[156]

But as we understand them, the majority of early wage access services do indeed offer credit. They advance consumers' wages to them and are repaid later either from the employee's wages through payroll deduction or from an electronic fund transfer (EFT) from the consumer's account. Some (like GreenDot's GoBank arrangement with Uber) advance the wages for only a few hours, until the employer and the provider settle at the end of the day. Others advance the wages until the regular payday, when the advance is repaid through a payroll deduction. Some services (like, we understand, ActiveHours and Even) repay themselves through the ACH system from the employee's account after the regular paycheck is deposited, just as payday lenders do. But in all of these services, the employee is given a wage advance and has the right to defer repayment of it through a later transfer of the employee's wages or deposits to the provider.

Many of these services may have a connection with the employer's time attendance data file or the payroll provider to find out how much in wages are already earned and owed. But the knowledge that

[156] We do have concerns about these products, which have some of the dangers of a cycle of debt posed by payday loans. Consumers can get into the same cycle of spending their paycheck early, having a hole in their pay, and needing to draw pay early again the next pay cycle. The ability to access wages early might help the first time, but if it becomes a pattern, it might make it more difficult for employees to manage large expenses like rent. In fact, one study found that payday loans that were repaid weekly had a far higher charge-off rate (97.37%) compared to those that are paid biweekly, semi-monthly or monthly (28% to 40%). J. Howard Beales, III & Anand M. Goel, Small-Dollar Installment Loans: An Empirical Analysis at 25 (Mar. 20, 2015) (Beales/Goel). Since payday loan payments usually correspond to the pay schedule, the fact that borrowers with weekly paychecks default at a higher rate may indicate that a weekly paycheck makes it easier to spend money quickly and more difficult to manage larger monthly expenses.

While the fees for early wage access products are relatively low, they can add up and effectively set up a situation where the employee is simply paying to access their wages. Spending pay early also can make transitions more difficulty if the employee is laid off or otherwise changes to another job. There is also the possibility that some of these products could charge extremely high fees even if the wages are paid early through direct deposit. Thus, the CFPB must keep a close eye on these products and consider the extent to which they should be considered credit or otherwise subject to protections.

wages are earned and waiting to be paid does not change the fact that the service is offering credit when it provides an advance and is repaid later from the employee's wages.

To ignore the credit aspect of this type of arrangement would open up a huge potential loophole in the proposed rule. That is essentially what payday lenders are in the business of doing: advancing wages until payday. When consumers take out a payday loan, they may have wages earned and unpaid with their employer. There is a lag between when wages are earned and when they are paid. If a payday lender were to confirm that the consumer has $300 in unpaid wages on the day of the loan, it would not be any less of a loan.

In fact, one payday lender is already claiming that its loans are earned wages. Shutter Lending charges $18 per $100 loaned with APRs that go as high as 1642%.[157] The lender claims:

> Employees of participating companies are advanced funds only in amounts that can be paid back via a direct payroll deduction on their next paycheck; in other words, *financing is based on actual wages earned* and not credit history.[158]

Thus, the fact that some of these services are integrated with employers does not prevent abusive lending products that should be covered by the rule. The CFPB is appropriately including payroll deduction loans in this rulemaking, and some very high-cost, dangerous products have been offered through employers.[159] It would be simple for a payday lender to match the size of a payroll deduction loan to the portion of the paycheck that is purportedly already earned at that point.

Moreover, some of these services are not directly integrated with employers and do little more to assess "earned but unpaid" wages than what payday lenders do. They look at the consumer's bank account and record of direct deposits and estimate how much unpaid earnings the employee has. If an employee normally earns $1000 every two weeks and comes in to a payday store one week before payday, the lender could claim that the employee has $500 in unpaid wages and that the loan is merely paying out those wages early. Any early wage access service could also charge payday loan pricing of $15 for every $100 in wages that are paid early. If the early payment is not considered "credit," then the size of the fee would not change that fact.

Some services are slightly more high-tech than most traditional payday lenders, obtaining login information from the consumer's bank account so they can directly observe direct deposits. But payday lenders could easily adopt that approach if it enabled them to claim that a loan is not a loan but is just accessing earned wages. Knowing past direct deposits also does not enable the provider to know the size of the upcoming paycheck; it could be smaller than usual, meaning that the consumer does not in fact have the anticipated earned wages.

It is critical that the CFPB not adopt an unduly narrow view of "credit" in an effort to exclude fintech providers from this rulemaking. In section 3.4.3.4 below, we propose a narrow exemption for low-risk, low-cost products that are farther away from traditional credit. But staying faithful to the full definition

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[157] https://www.shutterlending.com/fee_schedule.html.
[158] https://www.shutterlending.com/.
[159] For example, Think Finance, a payday lender that used a tribal lending model, see Jack Newsham, RICO Claims, Others Survive In Vt. Tribal Payday Lending Suit (May 20, 2016), previously had a payroll deduction product. See Elevate SEC Form S-1 at 170.

of "credit" under Regulation Z—even for products that might ultimately be exempted—is critical to the integrity of not only the Truth in Lending Act but also the CFPB's ability to address credit abuses in many unforeseeable ways in the future.

3.4.3.2. Early wage advancers compensated through "voluntary" "tips" are also lenders.

The CFPB has asked whether services that are compensated through purportedly voluntary "tips," are—or should be—"lenders." The answer is squarely yes for several reasons.

First, for loans of 45 days or less, the definition of covered short-term loan does not turn on whether or how much the lender charges. Only a charity or other entity that does not regularly make loans would be exempt. So excluding tip-based products would require a special exemption.

Second, permitting "voluntary" charges would open up evasions. Lenders could suggest a tip amount resulting in a high cost for a short-term loan, and it could make it easy to pay a tip and difficult not to. Indeed, a lender could have some mechanism to discourage consumers from using the service without paying a tip or cutting them off if they do so repeatedly. It is also likely that tips in isolation would appear low to the consumer but that they cumulate and add up to a high APR. That is part of the problem with payday loans: $15 per $100 doesn't sound like much but it is for a short-term loan, and it adds up with rollovers. Even if users are "tipping" $3 per $100, that is expensive for a short-loan. The consumer can get into the same cycle of reborrowing as with a traditional payday loan; there is no underwriting for ability to repay; and the same problems with failed payments can occur.

Moreover, lenders may start with "voluntary" tips and then move to mandatory ones once they have a base of consumers hooked. As the Bureau notes, some payday lenders offer their first loan for free.[160]

Third, users who "tip" incur debts that must be repaid and are secured through a leveraged payment mechanism that may cause consumer harm. Consumers likely preauthorize repayment through the ACH system and the bank account is debited for the payment on payday. If the anticipated pay is not deposited, or if other debits leave the account with insufficient funds, the ACH payment may either bounce and trigger an NSF fee or be paid through an overdraft, triggering an overdraft fee. If the payment fails, it may be re-presented, potentially triggering multiple fees. And if the borrower owes an unpaid debt, she could potentially be subjected to debt collection activity. Thus, these loans, even if they require only "tips," can lead to the same harms as any other payday loan.

3.4.3.3. Weekly or monthly fees not directly tied to credit advances can still be a form of paying for credit.

The CFPB has solicited comment on whether companies that impose no charge on the consumer, or that charge a regular membership fee that is unrelated to the usage of credit, should be considered lenders under the rule. In section 3.4.3.4 below, we propose an exemption for companies that charge low fees that are truly unrelated to credit. But unless they meet the criteria we have outlined, services that provide credit and charge fees should not escape the rule merely because they design a fee structure that obscures the pricing of the credit.

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[160] 81. Fed. Reg. at 47871, n.58.

There is no free lunch, and it is essential that the CFPB look closely at any product that claims to offer credit for free. Unless it is truly a rare event on a product that does not have a credit component—such as an inadvertent overdraft on a prepaid card that results from a force-pay situation and does not trigger a fee[161]—it is likely that any product with a credit component is finding a way to charge for that credit. However, in the next section, we propose an exemption for a narrow category of low-cost early wage access products that may include trivial amounts of risk-free credit.

As discussed in section 3.9 below, we agree with the CFPB's assessment that focusing on a "finance charge" directly tied to credit as defined in Regulation Z would open up too much space for evasions in an industry eager to exploit it. As the CFPB observed in the prepaid card rulemaking,[162] membership and other monthly or periodic fees can be a means of covering the cost of credit even if they are not directly tied to or triggered by specific advances of credit.

For example, PayActiv provides an app that enables employees to access earned but unpaid wages. It charges a $5 "membership fee" in every pay period in which the employees access services.[163] In other words, if the employee takes a wage advance, there is a fee. While it is possible that there are other services that also trigger the fee, clearly the advances are the main purpose of the app and the fee is charged for those advances. This is true regardless of whether the employee may take multiple advances per pay period without incurring additional fees.

An examination of one of the new income smoothing products on the market, Even, also shows how a membership fee can be used as way of charging for credit, and as a way of collecting the credit itself. We describe Even because it offers an illustration of the potential dangers of carving out exemptions for fintech products that work differently than traditional credit. Other lenders could use the Even model with a much higher pricing structure.

Even offers an app that offers to help consumers smooth the spikes and dips of uneven income. Even charges a $3 weekly fee, although apparently some employers cover that fee. The fee is not directly triggered by usage of credit, as it is charged whether or not the consumer borrows that week and is also charged to consumers who only move money in and out of savings and do not use any credit. But, as discussed below, the fee is clearly a way of charging for credit and recovering advances that are unpaid.

Based on a review of direct deposit activity, Even determines the consumer's average paycheck. On paydays when the pay is above average, the app automatically transfers the excess to a separate savings bucket. When the paycheck is below average, the app transfers funds from the savings bucket to make up the difference. The app will also advance funds to make up a shortfall if there is not enough money in the savings bucket. Repayment is taken from any excess paychecks.

Although the app will not take more than the "excess," the app recalculates the "average"—and thus the "excess"—based on the last three paychecks. So if the consumer's wages have gone down, so does

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[161] See Comments of NCLC on Prepaid Accounts Under the Electronic Fund Transfer Act (Regulation E) and the Truth in Lending Act (Regulation Z), Docket No. CFPB-2014-0031, RIN 3170-AA22 at 57 (Mar. 23, 2015), http://www.nclc.org/images/pdf/banking_and_payment_systems/nclc_prepaid_card_npr_comments-032315.pdf.

[162] See 79 Fed. Reg. 77102, 77230 (Dec. 23, 2014).

[163] See https://www.payactiv.com/faq/ ("How much is the MyMo Membership Fee?).

the average, and there can be “excess” that is taken to repay the credit even with a paycheck that is still reduced and does not leave the consumer enough funds to pay expenses. Payments appear to be made to and from Even through preauthorized ACH payments.

Employees using Even can incur debts that need to be repaid. The employee can turn off Pay Protection, but the app then goes into "Settling up" mode where Even continues to make withdrawals from any “excess” and continues to charge the $3 weekly fee (if not covered by the employer).

It appears that it is nearly impossible to stop the $3 weekly fee if the consumer owes money. If the employee loses her job, she can pause the account with no weekly fee for up to six months until receiving paychecks again. But short of that situation, Even does not allow the consumer to disenroll or stop the weekly fee if money is still owed, as illustrated by these statements in the terms and conditions:

> Just like you have the right to cancel, we have the right to cancel your use of Even….
> It can also happen if we have attempted to contact you by in-app notification regarding repayment and have not received a response. In the event of cancellation, Even may suspend or close your Even account. We will inform of our decision via in-app notification, and you can always talk to our support team if you have questions. *If you owe money to Even, your subscription payments stop when you have fully repaid your balance.*
> …
> Before we can close your Even account, we first need to pay back any advances you owe to Even. *We also need to pay any subscription payments that were unpaid during your use of Even.* This typically means that we split your balance owed into four payments on each of your next four paydays….If we attempt to contact you about building a repayment plan and we do not hear back from you, we will send you an in-app notification informing you of the repayment plan and schedule that we will be following.
>
> Two things we won’t do: we won’t sell your debt to a collections agency. We also won’t report your debt to a credit bureau, or use it to hurt your credit score. *Other than those two things, we will use the legal options available to us in order to collect the money you owe us.*[164]

In short, while there is no direct interest on Even’s advances, or any per-advance fee, the $3 weekly fee is unquestionably intended to cover the cost of advancing the funds and the risk that they will not be paid back. Although the fee also covers the service of transferring money to and from savings, that does not appear to be its primary purpose. The discussion on the website appears to contemplate employees who regularly need to access credit. Thus, the weekly fee should be considered to be a fee for the cost of credit.

We recognize that, under the right circumstances, income smoothing products like Even may be helpful. As discussed in section 3.4.3.4 below, we believe that Even may be able operate under the rules as proposed without an exemption. But Even is clearly offering credit, charging for that credit, and potentially subjecting consumers to injury if the credit proves unaffordable. Thus, products like Even’s must be covered by the rule.

[164] https://even.com/terms (emphasis added).

Indeed, it is clear that consumers can incur overdraft and NSF fees from Even payments. Even deducts the $3 weekly fee every Friday, and it appears that it will do so regardless of the account balance. The terms warn consumers that "we might charge your subscription fee during a time that your bank balance is low, causing your bank to charge you an overdraft fee." Even will refund overdraft or NSF fees in certain circumstances, but not if the Even account is "closed" (but still incurring fees), unless the consumer is paying on a payment plan. Thus, the $3 weekly fee that consumers cannot stop can trigger NSF and overdraft fees, making the payment protections of this rule important.

3.4.3.4. The CFPB should consider exempting a narrow category of low-cost, risk-free early wage access products.

For the reasons described above, it is very dangerous to ignore the credit aspects of early wage access products; to focus on the lack of a direct and obvious finance charge; or to provide a broad exemption for fintech products. The CFPB's recent action against LendUp[165] (which clearly would be subject to this rule) is another reminder about why regulators must resist calls to be lax about "fintech" products in the name of innovation.[166]

Nonetheless, we recognize that the requirements of the proposed payday rule may not mesh precisely with some products that are providing small amounts of credit and that may benefit consumers without posing any risk of harm.

Consequently, we propose a narrow exception for early wage products that do technically have a credit component but do not expose consumers to *any* potential for debt or for the harms of a leveraged payment mechanism. A price cap is also essential in order to prevent evasions. Of course, any product that does not offer credit at all would still be outside this rule. If the Bureau grants this exemption we urge it to monitor these lenders closely to ensure the exemption does not create opportunity for abuse.

Thus, we propose that the CFPB exempt from the definition of "lender" (but not the definition of "credit") a person who offers a service that:

(1) Enables the consumer to access actual earned wages, as determined from the payroll provider or access to the time attendance data file;
(2) Deducts wages that are paid early from payroll without any use of any other leveraged payment mechanism such as preauthorized ACH;

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[165] *See* Press Release, CFPB Orders LendUp to Pay $3.63 Million for Failing to Deliver Promised Benefits Online Lender Did Not Help Consumers Build Credit or Access Cheaper Loans, As It Claimed (Sept. 27, 2016), http://www.consumerfinance.gov/about-us/newsroom/lendup-enforcement-action/; Calif. Dep't of Bus. Oversight, Press Release, CA DBO Announces $2.7 Million Settlement with LendUp to Redress Widespread Violations of Payday, Installment Loan Laws Firm Charged Thousands of Borrowers Unlawful Fees and Rates (Sept. 27, 2016), http://www.dbo.ca.gov/Press/press_releases/2016/LendUp%20Settlement%20Release%2009-26-16.pdf.

[166] Another example of a flashy fintech product that failed expectations (before "fintech" was a word) was the short-lived "Tandem Money," which purported to help people transition from borrowing to savings. In reality, it was a sugar-coated payday loan tied to a prepaid card. NCLC, Press Release, Prepaid Card Payday Loan/Savings Product Folds (Nov. 9, 2012), https://www.nclc.org/images/pdf/pr-reports/pr-tandem-money.pdf.

(3) Does not pose any possibility that the consumer could incur a debt that has to be repaid other than through a payroll deduction from the next regular paycheck, and gives the provider or employer no right to collect against the consumer under any circumstances;
(4) Charges no more than $10 per month. Bona fide fees not tied to credit that are reasonable and customary for an account or service that does not offer credit would be excluded. (For example, an ATM fee on a prepaid card, or a $15 per month fee for a platinum rewards checking account with cash-back.)
(5) Permits the consumer to cancel the service with no further fees at any time.

This exemption hews close to the spirit of the definition of credit because the consumer does not incur a debt to anyone (even though it arguably is a debt repaid through payroll deduction). It does not pose the risks of ACH payments or other leveraged payment mechanisms or the risk of collection of unpaid credit.

The fee limit is necessary in order to prevent this from becoming a loophole for payroll deduction loans. For example, imagine a lender that offers a payroll deduction loan at $15 per $100. The consumer earns $600 every two weeks. Seven days before payday, the consumer wants a $300 loan. The lender can access the wage and hour system and can see that the consumer has already earned $300 in that pay period. The lender makes the loan but claims that it is just paying wages early, with $345 deduced from payroll. The lender might even have an arrangement with the employer where the lender gets paid the same day as the loan (or just through a normal payroll deduction on payday). Similarly, without a fee limit, the wage access provider could charge a $50 per week membership fee. The consumer can draw wages early whenever the consumer wants as long as they have been "earned."

These types of expensive payroll deduction loans should clearly be covered even if they are otherwise designed consistent with the proposal above.

On the other hand, some reasonably priced early wage access products on the market today would likely be exempt, or could become exempt with modest changes. For example, Green Dot's Uber Debit account charges no fees for Uber drivers to access their wages early. There is no monthly fee and only a bona fide out-of-network ATM fee that is typical for a prepaid card. Other services that charge for each early wage transfer could continue doing so as long as the fees are capped at $10 per month.

Services that allow consumers to incur debt and use ACH or other payment transfers that can fail should be subject to the rules.

3.5. "Loan sequence" or "sequence": § 1041.2(a)(12).

The proposal defines "loan sequence" or "sequence" as a series of consecutive or concurrent covered short-term loans in which each loan is made during the time period in which the consumer has a covered short-term loan outstanding and for 30 days thereafter.

We urge that this definition be revised to provide "for 60 days thereafter" rather than 30. This definition has significant relevance to the rule's provisions aimed at addressing flipping both short- and longer-term loans. As we discuss in more detail at sections 8.3 and 11.3.1, the evidence strongly suggests that a typical payday or vehicle title borrower has an expense cycle of longer than 30 days, and lenders should be expected to evade rollover restrictions by encouraging borrowers to reborrow 31 days later.

In addition, the Bureau solicits comment on whether it should modify this definition to address an evasion tactic whereby a lender permits a borrower to skip a payment in exchange for a late fee that functions the same as a rollover fee. We urge that it make this modification and provide that if a substantial portion of a portfolio's borrowers pay late fees in exchange for skipping a payment, each extended payment should be treated as a new loan in the sequence.

3.6. "Non-covered bridge loan": § 1041.2(a)(13).

Section 1041.2(a)(13) defines "non-covered bridge loan" as a non-recourse pawn loan substantially due within 90 days and made within 30 days of a covered short-term or covered longer-term balloon-payment loan outstanding, made by the same lender.

We urge that this definition be broadened to include any longer-term loan, covered or non-covered by the same lender. We also urge the time period be 60 days rather than 30, consistent with our recommended change to the definition of "loan sequence" above.

A broader definition of non-covered bridge loan is essential to preventing easy evasion of the rollover restrictions applicable to short-term and longer-term balloon loans. Regardless of the extent to which payday and vehicle title lenders make non-covered longer-term loans now, we should fully expect them to if this definition is not broadened. See sections 8.10 and 11.10 for further discussion related to the need to expand this definition.

3.7. "Outstanding loan": § 1041.2(a)(15).

The Bureau's definition of "outstanding loan" has significant implications for several parts of the rule, including the ability-to-repay determination, the rule's provisions addressing flipping, and the short-term exemption. The manner and extent to which delinquent debt should be considered may differ in each of those contexts.

The proposed definition of "outstanding loan" is:

> "a loan that the consumer is legally obligated to repay, regardless of whether the loan is delinquent or is subject to a repayment plan or other workout arrangement, except that a loan ceases to be an outstanding loan if the consumer has not made at least one payment on the loan within the previous 180 days." [167]

First, to clarify the situation where no payments were ever made, we suggest the language be modified to read:

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[167] The rule further proposes that once a loan is no longer outstanding, it cannot become outstanding again. 81 Fed. Reg. at 47908; Proposed § 1041.2(15); Proposed Comment 2(15)-2. Relatedly, we agree that a lender selling a loan or servicing rights to it should not affect whether the loan is outstanding, Proposed Comment 2(15)-2.

"except that a loan ceases to be an outstanding loan ~~if the consumer has not made at least one payment on the loan within the previous 180 days~~181 days after the last payment or, if no payments were made, 181 days after the disbursement of the loan."

More importantly, we urge the Bureau to expand this definition to include loans for which the last payment was made more than 180 days ago.

We are concerned that, with respect to the ability-to-repay determination, the exclusion of debt only six months old risks (1) understating payments on major financial obligations; and (2) permitting lenders to ignore indicators of financial distress that should be relevant to the borrower's ability to afford new debt. We discuss these concerns in detail at 6.2.2.

We recommend the following changes to "outstanding loan" to mitigate the risk that consumers with delinquent unaffordable loans will be harmed by additional unaffordable credit:

1. Modify the definition to exclude only loans with both no payment *and* no debt collection activity over the course of the established time period.
2. For loans from a different lender: Use a period of 365 days.
3. For loans from the same lender:
    a. If the loan has not been written off or sold to a debt buyer, include the loan regardless of how much time has passed.
    b. If the loan has been written off and is no longer being collected by the lender, or has been sold to a debt buyer, use a period of 365 days following the last collection attempt.

    Using 365 days rather than 180 for same-lender loans is consistent with the Bureau's concerns that lenders will exploit a cut-off point in an attempt to encourage new borrowing or revive collections activity.
4. Require that lenders report collections activity to the RISs, as noted in 14.4 (for debt buyers, we urge the Bureau to include this requirement in its proposed debt collection rules).

In addition, as discussed in section 11.4.2.211, we urge that loans that are repaid early be deemed to be "outstanding" for 30 days in order to prevent evasions. In that section we also urge that lenders be prohibited from refinancing their own defaulted loans even if the loans no longer meet the definition of "outstanding." We also address the issue related to the short-term exemption at section 9.8.2.6.

3.8. "Service provider: § 1041.2(a)(17).

We agree with the Bureau's proposed definition of service provider, which the Commentary provides includes credit access businesses and credit service organizations.[168] Credit access businesses and credit service organizations are used in some states to make payday loans in evasion of state interest rate caps (see section 2.6.2 above). As the Bureau notes, regardless of the formal division of functions between the nominal lender and the credit access business, the loans produced by such arrangement are functionally the same as those covered loans issued by a single entity and present the same set of consumer protection concerns."[169] See proposed revisions to the definition of "lender" at section 3.4.2

[168] Proposed Comment 2(a)(17)-1.
[169] 81 Fed. Reg. at 47908.

above, where we urge including "service provider" in the definition of "lender" to ensure that all loans involving CSOs and CABs are addressed as the rule intends.

3.9. "Total cost of credit": § 1041.2(a)(18).

We support the proposal's approach to provide a broad definition of "total cost of credit" that includes not only finance charges under Regulation Z, but any application fee, participation fee, charge imposed in connection with credit insurance (whether "voluntary" or not), and fees for credit-related ancillary products.[170] We also support the Bureau's note that fees paid by consumers to credit access businesses or credit service organizations are typically finance charges and thus would be included in the total cost of credit. A broad approach is critical to prevent evasion and consistent with the DoD's efforts to do the same under the MLA.

However, to prevent evasion that would persist under the proposal, we urge:

- Eliminating the exclusion of the cost of credit insurance and other ancillary products added more than 72 hours after disbursement of funds; and
- Explicitly ruling that all ancillary products are "credit-related."

Excluding costs incurred more than 72 hours after disbursement of funds will lead to evasion.[171] The Bureau explains that the purpose of this 72-hour period is to "ensure" that lenders cannot evade the rule. The Bureau further notes that it believes lenders' leverage will have diminished by 72 hours later, "and thus it is less likely that any charge for credit insurance or other credit-related ancillary products and services that the consumer agrees to assume after that date is an attempt to avoid coverage under" the leveraged payment mechanism/vehicle title trigger.

This approach leaves undue risk that lenders will use the 72-hour gap to evade the cost-based threshold, and thus the scope of the rule altogether, while still making very high-cost loans. Two points of context are very important here.

First, credit insurance and ancillary products have played *a key role* in lenders' evasion of cost limits in the past, and they should be fully expected to do so here if not fully covered. Consumer finance lenders, for example, sell more credit insurance in states with lower interest rate limits than they do in states with higher or no limits.[172] And where they do sell it, these "voluntary" products can have close

[170] § 1041.2(a)(18).

[171] § 1041.2(a)(18)(i)(A)-(B).

[172] The interactive map provided here—http://projects.propublica.org/graphics/installment-loans—shows the stated APR versus the effective APR on World Acceptance loans in the states where the company operates. In a state like Missouri that has no rate cap on longer-term loans, the effective and stated APRs are identical (203.9% each), meaning that the company does not sell insurance products (since that cost is typically excluded from the APR). But in states with rate caps on longer-term loans, the effective APR far exceeds the stated rate, with the difference largely attributable to credit insurance and other ancillary products. For example, Kentucky has a 36% rate cap for installment loans like World's. The stated APR on World's loans there is 33.6%, versus an effective APR of 75.1%. Pro Publica reported that World said that whether or not it sells insurance products in a state depends on state law and if "it makes business sense to do so." Kiel, Paul. The 182 Percent Loan: How Installment Lenders Put Borrowers in a World of Hurt (May 13, 2013), https://www.propublica.org/article/installment-loans-world-finance.

to 100% attachment rates.[173] Second, particularly on high-cost loans, credit insurance and other ancillary products are typically little more than junk fees that provide notoriously little value to the borrower.[174]

Thus, the rule should include the cost of all credit insurance and other ancillary products in the total cost of credit regardless of when the cost is incurred. Consistent with our proposed modifications to the leveraged payment mechanism trigger at section 4.4 below, if a lender does not make a reasonable ability-to-repay determination at the outset, then it should not be permitted to sell credit insurance or other ancillary products later that would put the all-in APR above 36%.

We note that including the cost of credit insurance and other ancillary products regardless of when incurred is the approach most consistent with the MLA, which both explicitly requires that credit insurance and other ancillary products be included in the MAPR and explicitly prohibits their costs from being excluded as "bona fide" fees for purposes of the credit card exemption.[175]

As an alternative approach, as also proposed for the leveraged payment mechanism prong at section 4.4 below, the rule could provide that if more than 25% of the portfolio exceeds an all-in APR including ancillary products, then all future loans must comply with the rules. In addition, the rule's payment protections should apply to any loan that exceeds an all-in 36% at any point during the loan term.

Further, we urge that the Bureau clarify that the term "credit-related ancillary products" includes any products or services sold by the lender, its affiliate, or a service provider that is in any way involved in a credit transaction. There is no end to the range of products that lenders may sell in an effort to increase the cost of a loan without triggering coverage under the rule. Whatever the value of these products when sold with a purchase money loan for a new car, they are highly likely to be exploitative in connection with covered high-cost auto title loans. Extended warranties and service contracts in particular have often proven to be scams.[176] It is also unclear whether the current definition includes auto club memberships, which are being included in certain lender proposals pushed at the state level.[177]

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[173] The attachment rates of these products in states where World sells them are close to 100%. In one study, 100% of World borrowers in samples from Tennessee and Louisiana and 99% in a sample from South Carolina had purchased a voluntary product. 96% of all such borrowers across all five states purchased a voluntary product; 75% purchased two or more voluntary products. The average borrower purchased 2.42 voluntary products per loan. "Mangrove Partners: Presentation to the Consumer Finance Protection Bureau." Washington, D.C., August 20, 2013. On file with Consumer Federation of America.

[174] See, e.g., Why Credit Insurance Is a Poor Value, Bank Talk (Sept. 11, 2015), http://banktalk.org/content/why-credit-insurance-poor-value; *See, e.g.,* Carolyn Carter, et al, Nat'l Consumer Law Ctr., "Installment Loans: Will States Protect Borrowers from a New Wave of Predatory Lending?" at 13-17 (2015), http://www.nclc.org/images/pdf/pr-reports/report-installment-loans.pdf (discussing loan packing); Paul Kiel, "The 182 Percent Loan: How Installment Lenders Put Borrowers in a World of Hurt", *ProPublica* (May 13, 2013), https://www.propublica.org/article/installment-loans-world-finance (discussing how add-on credit-related products increased the cost at no benefit to the borrower).

[175] 80 Fed. Reg. 43559 (July 22, 2015), http://www.gpo.gov/fdsys/pkg/FR-2015-07-22/pdf/2015-17480.pdf.

[176] *See* FTC, Auto Service Contracts and Warranties, https://www.consumer.ftc.gov/articles/0054-auto-service-contracts-and-warranties#beware.

[177] Arizona HB 2152, Signed into law March 24, 2016, http://www.azleg.gov//FormatDocument.asp?inDoc=/legtext/52leg/2r/bills/hb2152o.asp&Session_ID=115; Texas HB 3938 (2015), http://www.legis.state.tx.us/BillLookup/History.aspx?LegSess=84R&Bill=HB3938; *See also* Ben Protess, "Subprime Lender, Busy at State Level, Avoids Federal Scrutiny," The New York Times (Sept. 6, 2016)

4. THE SCOPE OF THE RULE IS APPROPRIATELY BROAD BUT SHOULD BE BROADER: § 1041.3.

4.1. Overview.

The scope of the rule is essential to its success. As discussed in sections 2.6.1 and 2.6.2 above, payday lenders have proven themselves adept at evading the scope of rules designed to cover them. The proposed scope is strong in that it applies to high-cost payday and car title loans regardless of how large they are or how long their stated term is, and it applies regardless of a lender's status as a government-insured depository institution or a tribe. But in other respects, the scope of the rule is significantly narrower than the evidence suggests it should be, and we urge the Bureau to broaden it accordingly. We make the following recommendations:

- The scope appropriately applies regardless of loan term, size, or issuer.
- Vehicle title loan coverage should not depend on whether the title is a "condition" of the loan.
- *All* high-cost loans with leveraged payment mechanisms or vehicle titles should be included. Lenders will game a rule limiting coverage to mechanisms obtained within 72-hours. Alternatively, the rules should apply to any lender that has obtained a leveraged payment mechanism from at least 25% of its borrowers.
- The 36% fee-inclusive APR must include all ancillary products, and regardless of when their cost is incurred.
- The term "leveraged payment mechanism" should be defined more broadly:
    - Payroll deduction loans should be included whether the payroll deduction is "voluntary" or not.
    - Loans where the lender retains the right to garnish wages should be covered.
    - We agree that coverage should not be limited to repayment tied to payday.
- Certain proposed exclusions from scope should be eliminated or narrowed to prevent foreseeable evasion:
    - The exclusion for credit cards should be eliminated or narrowed to lower-cost mainstream credit cards, consistent with the MLA approach.
    - The exclusion for pawn loans should be narrowed.
    - The exclusion for overdraft lines of credit should be eliminated or narrowed.
    - The exclusion for student loans should be eliminated.
- High-cost loans secured by personal property should be covered, consistent with the long-standing FTC Credit Practices Rule.
- In addition, any high-cost loan should carry an ability-to-repay requirement.

4.2. The Scope Appropriately Covers Loans Regardless of Length, Size, or Issuer: §1041.3(b)(2).

We strongly support the proposed scope as including both short-term balloon payment payday and vehicle title loans as well as longer-term loans for reasons discussed at sections 2.5 above and 10.2 and

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(noting "Another successful bill this year enabled the company to offer new types of insurance policies alongside its loans, including accidental death and dismemberment coverage, an important area for OneMain."), http://www.nytimes.com/2016/09/07/business/dealbook/subprime-lender-busy-at-state-level-avoids-federal-scrutiny.html?_r=0.

10.3 below.[178] Lenders can be expected to evade any rule that applies only to loans of less than a certain length.

The Bureau solicits comment on whether the scope for longer-term loans should be limited by a maximum loan size. A maximum loan size would invite evasion. Lenders have already used loan size limits to evade interest rate caps. One lender, for example, offered larger loans to consumers who wanted smaller loans and urged them to immediately repay the excess.[179] Additional examples include $601 vehicle title loans to evade South Carolina's $600 loan limit; California and Virginia loans over $2,500 to avoid the rate caps that apply to loans under that threshold; and evasions of the New Mexico 2007 Payday Loan Reform Act.[180]

The Bureau asks whether it should exclude loans with payments that are fully amortizing or not timed to coincide to payday, that lack prepayment penalties, or that restrict the collection methods that would be used in the event of default. We know of no evidence that such limitations would significantly mitigate the risk of evasion or the harm caused by unaffordable loans, particularly large ones. While those features can cause their own harms, dangerous high-cost loans that are not based on ability-to-repay take many forms.

Finally, the rule should, as proposed, apply regardless of lender status as a bank, credit union, or tribal-affiliated entity. Both banks and credit unions have made abusive payday loans in the past,[181] and tribal entities, even if the genuine lender, are clearly subject to federal law.

4.3. The Scope Should Include All Vehicle Title Loans, Regardless of Whether the Title Is a "Condition" of the Loan: § 1041.3(d) and Comment 3(d)(1)-1.

Section 1041.3(d) provides that a lender or service provider obtains "vehicle security" "if it obtains an interest in a consumer's motor vehicle . . . *as a condition of the credit*, regardless of how the transaction is characterized by State law." It goes on to provide that this includes any security interest

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[178] *See* Letters to CFPB, each from over 100 organizations, urging inclusion in scope and strong protections for longer-term loans: http://ourfinancialsecurity.org/2014/03/letter-regulator-afr-100-organizations-push-bureau-include-longer-term-multi-payment-products-expected-cfpb-rules-payday-lending/ (March 28, 2014); http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_longterm_loan_apr2016.pdf (April 2016); *see also* letter from 100+ Ohio groups to Director Richard Cordray, Consumer Financial Protection Bureau (Aug. 11, 2015), *available at* http://www.cohhio.org/files/Cordray%20letter%20stronger%20rules.pdf.

[179] CashCall paid a $1 million settlement in response to charges that it falsely advertised smaller loans and pushed consumers into taking out larger loans even though the customers didn't need or want to borrow that much. Calif. Dept. of Bus. Oversight, Press Release, "CashCall Pays Nearly $1 Million of Restitution to California Borrowers Under DBO Settlement" (July 10, 2015), http://www.dbo.ca.gov/Press/press_releases/2015/CashCall%20Restitution%20Announcement%2011-18-15.asp.

[180] Details on file with CRL.

[181] See 2013 Comments several of the undersigned groups submitted to the OCC and FDIC in response to their proposed guidance addressing deposit advance products, *available at* http://www.responsiblelending.org/research-publication/advocates-support-proposed; Letter from Lauren Saunders, NCLC to Michael E. Fryzel, National Credit Union Administration (Jan. 27, 2009), http://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/letter-ncua-payday-0109.pdf; NCLC, Stopping the Payday Loan Debt Trap: Alternatives that Work and Ones that Don't (June 2010), http://www.nclc.org/issues/stopping-the-payday-loan-trap.html (NCLC, Payday Loan Alternatives).

in the vehicle, title, or registration, regardless of whether it is perfected or recorded, as well as a vehicle title pawn loan. Comment 3(d)(1)-1 explains that a lender or service provider's interest in a vehicle is only a "vehicle security" to the extent that it is obtained "in connection with the credit." The rule does not cover a person that holds a security interest unrelated to the extension of credit. The Bureau provides the example of mechanic's lien attaching to the vehicle by operation of law because the consumer does not pay a mechanic's bill.

We support the Bureau's proposal to include loans secured by an interest in a motor vehicle regardless of how the transaction is characterized under State law and of whether the interest is perfected or recorded. As the Bureau notes, some loans are characterized under state law as "title pawn," and others, as in Arizona, are secured by *registration* to encumbered vehicles rather than by titles. As the Bureau recognizes, these should all be covered on the basis that the borrower reasonably believes that the car is security for the loan, leading to the same lender disincentive to determine ability to repay and the same risk of borrower harm as other vehicle title loans covered by the rule.

We urge the Bureau to make clear that any purported interest in the vehicle qualifies, even if there is no legal interest. As the Bureau discusses, some lenders may require consumers to hand over their registration or title but may not actually hold any legal interest in the vehicle. But the lender can still threaten to repossess the vehicle and coerce unaffordable payments even if the security interest is cloudy or nonexistent. While the Bureau appears to intend to cover such scenarios, it should add a comment with an example of this type of practice.

At the same time, we oppose the requirement that the security must be "a condition of the credit." In the context of Regulation E, lenders regularly evade the ban on requiring repayment by preauthorized EFT as a "condition of credit." The Bureau has observed that lenders use a variety of methods to coerce borrowers into preauthorizing EFTs despite the claim that doing so is voluntary: "in practice online payday and payday installment lenders are able to obtain such authorizations from consumers for almost all loans."[182] The same will happen with vehicle title lenders, and the Bureau and State enforcement agencies will have to litigate whether the security was required or not. Once a lender obtains vehicle title security, it does not matter how it was obtained. The impact on the borrower (and the lender) is the same.

We urge the CFPB to delete the phrase "as a condition of the credit" altogether. If it is a "lender" that obtained the vehicle title, then the loan should be covered. If ensuring that mechanic's liens are not covered is the Bureau's concern, we urge the Bureau to provide a narrow exclusion for mechanic's liens rather than an unnecessarily narrow definition of vehicle title loan that risks evasion.

A less preferable approach, but still better than the proposed, would be to replace "as a condition of" with "in connection with"—the language used in the proposed Comment. That language emphasizes the connection to the credit extension without getting into semantic debates about whether it was required or not.

[182] 81 Fed. Reg. at 47989, n.63.

4.4. The Scope Should Include All High-Cost Loans with a Leveraged Payment Mechanism or Vehicle Title, Beyond 72 Hours After Disbursement of Loan Proceeds: § 1041.3(b)(2)(ii).

The Bureau has proposed to apply the rule to longer-term loans only if the lender obtains a leveraged payment mechanism or a vehicle title within 72 hours of the entire disbursement of funds. The Bureau's rationale is that (1) it believes lender's leverage to obtain an authorization or security interest will "ordinarily have diminished" by then, and (2) there is a benefit in "allowing for consumers to set up automatic repayment as a matter of convenience at a later date."

This approach is insufficient to prevent foreseeable evasion. Instead, the rule should (1) include loans with a leveraged payment mechanism regardless of when authorization is obtained, which for practical purposes means the lender must either perform an ability-to-repay determination upfront or be prohibited from obtaining payment authorization later; and (2) prevent obtaining a vehicle title after the disbursement of funds. In the alternative, the Bureau should provide that any portfolio for which recurring payment authorization is obtained for more than 25% of loans, assessed quarterly, becomes subject to the scope on a going-forward basis, for all loans within the portfolio.

The risks of the proposal as designed far outweigh the benefits. We are already hearing reports of lenders that are planning to obtain leveraged payment mechanisms after 72 hours to evade coverage. There are just too many ways that lenders can coerce borrowers into doing so.

The Bureau is attempting to exclude lenders such as community banks that do not rely on leveraged payment mechanisms or vehicle titles as a substitute for underwriting but instead allow their borrowers to repay that way as a convenience. But the Bureau's primary task here is to prevent harm for a category of loans that goes well beyond community banks and includes some of the highest-cost, highest-risk loans available.

Further, consumers can still set up automatic bill payment through their own bank or prepaid accounts to obtain the convenience of automatic payment. These types of auto-pay are in the consumer's control and are not within the definition of leveraged payment mechanism. They can easily be changed or stopped any time the consumer desires; the lender does not have the ability to debit the account unilaterally.

Indeed, any high-cost loans where the lender can be first in line to the borrower's account *should be covered*. The ability to obtain direct access to the borrower's funds later still reduces the incentive to determine ability-to-repay upfront. It still triggers a need for the protections against failed payment transfers. And borrowers caught in an unaffordable loan will be subject to all the harms posed by a lender's control over their bank accounts, even if that control is taken later.

A better way for lenders to avoid being subject to the rule is to lower their rates. Or they could conduct an ability-to-repay analysis regardless of whether the consumer authorizes a leveraged payment mechanism.

We appreciate the Bureau's efforts to anticipate evasion of this provision, including providing examples in the Commentary of what constitutes obtaining a leveraged payment mechanism: requiring future authorization[183] or requiring a leveraged payment mechanism, wage assignment, or similar assignment

[183] Proposed Comment 3(b)(2)(ii)-1.

upon delinquency or default.[184] In addition, the anti-evasion provision suggests that offering a monetary or non-monetary incentive to obtain authorization after 72 hours may raise evasion concerns. At the very least, the rule should cover loans if the lender has a pattern or practice of providing monetary or non-monetary incentives for providing payment authorization after 72 hours. The Bureau acknowledged the significance of a lender incentive in this context in the SBREFA outline approach, where a lender incentive was one factor that would have triggered coverage under the leveraged payment mechanism prong in that proposal.[185]

The Bureau should also add another evasion example for financial institutions and open-end lenders that unilaterally change the terms of an account—either the credit account or the deposit account—after 72 hours to add a wage assignment, automatic transfers, or other leveraged payment mechanism.

But these Commentary examples are not strong enough to counter the extremely strong incentive lenders will have to avoid the scope of the rule entirely. Lenders may simply send consumers texts or emails 20 times per day with the note: "Click here to never miss a payment!," which the consumer eventually clicks just to stop the onslaught of messages.

For vehicle title, as the Bureau notes, consumers do not provide their vehicle title as a convenience, and lenders may well ask for a title as a concession when a borrower is having trouble paying. We see no benefit to, and only harm from, permitting taking a vehicle title after 72 hours.

Other alternative approaches the Bureau might consider, which we do not expect would provide adequate protections but that are stronger than the proposed rule, include:

- Apply the rule's payment protections to any loan for which a payment mechanism is taken at any point;
- Prohibit obtaining payment authorization without a reasonable ability-to-repay determination, even if the specific requirements of § 1041.9 do not apply, and apply the same back-end measures for review of delinquency and defaults as apply to other covered loans.

4.5. The Proposed Cost-Threshold of 36% Fee-Inclusive APR Is Reasonable But Must Include All Ancillary Products: § 1041.3(b)(2)(i)); § 1041.2(18)(a).

We support focusing the regulatory intervention for longer-term loans on those with an all-in cost exceeding 36%. We agree that as the cost increases, so does the risk of harm from inability to repay. A higher cost means a reduced incentive to underwrite, particularly when a leveraged payment mechanism or coercive security interest is involved.

We appreciate the Bureau's recognition of many states' usury limits and the MLA as strong precedent for a cost threshold of 36%. Limits on loans over 36% have a long history, dating back over 100 years, and have been reaffirmed repeatedly at the state and federal level.[186]

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[184] Proposed Comment 3(b)(2)(ii)-2 and -3.

[185] CFPB SBREFA Outline at 19.

[186] *See* Lauren K. Saunders, NCLC, Why 36%? The History, Use, and Purpose of the 36% Interest Rate Cap (April 2013), https://www.nclc.org/images/pdf/pr-reports/why36pct.pdf.

While we support a 36% rate cap, the proposed rule does not cap rates and thus does not implicate Dodd-Frank's prohibition on CFPB setting a usury limit.[187] Rather, it merely applies "differential regulation," focusing protections on loans more likely to cause substantial harm. Indeed HOEPA, which applies additional protections to high-cost mortgages, is not considered a usury law.[188]

Two elements of this approach, however, pose undue risk of evasion: excluding the cost of credit insurance and other ancillary products incurred 72 hours after disbursement, and a potentially overly narrow definition of ancillary products. We discuss these in the section on the definition of "total cost of credit" at 3.9 above.

4.6. "Leveraged Payment Mechanism" Should Apply to a Broader Range of Payment Arrangements: § 1041.3(c).

Proposed § 1041.3(c) defines the term "leveraged payment mechanism" to include a lender's:

- right to transfer money from a consumer's account;
- contractual right to obtain payment directly from the consumer's employer or other source of income (typically a wage assignment); and
- requiring the consumer to repay the loan through payroll deduction or deduction from another source of income.

We strongly urge the CFPB to strengthen this definition by including all payroll deduction loans, not just those where such deduction is "required." We also urge that it include the right to garnish wages. We agree that the definition should not be limited to repayment timed to payday.

We provide our recommendations on fintech providers that provide early wage access or income smoothing products in our discussion of the definition of "lender" at 3.4.3 above.

4.6.1. Payroll deduction loans should be included whether or not the deduction is "required": § 1041,3(c)(3).

The proposed definition of "leveraged payment mechanism" includes a lender that "requires" the consumer to repay the loan through payroll deduction or from another source of income.[189] The Bureau solicits comment on whether the definition should include circumstances where the lender provides an incentive for payroll deduction, noting that consumers may choose payroll deduction for convenience.

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[187] We also appreciate the Bureau's emphasizing that rate limits of less than 36%, in place in a number of states, will not be affected: "The protections imposed by this proposal would operate as a floor across the country, while leaving State and local jurisdictions to adopt additional regulatory requirements (whether a usury limit or another form of protection) above that floor as they judge appropriate to protect consumers in their respective jurisdictions." 81 Fed. Reg. at 47913.

[188] *Katline Realty Corp. v. Avedon*, 183 So. 3d 415 (Fla. 3d DCA 2014) (noting that HOEPA is not a usury law); S. Rep. No. 103-169 at 21 (1993), *reprinted in* 1994 U.S.C.C.A.N. 1881 ("Subtitle B does not create a usury limit or prohibit loans with high rates or high fees.... The bill amends the Truth in Lending Act to ... ensure that consumers understand the terms of such [high cost] loans.").

[189] § 1041.3(c)(3); Proposed Comment 3(c)(3)-1.

We do not observe any meaningful distinction between a “voluntary” payroll deduction for convenience and other “voluntary” preauthorized payments, which are covered regardless of whether or not they are incentivized.[190] Indeed, all preauthorized recurring electronic fund transfers are purportedly “voluntarily,” because compulsory use is prohibited by Regulation E.[191] But that does not stop lenders from effectively requiring it through a variety of steering mechanisms, incentives, and hurdles. The CFPB has found that “in practice online payday and payday installment lenders are able to obtain such authorizations from consumers for almost all loans.”[192] As noted above regarding ACH authorization, regardless of how the authorization is obtained, high-cost lenders who have direct access to the borrower’s funds have little incentive to determine ability-to-repay, and borrowers caught in a debt trap are harmed. Exempting “voluntary” payroll deduction loans would completely gut the protections for payroll deduction loans.

Payroll deduction is also different from preauthorized payments, as it is rarely used for consumers with prime credit scores and is not something that consumers routinely use as a matter of convenience. Rather, it is first and foremost a way of securing loans made to borrowers with lower credit scores who need the protection of this rule. Consumers rarely set up payroll deduction after taking out a loan. This would likely happen only if the lender pushed the consumer into doing so to evade the rule. The CFPB notes that consumers may wish to use payroll deduction as a form of “convenience.” But the same can be said for preauthorized payments and even more so.

Further, the fact that an employer is involved in a payroll deduction loan does not make it less likely to cause consumer harm. For example, Shutter Lending provides balloon-payment payday loans through payroll deduction at rates as high as 1,642% APR.[193]

Since payroll deduction provides a lender even higher priority than other preauthorized payments, the Bureau’s reasoning for why all preauthorized electronic fund transfers are leveraged payment mechanisms supports the conclusion that all high-cost payroll deduction loans should be as well, regardless of whether they are voluntary or whether they are incentivized.[194] This issue is discussed at greater length in section 7.5 below.

We agree that payroll deduction loans should be covered whether the payroll deduction is one-time or recurring.[195] Some payroll deduction loans, like Shutter Lending’s, are single-payment payday loans. In addition, as discussed in section 13 below, some payday lenders reserve the right to use wage assignment as a backup collection mechanism, which could be a one-time event.

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[190] Until changes adopted in 2016, Illinois required borrowers who had opted-in to a “voluntary” wage assignment to provide a legal defense to revoke authorization in conflict with federal law. See http://illinoisassetbuilding.org/wp-content/uploads/2016/03/Wage.Assignment.Fact_.Sheet_2-25-16.pdf
[191] 15 U.S.C. § 1693k.
[192] 81 Fed. Reg. at 47893.
[193] https://www.shutterlending.com/fee_schedule.html.
[194] While we oppose the approach the Bureau has proposed in limiting the timeframe for a leveraged payment mechanism to trigger coverage to 72 hours, we note that applying an “incentivized-or-not” approach to payroll deduction coverage would set up yet another series of complicated tests to determine scope.
[195] Proposed Comment 3(c)(3)-1.

4.6.2. Leveraged payment mechanism should include the right to garnish wages.

Proposed Comment 3(b)(2)(ii)-3.iii provides that a leveraged payment mechanism includes contractual wage assignment triggered by delinquency or default. We support this provision and urge its logical extension to loans where the lender retains the right to garnish wages. This right similarly reduces lenders' incentives to determine ability to repay, and unaffordable loans that lead to wage garnishment cause consumers severe harm. We note one example of a Missouri borrower whose $80 loan ballooned into a balance of over $19,000 due to post-judgment interest, for which the lender has already collected over $5,400 via wage garnishment.[196] The Bureau should add that a leveraged payment mechanism includes a loan contract that does not waive the collection remedy of wage garnishment.

4.6.3. Leveraged payment mechanism is appropriately not limited to payment schedules timed to coincide with expected inflows.

As proposed, leveraged payment mechanism loans should be covered regardless of whether scheduled payments are timed to coincide with expected inflows. Adding this limitation would be difficult to enforce and easy to evade. Lenders will often know when borrowers are likely to be paid. If not, they could often predict the date with reasonable precision, even by guessing—e.g., on Fridays, or on the 15th and last day of each month. In addition, having direct access to the borrower's account provides a significant disincentive to underwrite even if it is not precisely timed to payday.

4.6.4. "One-time" immediate electronic fund transfers should be limited and closely monitored for evasion: § 1041.3(c)(1).

The definition of "leveraged payment mechanism" does not include the initiation of a one-time electronic fund transfer immediately after the consumer's authorization. For example, a loan would not be a covered loan if the lender did not otherwise hold a leveraged payment mechanism but the consumer called and authorized an electronic payment that was due that day.

We note that Comment 3(c)(1)-3 provides the example of consumer who "does not otherwise provide" for transfers and where the payment is made "within minutes" of the authorization. We support this Comment's indication that this exclusion is **narrowly drawn**; we urge that it remain so and **carefully monitored to identify abuse.**

4.7. Certain Proposed Exclusions from Scope Should Be Narrowed: § 1041.3(e).

Several proposed exclusions from scope are far too broad and will invite evasion; we address each in turn below.

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[196] CRL, *Migration*, *supra* (citing Hollins v. Capital Solutions Investments I, Inc., No. 102093, 2015 WL 3485877 (Mo. Ct. App. June 2, 2015) (Dowd, R., concurring); *see also* Paul Kiel, "When Lenders Sue, Quick Cash Can Turn Into a Lifetime of Debt," Dec. 13, 2013. http://www.propublica.org/article/when-lenders-sue-quick-cash-can-turn-into-a-lifetime-of-debt.

4.7.1. The exclusion for credit cards should be narrowed to lower-cost mainstream credit cards, consistent with the MLA approach: § 1041.3(e)(3).

The Bureau has proposed to exclude all credit cards covered by the CARD Act.[197] We agree with the Bureau's general reasoning that few current credit cards would be covered even without this exclusion, because most charge all-in rates below 36%. However, the proposed broad exclusion for credit cards opens a wide avenue for evasion.

While the CARD Act's protections have been meaningful in the mainstream credit card market, even its fee harvester protections and its ability-to-repay requirements have not protected those with lower credit profiles from abusive credit terms.[198] As we understand it, issuers largely comply with the ability-to-repay requirement by relying on stated income and checking credit scores.[199] In the traditional credit card market, most issuers will not extend credit to consumers whose extremely low credit scores and information contained in credit reports suggest inability to pay.

But the deep subprime market is clearly different. If high-cost credit cards are not covered under the rule, payday lenders may migrate to them as a way to continue making unaffordable loans.

Payday lenders may issue very high-cost traditional Visa- or MasterCard- branded credit cards that are unaffordable for many payday borrowers.[200] They may load cards up with unaffordable fees while disclosing a relatively reasonable interest rate on them (e.g., $500 credit limit, $95 pre-application fee, $125 annual fee, 30% APR – all in compliance with the fee harvester rules).[201]

But payday lenders may also exploit the broad, vague Regulation Z definition of credit card to issue "credit cards" that bear no resemblance to traditional credit cards. Under Regulation Z, a credit card is "any card, plate, or other single credit device that may be used from time to time to obtain credit."[202] There are no limitations on what the card or device can be. The Regulation Z Commentary clarifies that a "credit card" can even be an account number without a device, if it accesses an open-end line of credit to purchase goods or services—on the Internet, for example.[203]

In addition, payday lenders could take advantage of the provisions of the new prepaid cards rules that will deem a prepaid card to by a hybrid prepaid-credit card if the card can access credit through

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[197] Proposed § 1041.3(e)(3).

[198] For example, on one fee harvester card, First Premier charges a $95 "processing fee" before the account is opened and a $75 annual fee for a card with a $300 credit limit. The fee harvester loophole allows the $95 fee to be imposed, meaning that consumers may be charged $170 in fees, more than half of their credit limit, before they make a single purchase. In subsequent years, when no fee cap applies, that same fee harvester card charges $120 in annual and "monthly servicing" fees, on top of 36% interest, for a card with only a $300 credit line.

[199] Consumer Financial Protection Bureau, Consumer Credit Card Market Report 142 (Dec. 3, 2015), available at http://files.consumerfinance.gov/f/201512_cfpb_report-the-consumer-creditcard-market.pdf

[200] There is nothing in Visa or MasterCard rules to prevent high-cost credit cards. The only limiting factor is the reluctance of banks and the networks to be associated with payday lenders and high-cost cards. But some issuers have been willing to issue credit cards with terms that appear clearly unaffordable.

[201] These are similar to First Premier's terms noted at 198 above.

[202] 12 C.F.R. § 1026.2(a)(15)(i). The current proposal's exclusion of the narrower "credit card accounts" definition under the CARD Act does not limit these sweeping elements of the Regulation Z's broad definition.

[203] Official Interpretations § 1026.2(a)(15)-2.ii.C (providing that an account number that accesses a credit account is a credit card if the number can access an open-end line of credit to purchase goods or services).

overdrafts at the point-of-sale, ATMs or person-to-person transfers. While fees in the first year will be capped at 25% of the credit line, the interest rate will not be. Thus, a 300% APR overdraft line of credit could be attached to a prepaid card. That credit line would be a “credit card” and would fall within the exemption from this rule.

We are concerned that any carve out for credit cards could be used as means to evade the rule, inviting payday lenders to migrate to “credit cards,” broadly defined. Payday lenders may issue a card that consumers can use when coming in for cash draws on an open-end line of credit. They could design a card that is accepted for goods or services at a more limited range of merchants than are accepted by Visa and MasterCards—such as for bill payments, check cashing and other goods or services sold at payday lending stores. As discussed at section 2.6 above, the creativity of payday lenders has no bounds.

We urge the Bureau not to provide any blanket carveout for credit cards. Instead, we urge that any exclusion be limited to an exclusion of reasonable, customary “bona fide” credit card fees from the “total cost of credit” definition that determines whether a longer-term loan is subject to the rule. This approach is consistent with that under the new MLA regulations.[204] Indeed, we highlight the DoD’s rationale for not providing a blanket exemption for credit cards here:

> Even though the CARD Act provides certain protections for all consumers that are not inconsistent with overarching objectives evident under the MLA, the Department has determined, at this time, that the interest-rate limit and other requirements of the MLA should not be completely set aside in reliance on the CARD Act for covered borrowers. The Department continues to believe that certain creditors could take advantage of an opportunity to exploit a complete exemption for credit cards by transforming high-cost, open-end credit products (which otherwise would be covered as ‘‘consumer credit’’) into credit card products.[205]

Mirroring the DoD’s approach will exclude the vast majority of mainstream credit cards while greatly reducing the risk of evasion. And it would have the added benefit of replicating a regulatory framework that is already being implemented.

Even if the Bureau does exempt credit cards from the longer-term portion of the rule, it should not exempt short-term credit cards unless the interest rate is MLA-compliant and there is no fee or charge if paid off in full each cycle. With this approach, the American Express charge card would be exempt, but a payday lender card that requires payment every 15 or 30 days at a rate of $15 per $100 would not be. Indeed, given the loose definition of “credit card,” lenders could issue charge cards that are due in full 14 or 30 days later, along with a very high fee.

The Bureau should, at a minimum, narrow the definition of “credit card” to fit the common understanding of a credit card. We propose this definition:

> 1) Credit card means any card, plate or other single credit device that may be used from time to time to obtain consumer credit under an open-end credit plan and that is either:

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[204] 32 CFR Part 232.4(d); see DoD’s discussion of its approach at 80 Fed. Reg. 43560, 43585 (July 22, 2015).
[205] 80 Fed. Reg. at 43573.

(a) Accepted by every merchant that participates in a widely accepted payment card network and is accepted upon presentation at multiple, unaffiliated merchants for goods or services,[206] or

(b) Accepted solely for the bona fide purchase of goods or services at a particular retail merchant or group of merchants and not to access cash,[207]

2) Provided that the term "credit card" does not include an overdraft line of credit that is accessed by a debit or prepaid card or an account number.

We further propose that the commentary to the regulations include the following examples:

(a) Examples of network branded credit cards: Cards that carry the Visa, MasterCard, American Express or Discover brands are network branded, are widely accepted, and are redeemable at multiple unaffiliated merchants and ATMs.

(b) Examples of merchant credit cards: Department store or gasoline credit cards are examples of merchant credit cards. A credit device that is not accepted by retail merchants for a bona fide purchase of goods or services is not a merchant credit card. For example, a credit device that offers credit primarily for worthless or overpriced goods or bogus buying clubs is not a merchant credit card.

The Bureau notes that it considered a narrower credit card exemption such as this but did not explain why it did not adopt this limitation, which would prevent evasions. This definition would cover all Visa, MasterCard, Discover and American Express cards as well as all department store cards, gas cards, and other traditional credit cards, without risking exotic new forms of payday lender credit cards.

If the CFPB retains a credit card exemption, it should also narrow that definition by excluding overdraft lines of credit from it. There is precedent for this exclusion, because Regulation Z presently excludes overdraft credit from the definition of the "credit cards" that are subject to the CARD Act protections.[208] While the final prepaid card rules do not extend that exclusion to prepaid card overdraft features (and thus, prepaid overdraft credit lines *are* CARD Act credit cards), the CFPB should nonetheless cover these credit lines under the payday loan rules as well, in light of the vulnerability of prepaid card holders and the dangers of payday lender prepaid cards.[209]

Finally, if the CFPB declines to narrow the definition of "credit card," it should include a faux credit card example in a Comment to the anti-evasion provision, making clear that the exclusion for credit cards is designed for products that function as credit cards widely understood, not for any high-rate loan tied to a card, plate, or other device.

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[206] The language in subsection (a) is adapted from the Regulation E definition of "general use reloadable" prepaid card. It is not necessary to include the exclusion for home-secured or home-equity plans as those would already be excluded from the CFPB's rule.

[207] This provision is intended to capture traditional retail store credit cards but to prevent payday lenders from calling their loan a "credit card" simply because it comes with a card that can be used for a purchase at the payday store or an affiliated merchant. Any card usable at a traditional ATM would be network-branded and fit under the previous provision.

[208] 12 C.F.R. §1026.2(a)(15)(ii)(B).

[209] See NCLC, Payday Lender Prepaid Cards.

4.7.2. The exclusion for pawn loans should be narrowed: §1041.3(e)(5).

The Bureau proposes to exclude non-recourse pawn loans. As noted at 2.6.2 above, some payday lenders merely disguise their payday loan as pawns by encouraging borrowers to pawn near-worthless items. We urge the Bureau exempt pawn loans only to the extent that the loan does not exceed the fair market value of the pawned item. Otherwise, the Bureau risks sanctioning this foreseeable evasion.

4.7.3. The exclusion for overdraft lines of credit should be narrowed: § 1041.3(e)(6).

While we generally agree with the Bureau that overdraft practices warrant their own rulemaking, we urge that the proposed exclusion for overdraft lines of credit be eliminated or significantly narrowed. It is not clear that a future Bureau rulemaking on overdraft will address the types of high-cost overdraft lines that generally do not exist now but may in the future as a way of evading the payday loan rules.

There is no precise definition of "overdraft line of credit" in Regulation E or Regulation Z.[210] An overdraft line of credit could be the functional equivalent of an open-end payday loan, like deposit advance, made by a bank.[211] It could have similar pricing and a similar repayment structure, and simply be triggered by overdraft rather than by—or in addition to—an affirmative advance by the consumer. Regulation E permits compulsory use of electronic repayment for overdraft lines of credits even if the account can be accessed in ways other than overdraft.[212] An overdraft line of credit could also be a pure cash advance, covered via overdraft, through an ATM.

A few years ago the tribal payday lender SureCashXtra developed a payday loan that functioned through overdraft on a prepaid card. As the payday lender's website described it in the FAQs:

> Each branded prepaid debit card has a transaction processor that evaluates and completes ATM and Point of Sale Signature transactions that are performed on their cards. The transaction processor for your prepaid card must allow SCX [SureCashXtra] to be enabled on their system.[213]

While these are not widespread products now, they are a foreseeable evasion.

In addition, some financial institutions have been eager to promote high-cost forms of credit like deposit advance. An exemption for overdraft lines of credit could be exploited. Thus, we urge the CFPB to eliminate this exemption.

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[210] Regulation E does not define "overdraft line of credit." But discussion in recent CFPB rulemaking indicates that the CFPB understands the term to refer to a credit plan under an agreement to extend overdraft credit that is subject to Regulation Z. See 79 Fed. Reg. 77,102, 77,245 (Dec. 23, 2014).
[211] The banks that offered deposit advance claimed that it was open-end credit.
[212] Reg. E, Official Interpretations § 1005.10(e)(1)-2.
[213] See Comments of NCLC et al. to CFPB on Electronic Fund Transfers (Regulation E), Advance Notice of Proposed Rulemaking, Docket No. CFPB-20120019, RIN 3170-AA22 at 7-85 (submitted July 23, 2012), http://www.nclc.org/images/pdf/rulemaking/cm-prepaid-card-july2012.pdf (citing websites that are no longer operational).

If any exemption for overdraft lines of credit is retained, it should be limited in three ways. First, any exemption should only cover credit lines offered by depository institutions that hold the borrower's deposit account. Tribal payment processors have offered overdraft lines of credit in the past. Distinguishing between an overdraft line of credit tied to a bank account from the same government-insured depository institution, on the one hand, and nonbank credit lines, on the other, is consistent with Regulation E, which gives only financial institutions, not other entities, an exemption from the ban on compulsory use of electronic repayment.[214]

Second, any exemption should not extend to entities that hold prepaid accounts.[215] Payday lender prepaid cards permit overdrafts, and lenders will be eager to exploit an exemption for overdraft lines of credit attached to prepaid cards.[216] High-cost credit lines with triple digit APRs will be permitted under the new prepaid account rules as long as the charges are imposed through interest and not overdraft fees (and fees can be added after the first year). The weaker ability-to-repay standards of the CARD Act are not sufficiently strong for high-cost credit.

Third, any exemption should only cover customarily priced overdraft lines of credit. Traditionally, overdraft lines of credit have been low-cost methods of covering overdrafts, far less likely to cause harm than high-cost fee-based overdraft programs. But fees have been rising, and some transfer fees can be as high as $12.50 or even $20 per day, even on small overdrafts. Thus, we urge the CFPB to limit the exemption by permitting two nominal transfer fees annually, plus a reasonable and customary annual fee (which are generally, when charged, in the $25 range), on overdraft lines of credit from the total cost of credit. We note that the DoD did not exclude any costs related to overdraft lines of credit from the Military APR calculation, so all overdrafts lines of credit are fully subject to that rule.

Regarding overdraft programs more generally, we appreciate the Bureau's ongoing work in this area. We offer the observation that overdrafts at ATMs are pure cash loans and should be subject to the same or more stringent requirements as payday loans. Please see [2012 joint CFPB Comment] and CRL's most recent report on overdraft fees[217] for concerns and recommendations regarding abusive overdraft programs more broadly.

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[214] Regulation E states that "[n]o financial institution *or other person* may condition an extension of credit" on preauthorized repayment. 12 C.F.R. § 1005.10(e)(1) (emphasis added). The commentary also uses the word "creditors" to describe the entities covered by this ban. Reg. E, Official Interpretations § 1005.10(e)(1)-1. But the very next comment precisely states only that a "financial institution" may require compulsory use on an overdraft credit plan. Reg. E, Official Interpretations § 1005.10(e)(1)-2. Although, in some contexts, the term "financial institution" can encompass entities other than depositories that hold consumer accounts or issue access devices, such as government agencies, the term generally would not apply to covered lenders. However, this issue bears closer scrutiny in connection with the prepaid card rules issued this week. We have not yet analyzed the expanded definition of "financial institution" or whether it could be exploited by, for example, payday lender prepaid cards. It appears clear, however, as discussed above, that this exemption should not be extended to financial institutions (whether a depository or not) that hold the consumer's prepaid account.

[215] As discussed in section 4.7.1, the proposed exemption for credit cards should not extend to prepaid cards that are deemed to be credit cards because they have an overdraft feature.

[216] See NCLC, Payday Lender Prepaid Cards.

[217] 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.

4.7.4. The exclusion for student loans is dangerous and unnecessary and should be eliminated: § 1041.3(e)(4).

Proposed § 1041.3(e)(4) exempts (1) credit made, insured, or guaranteed under the Higher Education Act (HEA) ("federal student loans") and (2) a "private education loan" as defined in Regulation Z. The exemption for federal student loans is unnecessary but appears to be harmless. The exemption for private education loans is unnecessary for true student loans and opens up a wide loophole. Indeed, payday lenders might favor these loans as they are also exempt from bankruptcy protections.

Any legitimate student loan, federal or private, would already be exempt because it would have a term of more than 45 days[218] and would have an interest rate of 36% or less. (It is also unlikely that these loans would have leveraged payment mechanisms (and certainly not vehicle title security), as they are normally not paid back until after the student finishes school. However, it is possible that some students could authorize repayment by EFT of private student loans that do require payments to begin immediately.)

The highest interest rate on federal loans is currently 6.31%.[219] Even with loan fees of a bit over 4% of the loan,[220] and even if these rates were to be increased in the future, it is hard to imagine the total cost of credit exceeding 36%.

While rates on private student loans can be higher, they also do not approach 36%. Surveys by both the CFPB in 2012[221] and NCLC in 2008[222] found rates no higher than 19% for students with the worst credit scores. The NCLC survey found variable rates as high as 10% over the prime rate.[223] That means that even when the prime rate was at its all-time high of 20.5% in December 1980,[224] a variable rate loan with that margin would be no more than 30.5%. Even the infamous Corinthian College student loans found abusive by the CFPB had a rate of 14.9% with an origination fee of 6%.[225]

Consequently, an exemption for either federal or private student loans seems completely unnecessary.

The exemption for federal student loans does not appear to pose a danger. Federal student loans are currently originated only by the federal government. Even if the government were to return to using private lenders to originate the loans, it appears unlikely that a payday lender would ever be making loans insured or guaranteed under the HEA. Thus, we perceive no harm in the exemption for federal student loans.

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[218] Federal student loans generally have a term of 10 to 25 years. *See* https://studentaid.ed.gov/sa/repay-loans/understand/plans. A true private education loan would also surely have a term of more than 45 days.

[219] https://studentaid.ed.gov/sa/types/loans/interest-rates.

[220] *Id.*

[221]CFPB, Private Student Loans at 12(Aug. 29, 2012), http://files.consumerfinance.gov/f/201207_cfpb_Reports_Private-Student-Loans.pdf.

[222] Deanne Loonin, NCLC, Paying The Price: The High Cost Of Private Student Loans And The Dangers For Student Borrowers at 2 (Mar. 2008), http://www.studentloanborrowerassistance.org/wp-content/uploads/2013/05/Report_PrivateLoans.pdf.

[223] *Id.*

[224] *See* http://www.fedprimerate.com/wall_street_journal_prime_rate_history.htm#primeratealltimehigh.

[225] *See* Complaint For Permanent Injunction and Other Relief, CFPB v. Corinthian Colleges, et al., No. 1:14-cv-0719, at 26 (N.D. Ill. Filed Sept. 16, 2014), http://files.consumerfinance.gov/f/201409_cfpb_complaint_corinthian.pdf.

On the other hand, the Regulation Z definition of "private education loan" is far broader and could easily be exploited. Notably, a broad definition was appropriate for purpose of Regulation Z, because the goal is to ensure that students receive disclosures. A loan that is a private education loan is not exempt from any other Regulation Z requirements.

Under Regulation Z, a "private education loan" is an extension of credit that is not a federal loan; is "extended to a consumer expressly, in whole or in part, for postsecondary educational expenses, regardless of whether the loan is provided by the educational institution that the student attends;" is not open-end credit or secured by real estate; and has a term more than 90 days.[226] There is also a small exemption for certain short-term credit and payment plans extended by colleges, discussed below.

While this definition would limit lenders to longer-term loans, nothing else prevents payday lenders from claiming that a loan is for postsecondary educational expenses. The Comments to Regulation Z add no limiting detail.[227] Indeed, the Comments make clear that a creditor "generally will not know before an application is received whether the consumer intends to use the loan for postsecondary educational expenses" and make clear that the consumer's self-certification is enough: If the consumer expressly indicates that the proceeds of the loan will be used to pay for postsecondary educational expenses by indicating the loan's purpose on an application, the loan is a private education loan.[228]

Education does not even need to be the primary purpose of the loan. The consumer may use the loan "for multiple purposes including, but not limited to, postsecondary educational expenses."[229]

It also appears that the borrower does not need to be the student. The loan might qualify if part of the loan is used to support another member of the household who is a student.[230]

Thus, as long as the loan is over 90 days and the consumer "indicates" that one purpose of the loan is for postsecondary expenses (including debt consolidation of a prior "private education loan"),[231] then the loan would be exempt from the payday rules.

Moreover, the term "postsecondary expenses" is also quite broad. It includes "miscellaneous personal expenses, room and board"[232] for a student at any covered educational institution—a term that

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[226] 12 C.F.R. §1026.46(b)(5).

[227] The Comments only add: "A private education loan is one that is extended expressly for postsecondary educational expenses. The term includes loans extended for postsecondary educational expenses incurred while a student is enrolled in a covered educational institution as well as loans extended to consolidate a consumer's pre-existing private education loans." Comment 46(b)(5)-1 to Regulation Z.

[228] Comment 46(b)(5)-2.i to Regulation Z.

[229] *Id.*

[230] Regulation Z appears to distinguish between a "consumer" and a "student." A private education loan "Is extended to a **consumer** expressly, in whole or in part, for postsecondary educational expenses, regardless of whether the loan is provided by the educational institution that the **student** attends." 12 C.F.R. § 1026.46(b)(5)(ii) (emphasis added).

[231] Comment 46(b)(5)-1 to Regulation Z.

[232] 12 C.F.R. §1026.46(b)(3).

includes unaccredited schools, trade schools, questionable online schools, and other for-profit colleges.[233] Thus, lenders could claim fairly easily that a loan is for postsecondary expenses.

While TILA applies the private education loan rules to a "private education lender," that term does not limit the scope. That term includes not only financial institutions and colleges but also "any other person engaged in the business of soliciting, making, or extending private education loans."[234] Thus, it does not provide any limitations. Regulation Z does not define or use that term at all and merely refers to a "creditor" that makes private education loans.[235]

If a payday lender purported to make a private education loan, it would have to provide the disclosures required by Regulation Z. But these do not pose a significant hurdle.

First, the lender has to provide certain solicitation or application disclosures.[236] These mostly focus on rates and terms. There are also some generic notices about other options for financing education. All of these could be provided by a payday lender. Moreover, multi-purpose loans—which most payday lender education loans would be—are exempt from the application and solicitation disclosures.[237]

Second, after approval, the lender must provide another set of disclosures about the actual loan approved, including interest rates, fees, and bankruptcy implications.[238] These disclosures as well could be standardized and would not pose a hurdle for a payday lender.

Third, after the student accepts the disclosures, a private student lender must provide final disclosures.[239] These are similar to the approval disclosures, with the addition of information about cancellation rights.

Consequently, even while including all aspects of how a private education loan is defined and what burdens come with those loans, it would be simple for payday lenders to claim that many of their longer-term loans are private education loans and are exempt from this rule.

Moreover, payday lenders would get other benefits from classifying their loans as private education loans. These loans—just like federal student loans—are generally not dischargeable in bankruptcy.[240] Thus, payday lenders would get an added protection by adding the student loan label to their loans.

With all legitimate student loans already exempt from the rule based on their interest rate, and a high risk of evasions, the student loan exemption should be completely eliminated. We considered attempting to recommend a tighter definition, but that is a difficult and unnecessary project, which

[233] 12 C.F.R. §1026.46(b)(1)(i) (defined as under the HEA "without regard to the institution's accreditation status").
[234] 15 U.S.C. § 1650(a)(6).
[235] 12 C.F.R. §1026.46(a).
[236] 12 C.F.R. §1026.46(d)(1).
[237] 12 C.F.R. §1026.46(d)(1)(iii).
[238] 12 C.F.R. §1026.46(d)(2).
[239] 12 C.F.R. §1026.46(d)(3).
[240] Student loans are dischargeable only if repayment of the debt "will impose an undue hardship on the debtor and the debtor's dependents," 11 U.S.C. § 523(a)(8), a condition that courts have interpreted so narrowly as to nearly read it out of existence.

could also undermine the protections for actual private education loans. Permitting this exemption will open up a cavernous hole for payday lenders.

4.8. High-Cost Loans Secured by Personal Property Should Be Covered, Consistent with the Longstanding FTC Credit Practices Rule: §1041.3(b)(2).

We appreciate the Bureau's question in its outstanding Request For Information inquiry (RFI) about whether taking a non-purchase money interest in personal property creates the same incentives and increased risk of harm as do payday and vehicle title loans.[241] But data available now, and the longstanding principles embodied by the FTC's 1984 Credit Practices Rule, provide ample support for including these loans in the scope of the present rule.

The Bureau notes the following in the context of the public policy prong of the unfairness test for longer-term loans:

> The FTC's Credit Practices Rule bans certain provisions in consumer credit contracts allowing for extraction of unaffordable payments from consumers, such as certain provisions for wage assignments *and taking a security interest in household goods*. That rule reflects the conclusion that such provisions can cause severe risk of injury to consumers.[242]

The Credit Practices Rule found that certain security interests met the three-pronged unfairness test because they effectively coerced repayment.[243] Accordingly, the rule prohibited non-possessory interests in household goods, which it defined as including clothing, furniture, appliances, and personal effects, including wedding rings, though it also provided for some exceptions.[244] This list has not been updated for many years, and it does not include certain personal property like mobile phones and computers. The Credit Practices Rule should be updated in many respects.[245] But in the meantime, the CFPB should ensure that any high-cost non purchase-money loan secured by a non-possessory interest in personal property is subject to a reasonable ability-to-repay determination.

Loans secured by personal property provide lenders coercive leverage similar to checking account or vehicle title access. These loans can be very high cost and the model can be driven by costly renewals at the expense of ability-to-repay.

Data on loans from New Mexico, for example, suggest that personal property is being used to leverage payment and to drive churning of unaffordable high-cost loans. In 2013, there were over 92,000 loans with APRs averaging over 175% secured by property other than vehicle titles. Over half of the loans were under \$5,000.[246] On nearly a third (32%) of these loans, the principal and interest were not

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[241] 81 Fed. Reg. at 47912.
[242] 81 Fed. Reg. at 48002.
[243] 16 C.F.R. § 444.
[244] 16 C.F.R. § 444.1(i).
[245] Margot Saunders, *Time to Update the Credit Practices Rule: CFPB Should Modernize FTC Rule Addressing Abusive Creditor Collection Practices,* National Consumer Law Center (Dec. 2010), *available at* https://www.nclc.org/images/pdf/debt_collection/credit-practices-rule-update.pdf.
[246] The average loan amount was \$4,542. This and all data from New Mexico obtained here: http://www.rld.state.nm.us/uploads/files/FID%202013%20HB337%20Reports.pdf.

repaid in full, and 35% of loans were renewed, refinanced, or extended—suggesting that borrowers lacked the ability to repay on a substantial portion of loans. Yet the property was repossessed or foreclosed on in only 128 loans, suggesting that the security is being used to coerce repayment.[247]

OneMain Financial, a large consumer lender created by the merger of Springleaf Financial (formerly American General Financial) and OneMain (formerly CitiFinancial), is an example of a large company with a significant portion of loan volume (57% for Springleaf; 27% and growing for OneMain) comprised of loans that are "hard secured," principally by automobile.[248] A significant portion of its loans are not collected via preauthorized payment. Thus, many of its loans likely would not be captured by the current proposed scope of the rule. Its average loans are in the $4,000-$8,000 range with typical terms of 2-5 years, with costs that may exceed an all-in APR of 36% due to the addition of fees for ancillary products.[249] OneMain emphasizes the importance of loan renewals to its model, noting that "Renewals are primarily generated through our branch lead management system and supported by marketing campaigns."[250] In investor reports prior to the merger, Springleaf emphasized the importance of loan renewals to its model, noting that they are an important component of its business plan, expecting "a substantial portion of the Loans will be renewed . . . ."[251] It also notes the importance of the collateral: "the possible loss of the collateral creates a strong incentive for the borrower to repay the personal loan."[252]

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[247] For more information on the harm these loans cause, see Letter from New Mexico Fair Lending Coalition to CFPB, Nov. 3, 2015, urging coverage of loans secured by personal property.

[248] OneMain: ABS East Conference September 2016, available at http://investor.onemainfinancial.com/Cache/1001214618.PDF?O=PDF&T=&Y=&D=&FID=1001214618&iid=4405478, at 6.

[249] OneMain Financial, OMFIT 2015-3 Private Placement Memorandum, at 91, http://files.shareholder.com/downloads/AMDA-28PMI5/1321842233x0x867148/8308BAA5-B813-4111-84BC-31DCD0DD0918/OMFIT_2015-3_--_Final_PPM.pdf. "OneMain Financial offers its customers optional credit insurance products and membership programs, and the premiums and fees for these products and programs typically are financed as part of the principal balance of the applicable personal loan. See '*Underwriting Process and Standards—Optional Products: Credit Insurance and Membership Program*' in this private placement memorandum. This represents approximately 4.9% of the aggregate principal balance of OneMain Financial's personal loan portfolio as of June 30, 2015. Similarly, Springleaf Financial Services, 2015-B Private Placement Memorandum (http://investor.springleaffinancial.com/asset-backed-securities.cfm) states: "Springleaf, Springleaf sells credit insurance products to its personal loan borrowers. These products are provided by a group of Springleaf- affiliated insurance companies and insure the personal loan borrower's payment obligations on the related personal loan in the event of such personal loan borrower's inability to make monthly payments due to death, disability or involuntary unemployment. Payment of the associated premiums can be made by the Borrower separately, but except in very rare instances, the personal loan borrower finances payment of the premium and it is included in the principal balance of the applicable personal loan. The financing of credit insurance products premiums generally represents approximately 4.00% of the aggregate principal balance of Springleaf's personal loan portfolio."

[250] OneMain Financial Holdings, Inc. S-1 Registration Statement, filed with the Security and Exchange Commission, Oct. 8, 2014, available at https://www.sec.gov/Archives/edgar/data/1619573/000119312514366223/d793139ds1.htm.

[251] SFLT 2015-B Private Placement Memorandum, March 2015, http://files.shareholder.com/downloads/AMDA-28PMI5/3643368980x0x814024/9a099512-d40d-425c-8784-877688a3e32c/SFT_2015-A_BLACK_as_printed_.PDF.

[252] *Id.*

Capturing loans secured by personal property will not only address current harms caused by these loans, but it is also essential to prevent evasion. Some lenders may shift away from preauthorized payments or vehicle titles and opt for other personal property as security to evade the scope of the rule. This seems particularly true of lenders who already make a substantial number of both vehicle title loans and loans secured by other property. These lenders could simply shift their portfolio more heavily toward loans secured by other personal property.

4.9. All High-Cost Installment Loans Should Carry an Ability-to-Repay Requirement.

We appreciate the Bureau's statement that the current proposed rule "does not mean to signal any conclusions" as to whether it is unfair or abusive to make other types of loans without assessing ability-to-repay, as well as its statement that it may engage in future rulemakings with respect to other types of loans (or other practices on covered loans).[253] We likewise appreciate the concurrent RFI.

Ability-to-repay is the cornerstone of all responsible lending. But the specific requirements of the proposed rule may not be necessary for lower cost forms of credit, where lenders have more incentive to ensure that the vast majority of borrowers can repay their loans. Responsible lenders may take a variety of approaches to ensure that their loans are affordable and do not result in consumer harm.

But high-cost loans, even absent a coercive repayment mechanism or security, provide a significant disincentive against lending based on ability to repay.[254] In a recent case by the New Mexico Attorney General against Fast Loans, for example, the State Supreme Court found the installment loans to be unconscionable on the basis that the lender routinely originated high-cost installment loans without inquiry into the borrower's ability to repay on its terms.[255]

We urge the Bureau to use its enforcement authority without delay to address unfair and abusive practices related to lending without regard to ability to repay in the unsecured high-cost market, including the typical practice of fee-laden serial refinancing in the consumer finance market.

4.10. Additional Comments on Scope.

We make the following additional comments on scope.

4.10.1. As proposed, auto refinances above the cost threshold should be covered: § 1041.3(e)(1).

The Bureau has proposed to craft no special exclusion for auto refinances above the cost threshold, noting that some credit unions currently make such loans. We support inclusion of auto refinance loans, as (1) there seems no rationale to support excluding a loan secured by a vehicle title that exceeds the cost threshold, and (2) there is little reason to expect that a carve-out designed with credit unions in mind would not be exploited by a broader range of lenders. Even at 36%, an auto refinance loan would be very expensive, and above that level, a reasonable ability-to-repay determination should be required to prevent harm.

[253] 81 Fed. Reg. 47910.
[254] See NCLC, Installment Loans.
[255] CRL, *Migration*, at 5, n.49.

4.10.2. The proposed cut-off for short-term loans at 45 days is reasonable but should be accompanied by anti-evasion provisions: § 1041.3(b)(1).

The Bureau proposes to craft the definition of short-term covered loans as loans required to be substantially repaid within 45 days.[256] We support the Bureau's use of 45 days here and agree that longer-term loans pose different risks and require different treatment in some ways. At the same time, we flag that loans slightly beyond 45 days—say, between 46 and 90 days—are not common today and thus raise heightened concern as evasion products, designed to evade the rollover restrictions of the short-term portion of the rule.

For example, one could imagine a 46-day, $300 loan that is structured with payments of $100 on days 15 and 30 and a $199 payment on day 46. This is effectively three back-to-back payday loans at a slightly cheaper rate than is typical today. The large payment due on day 46 is likely to trigger reborrowing, even though under the rule as proposed, this is a longer-term loan and is not even a balloon-payment loan. As discussed at section 3.2 above, we urge the CFPB to significantly broaden the definition of balloon payment. But even without a large balloon, 46-day loans pose concerns. Lenders who make several back-to-back 46-day loans in a row may be disguising the unaffordability of those loans. Without the 30-day waiting requirement in between, the consumer will have just barely made it through one monthly cycle and will be reborrowing to cover the final payment.

The Bureau should explicitly address these risks in the Commentary on the anti-evasion provision, which we note at section 17.4.

In addition, we agree with the recommendation of the Small Dollar Roundtable that if a lender requires that each advance be repaid in full before another advance may be taken out—and we would add *substantially* in full—then it should be treated as a series of closed-end loans. Thus, if each draw must be substantially repaid in full in less than 45 days, it should also be treated as a short-term closed-end loan. The concept of an open-end line is one that does not have a fixed balance and that allows a consumer to carry a balance that continues to accrue interest even while the consumer may draw on the line to the extent that credit is available. We thus propose that the following comment be added either to the anti-evasion section or in a section describing the definition of short-term loans:

> The consumer borrows $300 on a purportedly open-end line of credit. The minimum payments consist primarily of a $45 monthly participation fee. The credit line does not replenish and cannot be reused if the consumer pays less than the full $345 balance. The loan is treated as a 30-day closed-end loan that rolls over each month. Each rollover is considered to be a new short-term loan for purposes of the rules.

4.10.3. Limiting covered loans to consumer purposes is reasonable, but should be accompanied by additional anti-evasion provisions: §1041.3(b).

The Bureau's limitation of covered loans to loans extended to a consumer primarily for personal, family, or household purposes, consistent with Dodd-Frank's UDAAP authority, is reasonable. We appreciate the Bureau's noting that these purposes must not be merely ostensibly so.[257] Payday

[256] § 1041.2(6); §1041.3(b)(1).
[257] 81 Fed. Reg. 47910.

lenders may attempt to disguise their loans as small business loans to evade the rule's scope. We urge the Bureau to elaborate with additional Commentary.

4.10.4. Additional proposed exemptions are reasonable: §1041.3(e).

We agree that the following proposed exemptions are reasonable: certain purchase money security interest loans, emphasizing, as the Bureau does, that this exemption should be limited to the financing of the initial purchase of the good and not exceed the cost of acquiring the good;[258] and real estate secured credit.[259]

5. LENDING WITHOUT A REASONABLE DETERMINATION OF ABILITY-TO-REPAY IS ABUSIVE AND UNFAIR: § 1041.4 and § 1041.8.

In this section, we first describe the strong and growing precedent for an ability-to-repay standard. Next, we note that there is no precedent for exempting loans primarily made to financially vulnerable consumers. We then discuss the importance of an ability-to-repay standard that explicitly requires ability to repay *while meeting other obligations and expenses and without reborrowing*, and we urge that the regulatory provision be so modified. Finally, we offer a few points of emphasis regarding the Bureau's well supported determinations of abusive and unfair practices, while urging that the unfairness finding not exclude so-called "predictable" injury.

5.1. There is Strong and Growing Precedent for an Ability-to-Repay Standard.

Just as the legal landscape reflects growing recognition of the harm of payday car title lending, it also reflects growing precedent for the ability-to-repay principle in credit markets, as well as a finding that lending without regard to ability-to-repay is an abusive and unfair practice.

Years of regulatory guidance, advisory letters, and rules, as well as a growing body of federal legislative precedent, explicitly require that a lender determine the borrower's ability to repay a loan.[260]

The 2001 Interagency Subprime Guidelines, which apply to all subprime loans (mortgage and others), provide that "mak[ing] unaffordable loans based on the assets of the borrower rather than on the borrower's ability to repay an obligation" is predatory and abusive.[261]

The OCC's 2003 letter addressing predatory and abusive lending states in strong terms that "disregard of basic principles of loan underwriting," which the OCC describes as failing to determine ability to repay, "lies at the heart of predatory lending."[262] The letter also explains how such abusive practices can raise unfairness concerns under the FTC Act's unfairness prong.

[258] § 1041.3(e)(1); Proposed Comment 3(e)(1)-1.
[259] § 1041.3(e)(2).
[260] The Bureau notes much of this precedent at 81 Fed. Reg. at 47932, n.527.
[261] Interagency Expanded Guidance for Subprime Lending Programs, 2001: "Loans to borrowers who do not demonstrate the capacity to repay the loan, as structured, from sources other than the collateral pledged are generally considered unsafe and unsound."
[262] OCC 2003 Advisory Letter on Predatory and Abusive Lending.

In the credit card context, the 2009 Credit Card Act requires that lenders "consider[] the ability of the consumer to make the required payments under the terms" of the account.[263] The purpose of this law was "to implement needed reforms and help protect consumers by prohibiting various *unfair*, misleading and deceptive practices in the credit card market."[264]

In the mortgage context, since 1994, the Home Ownership and Equity Protection Act has prohibited making high-cost HOEPA loans without regard to the borrower's repayment ability.[265] In 2009, the FRB expanded this provision to a lower cost category of loans than "high-cost" loans, called "higher priced mortgages" (essentially subprime loans). The FRB required verification of income, assets and obligations for both high-cost and higher-priced loans.[266] The 2010 Dodd-Frank Act extended an ability-to-repay requirement to all residential mortgage loans.[267]

State law also strongly supports the principle that lending without regard to ability-to-repay is unfair and abusive. Some state statutes provide that extending loans to consumers when the lender believes there is no reasonable probability of repayment in full is an "unfair" or an "unconscionable" practice, including West Virginia, Illinois, and the District of Columbia.[268]

Many courts have also found that lending without regard to ability to repay is unconscionable or a violation of state laws prohibiting unfair and deceptive practices.[269]

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[263] 15 U.S.C. § 1665e.

[264] S. Rep. No. 16, 111th Cong., 1st Sess. 2009 (May 4, 2009)(2009 WL 1260169)(Leg. Hist.) The purpose is to "establish fair and transparent practices related to the extension of credit" in the credit card market.

[265] 15 U.S.C. 1639(h): "Prohibition on extending credit without regard to payment ability of consumer. A creditor shall not engage in a pattern or practice of extending credit to consumers under [high-cost] mortgages . . . based on the consumers' collateral without regard to the consumers' repayment ability, including the consumers' current and expected income, current obligations, and employment."

[266] Federal Reserve System, Truth in Lending, Regulation Z; Final Rule, 73 Fed. Reg. 44522, 44546 (July 30, 2008).

[267] 15 U.S.C. § 1639c(a)(3).

[268] West Virginia and Indiana's statutes address "fraudulent" or "unconscionable conduct," both noting "consideration shall be given to each of the following factors, among others: (a) Belief by the creditor at the time consumer credit sales, consumer leases or consumer loans are made that there was no reasonable probability of payment in full of the obligation by the debtor." W.V. Code § 46A-7-109(3)(a); Ind. Code, §§ 24-4.5-5-102, 24-4.5-6-111(l)(3); *see also* D.C. Code § 28-3904(r)(1).

[269] In a recent case by the New Mexico Attorney General against Fast Loans, the New Mexico Supreme Court found the installment loans to be unconscionable on the basis that the lender routinely originated high-cost installment loans without inquiry into the borrower's ability to repay on its terms. CRL, *Migration*, at 5, n.49. *See also* Colorado Security Finance case discussed in section 11.4.1.5 below; *Commonwealth v. Fremont*, 897 N.E.2d 548 (2008) (Massachusetts Supreme Court affirmed a preliminary injunction against the lender based on a likelihood it had violated the state UDAP statute in the origination and servicing of mortgage loans. The court described the "central element of unfairness" found by the trial court as "the origination of a home mortgage loan that the lender should recognize at the outset the borrower is not likely to be able to repay." *Id.* at 560. The trial court in this case noted, "It is noteworthy that the issuance of such a loan is deemed to be unfair under [the state UDAP statute] even if the lender provides fair and complete disclosure of the terms of the loan and the borrower is fully informed of the risks he faces in accepting the loan. The unfairness, therefore, does not rest in deception but in the equities between the parties." *Commonwealth v. Fremont*, 23 Mass. L. Rptr., 567, 9. *See also Commonwealth v. Option One* 75 Mass.App.Ct. 1110 (2009); *Frapper v. Countrywide Home Loans, Inc.*, 645 F.3d 51 (1 Cir. 2011) (both citing *Fremont* in denying lender's motion for summary judgment on claim of violation of Mass. UDAP statute regarding ability to repay); *Gilroy v. Kasper*, 07-CV-300 JL, 2008 WL 591049 (D.N.H. Mar. 3, 2008) (survives motion to dismiss claim that borrower was made mortgage loan while lender knew she could not repay it, applying *Sperry & Hutchinson* test to New Hampshire's general UDAP law); *James v. Nat'l Financial, LLC*,

Thus, a determination that lending without making a reasonable determination that the borrower has an ability to repay is abusive and unfair is consistent with a wide range of existing credit regulation.

5.2. Ability-to-Repay Requirements Typically Apply Across the Board, and There Is No Precedent for Exempting Loans That are Primarily Made to Financially Vulnerable Consumers.

In the two other markets where federal ability-to-pay requirements apply, there are no exemptions crafted for any subset of transactions that are substantially similar to a broader class of transactions. There are also no exemptions at all for products primarily made to financially vulnerable consumers; in fact, to the contrary, precedent supports greater assurance of an ability-to-repay determination in those circumstances.

For credit cards, the ability-to-repay requirements apply to all credit cards other than home equity lines of credit or overdraft lines of credit—two entire product lines that can be reasonably distinguished from those credit cards to which the requirements apply. For mortgages, ability-to-repay requirements apply to all residential mortgage loans.[270]

Further, the Bureau's implementation of the mortgage ability-to-repay requirements support that heightened care must be taken to ensure that financially vulnerable consumers are adequately protected by ability-to-repay requirements. In that context, the Bureau refused to provide a safe harbor for compliance with ability-to-repay requirements on higher-priced Qualified Mortgage loans, even while it provided a safe harbor for lower-cost loans. Its rationale included that:

> "[T]he subprime segment of the market is comprised of borrowers who tend to be less sophisticated and who have fewer options available to them, and thus are more susceptible to being victimized by predatory lending practices. The historical performance of subprime loans bears all this out. The Bureau concludes, therefore, that *for subprime loans there is reason to impose heightened standards to protect consumers* and otherwise promote the policies of the [Dodd-Frank] statute."[271]

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132 A.3d 799 (Del. Ch. 2016) (rescinding "a one-year, non-amortizing, unsecured" loan as unconscionable under Delaware law)*; see also* NCLC, Unfair and Deceptive Acts and Practices § 6.3.2, https://library.nclc.org/udap/060302.

[270] Residential mortgage loans are closed-end, dwelling-secured mortgages. These include manufactured housing loans. They do not include open-end credit, timeshares, reverse mortgages or bridge/construction loans (all of which should have ability-to-repay requirements, but for which it is reasonable that the specific approach to the ability-to-repay determination be different). Cite. Though some aspects of the mortgage ability-to-repay rule are more prescriptive for certain categories of lenders and/or transactions, there are not blanket exemptions from an ability-to-repay determination as long as the loan is otherwise covered as a residential mortgage loan. *See* CFPB, General Comparison of Ability-to-Repay Requirements With QM Mortgages, http://files.consumerfinance.gov/f/201404_cfpb_atr-and-qm-comparison-chart.pdf.

[271] Ability-to-Repay and Qualified Mortgage Standards under the Truth in Lending Act (Regulation Z); Final Rule, 12 CFR Part 1026, 74 Fed Reg 6408, 6411 (January 30, 2013) (emphasis added; internal citations omitted).

Similarly, in the current rule, the Bureau notes in its discussion of public policies supporting ability-to-repay requirements: "These public policies show that such determinations are especially critical when subprime or high-cost credit is extended to vulnerable consumers."[272]

The Bureau should not act contrary to precedent by providing the first exemption of which we are aware from ability-to-repay requirements on a product targeted at financially vulnerable consumers.

5.3. The Widely Accepted Definition of "Ability-to-Repay"—Ability to Repay (1) While Meeting Other Obligations and Expenses and (2) Without Reborrowing—Is Critical and Should Be Explicit.

5.3.1. Overview.

The "ability-to-repay" standard, by virtually all regulatory measures, has long meant the ability to repay (1) *while meeting other obligations and expenses* and (2) *without reborrowing*. But this has not kept lenders from asserting that repayment alone evidences ability-to-repay—that is, they confound the lender's ability to collect with the consumer's ability to repay. Lenders have also asserted that repeat reborrowing, absent delinquency or default, does not evidence inability-to-repay. While the CFPB's discussion of ability-to-repay generally is consistent with our understanding, the identified unfair and abusive practice should be strengthened to make explicit the importance of ability to meet other expenses without reborrowing. In addition, in section 11 below, we urge a number of ways the rule's approach to longer-term refinancings should be strengthened to ensure consistency with this standard.

5.3.2. Precedent is clear that ability-to-repay means having the ability to repay a loan *while meeting other obligations and expenses* and *without reborrowing*.

The understanding that ability-to-repay means the ability to repay while meeting other obligations and expenses and without reborrowing is consistent with many years of regulatory precedent.

With respect to the ability to meet other obligations and expenses, HOEPA's statutory language since 1994 has required that a repayment ability include "current and expected income, *current obligations*, and employment."[273] The 2009 FRB rules required verification of income, assets *and obligations* for both high-cost and higher-priced loans.[274] Dodd-Frank, for all residential mortgages, requires "a reasonable and good faith determination based on verified and documented information,"[275] including, among other items, expected income, *current obligations, debt-to-income ratio or residual income*, and other financial resources other than the consumer's equity.[276] The Federal Reserve interpreted the CARD Act's ability-to-repay provision to require that the lender consider ability to repay "based on the consumer's income or assets and *current obligations*."[277]

[272] 81 Fed. Reg. at 48002.
[273] 15 U.S.C. § 1639(h): "Prohibition on extending credit without regard to payment ability of consumer. A creditor shall not engage in a pattern or practice of extending credit to consumers under [high-cost] mortgages . . . based on the consumers' collateral without regard to the consumers' repayment ability, including the consumers' current and expected income, current obligations, and employment."
[274] Federal Reserve System, Truth in Lending, Regulation Z; Final Rule, 73 Fed. Reg. 44522, 44546 (July 30, 2008).
[275] 15 U.S.C. § 1639c(a)(1).
[276] 15 U.S.C. § 1639c(a)(3).
[277] 12 CFR § 226.51(a).

Relatedly, regulators have typically contrasted loans made based on the value of the underlying collateral with loans made with regard to a borrower's ability to repay the loan, indicating that these practices are mutually exclusive. The 2001 Interagency Subprime Guidance describes that abusive lending practices occur when "the lender structures a loan to a borrower who has little or no ability to repay the loan from sources other than the collateral pledged."[278] As the FDIC and OCC note in their guidance addressing payday lending by banks, in the case of bank payday lending, the collateral is the customer's future deposit.[279] The OCC's 2000 letter on abusive lending practices, which is applicable to payday loans,[280] discusses collateral or equity stripping as "reliance on . . . collateral, *rather than* the borrower's independent ability to repay. . . ."[281] The OCC's 2003 letter on abusive and predatory lending does the same.[282]

With respect to the ability to repay without reborrowing, the banking regulators have long recognized that serial refinancings are an indication of disregard for a borrower's ability to repay, both generally and in the context of payday lending specifically. The HOEPA rules note that "[l]ending without regard to repayment ability . . . facilitates an abusive strategy of 'flipping' borrowers in a succession of refinancings."[283] The FDIC's 2005 payday loan guidelines describe concerns with "payday loans to individuals who do not have the ability to repay, or that may result in repeated renewals or extensions and fee payments over a relatively short span of weeks."[284] The more recent bank payday loan guidance reiterates this concern.[285]

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[278] Interagency Expanded Guidance or Subprime Lending Programs, FIL 9-2001, January 31, 2001. The FDIC's 2005 payday loan guidelines also notes that it clarifies previously issued guidance, including the 2001 Expanded Subprime Guidance; the 2001 Expanded Subprime Guidance also contemplates equity stripping outside the context of mortgage lending, noting that lenders may make a loan to a borrower who has little or no ability to repay other than from the collateral pledged, then take possession of the borrower's home or automobile upon default.

[279] OCC/FDIC Deposit Advance Guidance, *supra*.

[280] The OCC's 2000 Advisory Letter on Payday Lending states that the OCC's 2000 Advisory Letter on Abusive Lending Practices is applicable to payday lending.

[281] OCC Advisory Letter on Abusive Lending Practices, AL 2000-7 (June 25, 2000), *available at* http://www.occ.gov/static/news-issuances/memos-advisory-letters/2000/advisory-letter-2000-7.pdf (emphasis added).

[282] OCC Advisory Letter, Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices, AL 2003-2 (Feb. 21, 2003), *available at* http://www.occ.gov/static/news-issuances/news-releases/2003/nr-occ-2003-8-advisory-ltr-2003-2.pdf [hereinafter OCC 2003 Letter on Predatory and Abusive Lending Practices]: "When a loan has been made based on the foreclosure value of the collateral, rather than on a determination that the borrower has the capacity to make the scheduled payments under the terms of the loan, based on the borrower's current and expected income, current obligations, employment status, and other relevant financial resources, the lender is effectively counting on its ability to seize the borrower's equity in the collateral to satisfy the obligation and to recover the typically high fees associated with such credit."

[283] Federal Reserve System, Truth in Lending, Regulation Z; Final Rule, 73 Fed. Reg. 44522, 44542 (July 30, 2008).

[284] FDIC 2005 Payday Loan Guidelines, supra.

[285] FDIC and OCC Deposit Advance Guidance, supra.

5.3.3. The Bureau's approach is generally consistent with precedent, but the rule should explicitly identify the unfair and abusive practice as lending without a reasonable determination of ability to repay, *while meeting other expenses*, *without reborrowing*: §§ 1041.4, 1041.5(b)(1)(i), 1041.8, 1041.9(b)(1)(i).

The Bureau's general approach to this rule and its related discussion indicates that the Bureau's view, also, is that ability to repay means ability to repay while meeting income and expenses and without reborrowing. The Bureau notes: "'ability to repay' in this context means that the consumer has the ability to repay the loan *without reborrowing* and while meeting the consumer's major financial obligations and basic living expenses."[286]

But outside of the discussion, the rule suggests but does not directly state the "without reborrowing" aspect of ability to repay. Proposed § 1041.4 and § 1041.8, which identify the unfair and abusive practices, state merely: "It is an abusive and unfair practice for a lender to make a covered [short-term or longer-term] loan without reasonably determining that the consumer will have the ability to repay the loan."[287] Neither provision is accompanied by Commentary.

Subsequent provisions prohibit lenders from making loans unless the lender first makes a reasonable determination that "the consumer will have the ability to repay the loan according to its terms."[288] The phrase "according to its terms" implicitly requires the borrower to be able to repay the loan *without refinancing.* A Comment states that this means that the consumer must be able to "make all payments under the loan and to meet basic living expenses during the term of the loan." [289] Another Comment explains that this standard must be met without any "implicit assumption that the consumer will obtain additional consumer credit . . . ."[290] That Comment is helpful, but it only goes to the lender's assumptions, not the consumer's behavior and ability.

Other Comments indicate that a lender's reborrowing rates may be relevant to assessment of whether a lender's ability-to-repay determinations are reasonable. That, too, is helpful,[291] but it is not part of any rule or requirement.

The Bureau's proposed ability-to-repay requirements appropriately require consideration of obligations and expenses. Those requirements and additional provisions are also aimed at ensuring ability to repay without reborrowing; for example, residual income must include a cushion sufficient to cover income and expense volatility, and provisions addressing loan flipping are provided for both short- and longer-term loans. A focus on ability-to-repay without reborrowing is necessary in light of the harm caused by reborrowing; we discuss these concerns more fully in sections 8 and 11 addressing short-term and long-term loan flipping.

The CFPB should make explicit in the regulatory language the generally accepted standard for what ability-to-repay means: ability to repay while meeting other expenses without reborrowing. The CFPB

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[286] 81 Fed. Reg. at 47924, 47933 (emphasis added).
[287] Proposed §§ 1041.4 & 1041.8.
[288] Proposed §§ 1041.5(b)(1)(i), 1041.9(b)(1)(i).
[289] Proposed Comment 5(b)-1 (emphasis added); proposed Comment 9(b)-1.
[290] Proposed Comment 5(b)-2.ii.A; proposed Comment 9(b)-2.ii.A.
[291] As discussed in section 6.2.5.2, we have serious concerns about the standard of comparison being other high-cost lenders.

should then, as discussed throughout the remainder of these comments, ensure that standard is applied consistently throughout the rule.

Thus, in all four places in the rule where the phrase “ability to repay” is used to describe unfair, abusive or prohibited practices—§§ 1041.4, 1041.5(b)(1)(i), 1041.8, 1041.9(b)(1)(i)—the phrase should be replaced with:

> “ability to repay the loan according to its terms *while meeting debt obligations and expenses and without reborrowing*.”

Alternatively, but less preferable, the CFPB could add comments to those four provisions explaining this interpretation of the phrase “ability to repay.”

Including the standard explicitly in the rule will help emphasize to lenders the obligation to ensure ability to repay without reborrowing. It will also help to support compliance with and enforcement of the rule. The CFPB will be in a stronger position to use evidence of high reborrowing rates as part of an assessment of a lender’s ability-to-repay assessments if the rule itself clearly sets out the full standard.

5.4. The Bureau’s Determination of “Abusive” Is Appropriate and Abundantly Supported: § 1041.4.

The Bureau provides a detailed discussion of its preliminary application of the “abusive” standard at pages 47933-36 of the proposed rule. We generally agree with the details presented there as well as the Bureau’s conclusions, and we do not reiterate them here. Instead, we offer only a few points of emphasis below, particularly with respect to how the Bureau’s findings here should support strengthening certain aspects of the Bureau’s proposal, addressed in more detail throughout our comments.

With respect to the costs and risks of these products, we reference section 2.2 above, summarizing the extended cycle of debt generated by both short- and longer-term loans, and discussing the harms associated with default and making unaffordable payments.

As the Bureau notes, Dodd-Frank provides that an abusive practice is one that *takes unreasonable advantage* of (1) a lack of understanding on the part of the consumer of material risks, costs, or conditions of the product or service, or (2) the inability of the consumer to protect the interests of the consumer in selecting or using a product or service.

5.4.1. Lack of understanding.

We support and highlight the Bureau’s conclusion that a “generalized understanding” of a debt with a due date does not suffice to establish that consumers understand the material costs and risks of these products.[292] We emphasize that, for longer-term loans, borrowers likely have the reasonable expectation that payments will reduce principal within a reasonable time. Some may anticipate being able to pay off a high-cost loan early (using a tax refund or year-end bonus) without realizing that they may still owe nearly the entire debt even after making many payments. See our discussion of longer-term refinancings below at section 11.

[292] 81 Fed. Reg. at 47933.

We further emphasize the Bureau's discussion of the well-established realities of tunneling (focusing on the present more than the future, particularly by those with immediate needs) and optimism bias as contributing to the likelihood that consumers do not understand the material costs and risks.

Finally, we offer the additional observation that consumers are unlikely to understand the costs and risks associated with these products *simply because they are so severe.* It would be entirely reasonable for consumers to believe that any practice capable of inflicting such severe financial harm would be illegal.

5.4.2. Inability of consumer to protect consumer's interests.

We concur with the Bureau's interpretation of the abusive standard, including that (1) even in circumstances where consumers understand material risk and costs, they may not be able to protect their own interests, and (2) that this is particularly true when they are in a financially vulnerable position.[293]

5.4.3. Practice takes unreasonable advantage of consumer vulnerabilities.

As the Bureau notes, Dodd-Frank has delegated to the Bureau the responsibility for determining when a practice is taking "unreasonable advantage" of a consumer. And we do not disagree with the observation that, in a market economy, market participants can be expected to take advantage of their superior knowledge or bargaining power.[294] We also agree that there comes a point at which a line is crossed, and conduct in leveraging that knowledge or power becomes unreasonable taking advantage.[295]

As the Bureau notes, determining when that line is crossed is best done taking into account all the relevant facts and circumstances of the practice in question.[296] We note again the strong regulatory precedent that supports finding that lending without ability to repay is abusive. We particularly emphasize the Bureau's findings that the vulnerability of consumers who are likely to seek covered loans is relevant to this inquiry, and that lenders further *exacerbate* the risks and costs *inherent* in these loans with their practices. The Bureau notes that storefront lenders, in particular, encourage long loan sequences.[297] We emphasize that, in both the short-term and longer-term markets, regardless of origination channel, refinancing rates are extremely high, due to some combination of product design and lender practices that encourage ongoing indebtedness.

We highlight, as well, this powerful finding:

> "*Lenders also know that the defining loan features will enable the lender to extract payment from the consumer even if the payment exceeds the consumer's ability to repay and leaves her*

[293] 81 Fed. Reg. at 47934.
[294] 81 Fed. Reg. at 47935.
[295] *Id.*
[296] *Id.*
[297] 81 Fed. Reg. at 47936.

in financial distress, but consumers do not understand the likelihood or severity of the harms they will suffer in that scenario."[298]

We recommend that the rule reflect this finding more fully, particularly by limiting lender discretion in the ability-to-repay determination; eliminating exemptions from ability-to-repay requirements; and recognizing a broader range of longer-term refinancings as abusive.

5.5. The Bureau's Determination of "Unfair" is Appropriate and Abundantly Supported: § 1041.4.

The Bureau provides a detailed discussion of its preliminary application of the "unfair" standard at pages 47936-40 of the proposed rule. Again, we do not reiterate the details or conclusions here.

We likewise generally agree with the Bureau's preliminary application of the "unfairness" standard as well as its conclusions, with one significant exception. We object to the notion that if a borrower were hypothetically able to accurately predict the length of a relatively short loan sequence, or the harm from a longer-term loan, the injury would be reasonably avoidable. This conclusion is unfounded, and in the substantial body of "unfairness" precedent the Bureau references,[299] we are not aware of analogous reasoning. We urge the Bureau to strike this unnecessary and unhelpful caveat, as it risks undermining not only the current rule, but also the unfairness standard going forward.

With respect to the substantial harm caused by the practices in question, we again reference section 2.2 above, summarizing the extended cycle of debt generated by both short- and longer-term loans, and discussing the harms associated with default and making unaffordable payments.

5.5.1. Substantial injury.

We support the Bureau's finding that lending without a reasonable ability-to-repay determination "causes or is likely to cause *both* [injuries]—a substantial number of consumers suffer a high degree of harm, and a large number of consumers suffer a lower but still meaningful degree of harm."[300] We reference the earlier discussion at 2.2 for the Bureau's categorization of harms, which the Bureau appropriately uses to support this prong of the unfairness test.

We underscore the following findings from the Bureau's discussion of the substantial injury prong for longer-term loans:

- "[E]ven consumers who are able to make all of their payments on a payday installment or vehicle title installment loan can suffer substantial injury" resulting from the lack of an ability-to-repay determination.[301]

- "Indeed . . . the lender *is likely to* receive payment even when that leaves the consumer with insufficient funds to meet other obligations and expenses. At a minimum . . . the consumer

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[298] 81 Fed. Reg. at 47997 (emphasis added).
[299] 81 Fed. Reg. at 47936, n.534.
[300] 81 Fed. Reg. at 47936 (emphasis added).
[301] 81 Fed. Reg. at 47997.

loses control over her finances, including the ability to prioritize payments of her obligations and expenses based on the timing of her receipts of income."[302]

- "Such consequences could occur prior to default – if the lender for a time was able to extract unaffordable payments from the consumer's account – or could occur in lieu of a default, if the lender is able to consistently extract payments that are not affordable."[303] Further, the Bureau notes that the payment may be made even when the account lacks sufficient funds, through overdraft.[304]

- "[A]n imminent unaffordable" loan payment may bring about a refinance or reborrowing, which, the Bureau states, is especially likely to be caused by a balloon payment.[305] But the Bureau proceeds to discuss a dynamic that is in no way limited to balloon payments. It notes the injury caused when refinancings and reborrowing add "dramatically" to the total cost of credit when the prior payments did little if anything to amortize principal.[306] It notes this in the context of interest-only payments preceding the balloon. But many other high-cost longer-term loans have payments, particularly early in the loan term, that make very little progress toward principle. And certainly even when the looming payment is not a balloon payment, it can trigger the need to refinance.

These are all important findings reflecting the very essence of the business model. Again, we fear that these findings are not consistently given due weight, particularly with respect to longer-term refinancings.

5.5.2. Injury not reasonably avoidable.

We support the general analysis of this prong but note the following troubling footnote:

> "It appears that some consumers are able to accurately predict that they will need to reborrow one or two times, but decide to take the loan regardless of the additional cost of one or two additional loans. Accordingly, such costs do not count as substantial injury that is not reasonably avoidable."[307]

The Bureau makes similar points in the countervailing benefits prong that follows. With respect to short-term loans, it notes that "[f]or consumers who accurately predict their reborrowing, the Bureau is not counting their reborrowing as substantial injury that should be placed on the 'injury' side of the countervailing benefits scale."[308] For longer-term loans, the Bureau notes that it "would not count for purposes of substantial injury the default costs of individual consumers who fully recognized the risks of [longer-term loans] and decided that the temporary reprieves were worth the downstream costs, but the Bureau believes there are few such consumers."[309]

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[302] 81 Fed. Reg. at 47997-98 (emphasis added).
[303] 81 Fed. Reg. at 47998.
[304] *Id.*
[305] *Id.*
[306] *Id*.
[307] 81 Fed. Reg. at 47937, n.537.
[308] 81 Fed. Reg. at 47939.
[309] 81 Fed. Reg. at 48001, n.685.

The Bureau's own findings throughout this rulemaking suggest two problems with this reasoning. First, the Bureau also notes in its discussion of this prong that the FTC and other agencies have focused on the vulnerability of affected consumers and their perception of the availability of other products when applying this prong of the unfairness test.[310] Through this appropriate lens, expecting to be in a series of two or three loans does not mean that a vulnerable borrower can reasonably avoid injury from the—by definition—unaffordable rolled over loans. Indeed, in the subprime credit card rule, for example, the three promulgating agencies did not exclude from their analysis of "injury" some subset of instances when borrowers accurately predicted the cost of the card.[311]

The Bureau's analysis of this issue appears to confound deception with unfairness. There may be unfairness even if a consumer is not deceived. An injury may not be reasonably avoidable even if it is predictable.

Second, the research the Bureau cites found only that some borrowers accurately predicted the length of their series. It does not establish that the borrowers accurately predicted the collateral harms that may have been caused by unaffordable loan payments, or that they could reasonably avoid those harms. In the following prong—whether injury is outweighed by benefits or competition—the Bureau clearly acknowledges this collateral harm. The Bureau notes that even consumers whose short-term loans become short-to-medium-length loan sequences incur injury ranging from modest to severe: The injury includes, among other things, "the extent to which the consumer incurred collateral harms from making unaffordable payments."[312] The Bureau continues, saying some may experience injury from repaying a loan but not being able to meet other obligations and expenses.[313] And yet, even if borrowers *had* predicted the collateral harms, the ability to predict harm does not equate with the ability to reasonably avoid it. We are not aware that it ever has, and this rule should not change that.

Finally, we observe that the evidence of injury is so overwhelming that unfairness is clear even without considering the injuries to consumers who purportedly can predict the harm. However, it is important that the Bureau not create precedent that so-called predictable injuries may in other cases be an appropriate consideration in evaluating unfairness.

5.5.3. Injury not outweighed by benefits to consumers or competition.

In its application of this prong to consumers for short-term loans, the Bureau groups borrowers into three groups—those who repay without reborrowing, those who eventually default, and those who reborrow. The Bureau concludes that for those who default and those who reborrow, the costs of lending without regard to their ability to repay "dwarfs" any benefits they may receive.[314] The evidence of harm from default and reborrowing (see section 2.2, above) clearly warrants this conclusion.

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[310] 81 Fed. Reg. at 47937, n.538.
[311] 74 Fed. Reg. 5503. The Federal Reserve noted: "Accordingly, the test [for reasonably avoidable] is not whether the consumer could have made a wiser decision but whether an act or practice unreasonably creates or takes advantage of an obstacle to the consumer's ability to make that decision freely" (citing the FTC Credit Practices Rule).
[312] 81 Fed. Reg. at 47938.
[313] *Id.*
[314] 81 Fed. Reg. at 47939.

We highlight the Bureau's observation here that some repayers may not be able to afford the loan but "choose" to repay it anyway, which may result in other costs, like a late fee on a utility bill.[315] We would add among costs here overdraft fees incurred when the account lacked sufficient funds. We would also suggest that this repayment—essentially extraction of the borrower's funds on payday—is likely not best described as the borrower's "choice." Finally, some consumers may cover the repayment of a loan from some other source, which also has costs.

With respect to this prong for longer-term loans, the Bureau divides borrowers into only two groups, repayers and defaulters. It includes within repayers those who "find it necessary to reborrow," "most notably" related to a balloon payment, a categorization we find curious. The Bureau notes that 62% of payday installment loan borrowers and 69% of vehicle title borrowers qualify as "repayers," and that it believes most of these borrowers would be able to meet an ability-to-repay determination and thus would not be significantly impacted by the proposed ability-to-repay requirements.[316]

First, we are surprised the Bureau would not assess repayers who do not refinance separately from borrowers who refinance, especially those who refinance repeatedly. In addition, as discussed at greater length in sections 8 and 11, a meaningful ability-to-repay standard must focus on ability-to-repay *without reborrowing*.

We are also surprised at the Bureau's finding that most of these repayments would be expected to meet ability-to-repay determinations under the proposal. The CFPB's findings in the "substantial injury" prong illustrate clearly why repayment of a loan secured by a leveraged payment mechanism does not equal affordability. We do appreciate the observation that "some current repayers may not actually be able to afford payments" under current loans but end up repaying it nonetheless.[317] And we would expect that, as a result, more borrowers who currently repay longer-term loans would not in fact be reasonably deemed to have the ability-to-repay those loans.

With respect to defaulters, the Bureau again notes that while a loan may provide a "temporary reprieve," this "reprieve" is "illusory and actually detrimental" compared to a system in which lenders made loans consumers can afford.

With respect to competition, the Bureau concludes that the rule should not reduce the competitiveness in a market that already generally lacks meaningful price competition;[318] we agree.

5.5.4. Consideration of public policy.

The Bureau appropriately gives weight to the considerable public policy supporting a finding that lending without regard to ability-to-repay is unfair. The Bureau cites numerous examples of consumer financial statutes, regulations, and guidance that require or recommend an ability-to-repay determination,[319] including state legislation. (See also section 5.1 above for discussion of several examples.)

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[315] *Id.*
[316] 81 Fed. Reg. at 47999-48000.
[317] 81 Fed. Reg. at 48000.
[318] 81 Fed. Reg. at 48001.
[319] 81 Fed. Reg. at 47940.

We note here that in § 1041.7, .11, and .12, establishing the exemptions from ability-to-repay, the Bureau cites no relevant precedent for these exemptions. In fact, the Bureau notes here, to the contrary: "These public policies show that such determinations are especially critical when subprime or high-cost credit is extended to vulnerable consumers."[320]

6. THE ABILITY-TO-REPAY DETERMINATION REQUIREMENTS MUST BE SIGNIFICANTLY STRENGTHENED: § 1041.5 and § 1041.9.

6.1. Overview.

Sections 1041.5 and 1041.9 prohibit a covered (non-exempted) loan unless the lender has made reasonable determination of the borrower's ability to repay and set out the requirements related thereto. The rules and Commentary are largely identical except that § 1041.9 includes additional requirements related to longer-term loans. We discuss the requirements and considerations unique to longer-term loans at section 10 below, while discussing the common elements here. We also address the few elements unique to short-loans here, at sections 6.3.2 and 6.3.3.

We appreciate that the task before the Bureau in designing an ability-to-repay test for payday and vehicle title loans is not an easy one. We strongly support certain elements of the test. But we are concerned about a few significant proposed elements that we fear lenders will exploit on their way to, in important respects, continuing business as usual.

We evaluate the proposed ability-to-repay test in light of three key factors, among others: (1) virtually every loan covered by this rule is a high-risk loan with extraordinary potential to inflict substantial harm on consumers; (2) lenders lack the incentive to determine ability-to-repay in light of a borrower's other obligations and expenses, given that their super-lien position and high costs will persist under the rule; and (3) many covered lenders have always relentlessly trapped borrowers in unaffordable debt and evaded laws designed to stop them from doing so.

Put another way, the rule should approach lenders' interest in making genuinely affordable loans, which allow borrowers to meet other obligations and expenses, with great caution. Covered lenders cannot be given the discretion or flexibility that might be appropriate in other regulations.

Relatedly, we expect that lenders will routinely manipulate any provision permitting reliance on borrower self-certification or borrower statements in their efforts to make unaffordable loans. Indeed, the Bureau notes: "Lenders have an incentive to encourage . . . misestimates to the extent that as a result consumers find it necessary to reborrow."[321] So we oppose, under any circumstances, permitting such certifications or statements to result in projections of higher income, or lower obligations or expenses, than reliable third-party evidence supports.

With that context, we summarize our feedback and recommendations here, which we discuss in further detail below:

[320] 81 Fed. Reg. at 48002.
[321] 81 Fed. Reg. at 47952.

We strongly support the requirement that income and major financial obligations be verified using verification evidence. Departures from verification evidence should not be permitted except, in very rare circumstances, with other reliable third-party evidence—not consumer statements (section 6.4).

Major financial obligations should generally include payments due on delinquent debt that appears on the credit report or registered information system (RIS) unless there has been no activity for at least 365 days (section 6.2.2). Claims that a consumer has only partial responsibility for joint obligations, other than for rental housing, should be permitted only with verification evidence (section 6.4.2).

With respect to rental housing (section 6.4.4.3.2):

- We urge that rental housing generally be required to be verified using verification evidence. In the limited circumstances when verification evidence is not available, the greater of a reliable locality-based proxy or borrower statement should be used.
- To assume shared housing, lenders must obtain verification evidence or other reliable third party evidence of the shared arrangement. In addition, supervision guardrails should be established to protect against an unreasonable volume of shared housing circumstances in a lender's portfolio.
- At the very least, on any loan where there is a presumption of inability to repay, and on a second refinance of a longer-term loan (as discussed in 11), verification evidence of rental housing should be required. Shared housing in these scenarios should be the greater of that indicated by reliable third-party evidence or a reliable locality-based estimate.

Basic living expenses should be defined much more broadly, beyond strictly "necessary" expenses, to include "typical" household expenses based on income, location, and household size. Again here, borrower certification should not be used to assume a smaller household size than reliable evidence supports.

The examples of "reasonable methods" for projecting basic living expenses should be strengthened (section 6.3.8):

- With respect to a statistical survey approach, use of a well-researched government survey is the preferable approach.
- Analysis of checking account activity should be included more explicitly as a "reasonable method" and encouraged.
- Projections based on statistical data other than government data or "other reliable methods" should be subject to heightened scrutiny. The method much actually predict expenses, not just collection success.

The examples of "unreasonable methods" must be strengthened (section 6.3.9). They must *not*:

- set the bar too low;
- suggest that a flat percentage of income approach is appropriate, no matter how low the family's income or how large the household; or
- provide that the reasonableness of an expense projection can be determined by comparing loan performance to that of similar lenders making loans to similarly situated consumers.

Lenders' expense estimates should be reported to the Bureau, and lenders who routinely project lower expenses than research would support should face close scrutiny.

Lenders should be explicitly required to take into consideration information on the credit report and RIS report that sheds light on the consumer's ability to make the loan payment on top of other debt obligations and basic living expenses. This includes delinquencies or defaults on covered loans, other debt obligations, or basic living expenses within the past year (section 6.3.5).

A pattern of reborrowing is information known to the lender that should require consideration (section 6.3.4).

We strongly oppose permitting evidence of whether determinations of ability-to-repay are reasonable to include the extent to which delinquency, defaults, and reborrowing rates are low, equal to, or high, including in comparison to the rates of other lenders making covered loans to similarly situated consumers. We discuss this issue in a separate section, 7.5 , urging that these rates be required to be low in the absolute.

Short-term open-end loans are exclusively, or nearly exclusively, evasion products and should be regulated as such. Each advance on a short-term open-end loan should be treated as a new loan subject to its own ability-to-repay determination (section 6.3.2).

6.2. Certain Definitions of the Components of the Determination Should be Modified: §1041.5(a) and § 1041.9(a).

We support the definition of "net income." We have some concerns about the narrowness of "major financial obligations," including its omission of payments on older delinquent debt, and substantial concerns about the narrowness of "basic living expenses."

6.2.1. "Net income" definition is appropriate: § 1041.5(a)(4).

We support the Bureau's proposed definition of "net income" as essentially take-home pay (gross income net of taxes and all other deductions from net pay, including voluntary deductions). Any other approach would allow for the unsound assumption that borrowers have access in the short-run to funds currently deducted from their gross pay.

6.2.2. "Major financial obligations" definition presents some concerns: § 1041.5(a)(2).

Section 1041.5(a)(2) defines "major financial obligations" as "a consumer's housing expense, minimum payments and any delinquent amounts due under debt obligations (including outstanding covered loans), and court- or government agency-ordered child support obligations." The Bureau's rationale is based in part on its observation that these costs can be a significant portion of the consumer's income, and that the consumer has little or no ability to change these costs in the short-run.[322]

The Bureau solicits comment on whether there are additional costs that are "typically recurring, significant, and not changeable," like alimony,[323] daycare, health insurance premiums, unavoidable

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[322] The Bureau also notes that these are roughly analogous to the costs included in the debt portion of the mortgage debt-to-income ratio under the Bureau's mortgage rules.

[323] The Bureau also notes that it has excluded alimony from major obligations since the SBREFA proposal in part because few borrowers have this obligation.

medical expenses, or other costs for which a consumer is legally obligated, like contractual telecom services, that should be included.[324]

We are concerned that the Bureau's current approach—when considering "major financial obligations" and "basic living expenses" combined—may result in the exclusion of significant costs that many borrowers are likely to have, particularly childcare, health insurance premiums (not deducted from net pay), medical expenses, and telecom services. We recognize, though, that the Bureau's approach to major financial obligations is to generally require verification of all obligations via the credit report, and these costs will not typically show up on a credit report. We also, as mentioned, have no confidence lenders will obtain and use accurate borrower certifications as to the presence of these costs. Thus, we recommend these shortfalls be addressed by significantly strengthening the approach to projecting basic living expenses. Please see further discussion of related issues under the definition of "basic living expenses" at section 6.2.3 and the proposed reasonable and unreasonable methods of projecting them at sections 6.3.8 and 6.3.9.

The Bureau also solicits comment on the treatment of delinquent amounts, including the practicality of asking consumers about them, comparing stated amounts to amounts in verification evidence, and accounting for these amounts. We recommend that the consideration of delinquent obligations be expanded.

With respect to delinquent amounts, the definition of "major financial obligations" includes "minimum payments and any delinquent amounts due under debt obligations (including outstanding covered loans)." We first note some lack of clarity regarding the extent to which the Bureau intends delinquent obligations on non-covered loans that would not be deemed "outstanding loans" under the proposal (because they have not been paid on for over 180 days) to be included as payments on major financial obligations. We think delinquent amounts due on those loans may be included because they are not excluded from the definition above, but clarification would be helpful (see section 3.7 above). The proposal does appear to exclude payments on covered loans that have not been paid on for over 180 days, by virtue of its definition of "outstanding loan."

In a determination of ability-to-repay, delinquent credit is relevant in two ways. It is relevant to the borrower's current and future debt load. And it is relevant as a warning sign of distress and an indicator of the borrower's capacity to repay new debt. We fear the Bureau's approach to delinquent debt will result in undervaluing its relevance in both of these assessments.

The Bureau notes that 180 days is the point at which the Federal Financial Institutions Examination Council (FFIEC) generally requires depositories to charge off open-end credit (and at 120 days for closed-end). But the charge-off point may be the very point at which a collection action has been filed against the consumer or the debt has been sold to debt buyers that have begun aggressive debt collection efforts. These efforts to collect unaffordable charged-off debt may be the very reason that the consumer is seeking a new loan. While there may come a point where the past should be forgotten, six months is not the far distant past. Under the FCRA, for example, delinquent debt can remain relevant and reported for seven years after the last payment.

[324] As the Bureau notes here, in SBREFA, it noted an additional approach under consideration whereby major financial obligations would also include utility payments, "regular medical expenses," and potentially others.

In addition, the consumer's ability to repay other debt within some period longer than six months is relevant to whether the consumer can repay a new loan. If a consumer was unable to repay a loan taken out six months ago—and still is unable to resolve that debt—it is not prudent to a rule that explicitly permits the lender to disregard that fact. In reality, there is little to reason to expect that the situation of a consumer, statistically likely to be financially distressed, is likely to have improved markedly in the last six months since defaulting on a loan; more likely, it has deteriorated. (See our related recommendation that lenders be required to consider credit report information at section 6.3.5.)

The Bureau solicits comment on the length of the time period; whether a loan should still be considered an outstanding loan if charged off by the lender prior to 180 days of delinquency; whether a loan should be considered outstanding if there has been activity on the loan (like collections activity) within the previous 180 days regardless of whether the consumer has made a payment on the loan; and whether a loan should be considered an outstanding loan if there has been activity on a loan more than 180 days after the consumer has made a payment (such as collections lawsuit), which would seem to result in a loan changing status from not outstanding to outstanding.

We recommend the following modification to the definition of "outstanding loan" to mitigate the risk that the ability-to-repay determination could disregard relevant unaffordable obligation:

1. Modify the definition to exclude only loans with both no payment *and* no debt collection activity over the course of the established time period.
2. For loans from a different lender: Use a period of 365 days.
3. For loans from the same lender:
    a. If the loan has not been written off or sold to a debt buyer, include the loan regardless of how much time has passed.
    b. If the loan has been written off and is no longer being collected by the lender, or has been sold to a debt buyer, use a period of 365 days following the last collection attempt.

    Using 365 days rather than 180 for same-lender loans is consistent with the Bureau's concerns that lenders will exploit a cut-off point in an attempt to encourage new borrowing or revive collections activity.
4. Require that lenders report collections activity to the RISs, as noted in section 14.4 below (for debt buyers, we urge the Bureau to include this requirement in its proposed debt collection rules).

(In addition, as discussed in section 11.4.2.2, we urge that loans that are repaid early be deemed to be "outstanding" for 30 days in order to prevent evasions. In that section we also urge also that lenders be prohibited from refinancing their own defaulted loans even if the loans no longer meet the definition of "outstanding.")

The Bureau also solicits comment on the treatment of joint obligations—major costs such as rent or credit cards that consumers may share with other members of the household. We address this in the context of §1041.5(c)(1) at section 6.4.2 below.

6.2.3. "Basic living expenses" should be defined much more broadly: § 1041.5(a)(1).

The proposal limits the definition of basic living expenses to expenditures, other than payments for major financial obligations, "necessary to maintain the consumer's health, welfare, and the ability to produce income, and the health and welfare of members of the consumer's household who are financially dependent on the consumer." The Bureau acknowledges that its current approach leaves ambiguity with respect to both the types and amounts of expenses that are "'necessary" for the stated purposes and solicits comment on whether it should instead use the following definition it considered but did not propose: expenses "likely to recur through the term of the loan and in amounts below which a consumer cannot realistically reduce them."[325]

Instead of a narrow focus on expenses that are "necessary," we urge instead that "basic living expenses" be defined as either (1) the proposed definition *plus* expenses likely to recur through the term (with *no* qualification that expenses be "necessary" or that consumers not be able to "realistically reduce" them), or, (2) a potentially simpler approach: "typical expenses" based on geography, income, and household size. We also urge more specific examples in the Comments.

The proposed definition is far too narrow. The Bureau notes that its proposed definition is a principles-based one, and it does not provide a comprehensive list of what the definition includes. But we are concerned that the few examples the CFPB provides could be taken as an exhaustive list. The Bureau provides the following examples in the Commentary: food and utilities, transportation to and from work, and childcare. In the discussion of a cushion on longer-term loans, it suggests that medical costs must be considered for consumers who do not have health insurance (yet medical costs should be included even if they do have health insurance).[326] We have found no other examples of basic living expenses in the rule or discussion.

The rule may invite lenders to take the narrowest possible approach, leaving enough income only for a few narrow categories of expenses and ignoring the realistic everyday life of struggling families. Yet certainly most if not all transportation, and not just work-related transportation, is necessary to carry on one's daily affairs. The Bureau notes that it considered including cell phone costs as "major financial obligations" but has not. These should be considered, at a minimum, expenses included in the ability-to-repay determination, but it is by no means clear that they are under the proposal. Similarly, it is not clear where health insurance premiums not deducted from a borrower's net pay are accounted for. Even clothing is not listed.

Thus, we urge the Bureau expand the definition to include what it deems "basic living expenses," plus expenses "likely to recur" throughout the loan term. A similar simplified approach would be "typical expenses," based on geography, income, and household size. Even under the best and most predictable circumstances, everyone has expenses that may not be considered "necessary" by the Bureau's proposed definition but that are "likely to recur" or "typical." The Commentary should provide a very broad, but non-exhaustive, list of examples of "typical expenses. We note that the Bureau of Labor Statistics publish data on what households typically spend. And borrower certification should not be used to assume smaller household size than reliable evidence supports.

We strongly oppose inclusion of a requirement that the consumer be unable to "realistically reduce" the expenses. This will invite lenders to employ a "thrifty household" standard and result in the exclusion of significant necessary and typical expenses. The Bureau suggests that borrowers have some

[325] 81 Fed. Reg. at 48005.
[326] 81 Fed. Reg. at 48013.

ability to reduce basic living expenses—even necessary ones—noting that borrowers have "somewhat greater ability" to reduce basic living expenses (than major financial obligations) in the short-run by, for example, ride-sharing.[327] But we dispute an assumption that lower-income, financially strapped borrowers will be able to reduce their basic living expenses in the short-run. The U.S. Financial Diaries project, for example, which finds high volatility in both income and expenses, finds that income dips are not correlated with expenses dips, strongly suggesting that borrowers, already financially strapped, typically cannot significantly reduce their expenses at will.[328] Further, the generally lower-income, credit-impaired consumers who take out covered loans have already faced challenges making ends meet. If they do have simple ways of reducing their expenses, they likely have done so already, before reaching the point of seeking a covered loan.

The Bureau also solicits comment on whether there are standards in other contexts that could be relied upon, citing, in particular, the IRS standard for delinquent tax liability and bankruptcy courts' standards for bankruptcy-related repayment plans. We note generally that while government data can be helpful in providing estimated dollar figures for what households typically spend (as noted in section 6.3.8), caution should be exercised to ensure that the expenses lenders include for borrowers are not limited to overly narrow "necessary" or "essential" categories.

6.2.4. "Payment" under a short-term loan is appropriately broad: § 1041.5(a)(5).

Section 1041.5(a)(5) defines the payment under a short-term loan. We support the proposal to include all amounts payable regardless whether to a lender or third party, including "voluntary" insurance or memberships.[329] (See discussion of "total cost of credit" definition at section 3.9 supporting inclusion of such costs as appropriate.) For open-end credit, the provision further requires that the payment be calculated assuming that (1) the consumer utilizes the full amount of credit as soon as available; and (2) the consumer makes only the minimum payments under the short-term loan. We support both provisions. Assuming full utilization of the line provides the most assurance that the borrower does not receive credit that she does not have the ability to repay. Assuming the minimum payments is also an appropriate approach that we note will often require underwriting to a balloon payment due within 45 days.

6.3. A Reasonable Determination of Ability-to-Repay Must Reduce Lender Discretion and Prohibit All Unverified Inputs That Would Increase Residual Income: § 1041.5(b) and § 1041.9(b).

6.3.1. Overview.

Critical to the success of this rulemaking are the rules and guidelines the Bureau provides as to what constitutes a "reasonable" ability-to-repay determination. Ability to repay must be evaluated both at

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[327] The Bureau further offers that assertion to support not proposing to prescribe a particular method for estimated basic living expenses; see further discussion in the "reasonable determination" at section 6.3 below.
[328] Morduch, Jonathan and Anthony Hannagan. 2015. *Income Gains and Month-to-Month Income Volatility: household evidence from the US Financial Diaries*. US Financial Diaries Project. https://www.stlouisfed.org/~/media/Files/PDFs/Community%20Development/Econ%20Mobility/Sessions/MorduchPaper508.pdf.

[329] See high attachment rates discussed at n.173.

the front-end (when considering an individual consumer's application) and, at the portfolio level on the back-end (reviewing evidence that significant numbers of consumers are struggling to repay). We have significant concerns about this provision and several recommendations to strengthen it.

Sections 1041.5(b)(1)(i) and 1041.9(b)(1)(i) provide that a lender not make a loan, or increase credit available on a line of credit, unless the lender first makes a reasonable determination that the consumer will have the ability to repay the loan. Section 1041.5(b)(1)(ii) provides requirements specific to short-term open-end lines of credit. Section 1041.5(b)(2)(ii) requires that a lender assess whether the borrower will be able to meet obligations and expenses for 30 days following the highest payment due under the loan.

The Commentary provides standards for evaluating whether the ability-to-repay determination is reasonable. To be reasonable, it must (A) include the specific determinations required by the rule; (B) be based on reasonable projections of net income and major financial obligations; (C) be based on reasonable estimates of basic living expenses; (D) be grounded in reasonable inferences and conclusions based on the information the lender is required to obtain or consider; and (E) appropriately account for information known by the lender, whether or not the lender is required to obtain it. In addition, for longer-term loans, the lender must (F) appropriately account for the possibility of volatility in the consumers income or expenses during a term of the loan; we discuss this separately at section 10.

We discuss each of these elements in turn. We generally follow the sequencing of the proposed regulations and Commentary. Thus, even while reasonable projections of net income and major financial obligations (including housing rental expense) are required under § 1041.5(b), they are not discussed until 1041.5(c), so our own discussion of those processes is not addressed until the following section.

6.3.2. The requirement for a reasonable ability-to-repay determination is appropriate but it must be stronger for open-end loans: § 1041.5(b)(1)(i) and (ii).

We strongly support proposed § 1041.5(b)(1)(i), which requires lenders to make a reasonable determination that a consumer has the ability to repay a loan according to its terms, for the reasons discussed in section 5 above. As discussed in that section, we urge the Bureau to add "while meeting expenses without reborrowing" to that provision.

We are concerned, however, that as applied to open-end loans, the requirement is far too weak, as discussed below. Short-term open-end loans are products typically designed to evade some aspect of law that applies to closed-end but not open-end credit. They should be treated as such under this rule, and every advance on an open-end loan should be treated as a closed-end loan.

6.3.2.1. Short-term open-end loans are high-risk evasion products.

Short-term open-end loans are rare products that have, to date, been used primarily to skirt stricter laws applicable to closed-end products. The very nature of an open-end product—whereby a lender offers a replenishable credit line that is used in varying amounts for repeat transactions—does not lend itself to full repayment due in less than 45 days. These products are rare in the market today, and where lenders do make these loans, it is to evade state provisions aimed at closed-end loans.

The most prevalent purportedly open-end short-term loan that we have known was the "deposit advance" bank payday loan product.[330] The open-end structure enabled it to avoid coverage under the original Military Lending Act regulations, which covered only closed-end payday loans. As with other fee-based open-end products, deposit advance products also exploited loopholes in Regulation Z and avoided disclosure of the triple-digit APR they carried. As discussed in section 10.6.1 below, there are a variety of protections that lenders evade by structuring their loans as open-end.

Open-end credit requires a plan that:

- reasonably contemplates repeated transactions;
- imposes a finance charge computed from time to time on an outstanding unpaid balance; and
- provides a replenishable credit line that is reusable without further approvals. The label of a plan or account is not determinative, and courts have sometimes found credit to be spurious open-end credit.[331]

Any high-cost credit line that is substantially repaid in full in 45 days (or that requires individual advances to be repaid within 45 days) would not genuinely meet these criteria or would evade the ability-to-repay rules and should be subjected to the closed-end rules. Otherwise, short-term open-end loans will allow lenders to evade the rollover protections entirely, a key aim of which is to address short-term repeat transactions.

The mere fact that the credit agreement contemplates repeat transactions and can be reused does not make it an open-end credit line. Online payday loans contemplate repeat rollover transactions, but that does not make them open-end. To the extent that no further approval is needed, that aspect of open-end credit could eviscerate the ability-to-repay rules and other limits on short-term loans.

The requirement that a finance charge be imposed that is computed from time to time on an outstanding unpaid balance is a key requirement to distinguish true open-end lines from high-cost closed end loans in disguise. If an advance must be substantially repaid within 45 days, the product contradicts this requirement because there will be no outstanding balances upon which to calculate the finance charge. The requirement assumes that the plan does not require the entire credit advance to be repaid in full within such a short period, and that the cost of the credit is not a fixed amount determined in advance. Rather, this aspect of open-end credit assumes that the balance on the credit line fluctuates, and charges are determined based on how much of the credit remains unpaid after a period of time. Short-end credit lines, however, are more likely to be fully utilized immediately, with fees based on the size of the draw, not based on a periodic interest computed based on the time the balance remains unpaid.

Finally, a credit line is replenishable and reusable without further approvals. But high-cost lenders typically have control over whether and how consumers can draw on the credit line. Their open-end products do not operate like credit cards that can be used unilaterally and immediately without any action on the bank's part. Moreover, even to the extent that the lender does permit the consumer to make additional draws without further approvals, that would evade the ability-to-repay requirements. Each draw could be done without underwriting.

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[330] These, as the Bureau notes, have been discontinued with the exception of Fifth Third's product.

[331] *See* National Consumer Law Center, Truth in Lending § 6.2.3 (9th ed. 2015), *updated at* www.nclc.org/library.

When credit is due in full, or virtually in full, in a finite period of time (45 days or less) it actually is—or should be viewed as—a series of closed-end loans, not a plan permitting a balance that fluctuates, can rise and fall, and can be carried as an outstanding balance over time. Regardless of the label that lenders may put on their loans, the CFPB should impose the same rules for each extension of short-term credit, whether viewed as a closed-end loan or a draw on an open-end line.

Minnesota recently took a comparable approach. The state's largest payday lender began making short-term open-end loans, due in full on the borrower's next payday, under an open-end (mortgage-related) statute because that statute permitted even more generous rates than the $15 per $100 permitted by the closed-end statute.[332] Following that migration, the state enacted a law that covered payday loans whether closed-end or open-end. Notably, that statute requires that every advance on a short-term open-end loan be treated as a new loan.[333]

We emphasize that the CFPB's treatment of open-end credit lines does not need to turn on whether the CFPB views the credit lines as genuinely open-ended or not. Even if the Bureau views a product as open-ended, it may still treat each advance as a new loan for purposes of the ability-to-repay rules in order to protect consumers and prevent evasions.

Any uptick in the offering of short-term open-end loans following this proposed rule should raise serious flags about evasion, either of state laws that are stronger as to closed-end products; of an APR requirement that is more likely to apply to closed-end loans; or of these rules themselves. The Bureau should explicitly acknowledge this reality in the rule and ensure its rules are designed to prevent evasion through the use of short-term open-end products

6.3.2.2. "Reasonable determination" on a short-term open-end loan should treat every advance as an individual loan requiring an ability-to-repay assessment (§ 1041.5(b)(1)(ii)).

Section 1041.5(b) requires that a reasonable determination of ability-to-repay be done for short-term open-end loans (1) before making a new loan; (2) before increasing the credit line; or (3) before advancing more credit if more than 180 days have passed since the last determination.

We strongly oppose permitting lenders who make short-term open-end loans to make multiple advances without considering whether the consumer has the ability to repay each advance, while meeting other obligations and without reborrowing. It would be simple for payday lenders to convert their products to open-end credit lines and evade the 30-day periods between short-term closed-end loans.

Thus, we urge treating every advance as an individual loan requiring its own ability-to-repay determination. This approach is warranted in light of the high likelihood that a short-term open-end

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[332] http://jrlc.org/jrlc/images/stories/IssuePapers/PaydayLendingPaper0514.pdf.

[333] MN Statutes 47.601. https://www.revisor.mn.gov/statutes/?id=47.601. ("Consumer short-term loan" means a loan to a borrower which has a principal amount, or an advance on a credit limit, of $1,000 or less and requires a minimum payment within 60 days of loan origination or credit advance of more than 25 percent of the principal balance or credit advance. *For the purposes of this section, each new advance of money to a borrower under a consumer short-term loan agreement constitutes a new consumer short-term loan*) (emphasis added).

loan is an evasion product. It would also be consistent with the approach Minnesota took to address short-term open-end loans as noted in 6.3.2.1

6.3.3. The time periods relevant to the ability-to-repay determination for short-term loans should be modified: § 1041.5(b)(2).

Section 1041.5(b)(2) provides that a reasonable determination requires the lender to determine sufficiency of residual income for (1) the shorter of the loan term or the period ending 45 days after consummation; and (2) for 30 days after the highest payment under the loan on its due date.

With respect to (1) above, the Bureau notes that this would permit lenders to make one determination based on the sum of all payments due during the term of the loan, rather than having to make a separate determination for each payment and pay period in isolation. We urge instead that every payment on a short-term loan have its own ability-to-repay determination, for two reasons.

First, as the Bureau notes, the compressed time period of a short-term loan makes the payments very sensitive to the precise timing of income and obligations and expenses. This rationale supports requiring a determination that the borrower has the ability to make every individual payment in light of income and expenses occurring at that time.

Second, there are almost no multi-payment loans with terms of 45 days or less today. Any shift to multi-payment short-term loans going forward is likely an evasive measure in an effort to make payments appear more affordable and to extract more days' indebtedness out of borrowers in light of the rule's provisions aimed at preventing flipping of short-term loans. In light of that, the rule should do more to ensure these ability-to-repay determinations are meaningful and require that each payment be individually underwritten.

The Bureau also notes that this provision would require the lender to make the determination for the actual term of the loan so that, for example, the residual income assessment cannot be based on some other period, even of potentially the same length, that might include, for example, more paychecks than will actually be available to the borrower for loan repayment. In addition, the Bureau explains that this provision ensures lenders cannot count residual income that will accrue after 45 days, even if an unsubstantial amount of the loan is due after 45 days. We support this approach. The Bureau suggests that the example provided in Proposed Comment 5(b)(2)(i)-1.i. illustrates this point; as we understand the provision and the Proposed Comment, we would recommend an additional example to illustrate the provision more clearly.[334]

With respect to the 30-day period following the highest payment, we strongly support extending the underwriting period beyond the loan term, given the clear evidence that these loans lead to reborrowing. Moreover, considering only at a two-week loan term, for example, would ignore the fact that a large rent payment may be due shortly following repayment of the loan. We further agree with the Bureau's assessment that a period beyond the loan term is particularly necessary given that repayment occurs on payday, meaning that a full pay cycle will elapse before a borrower's next paycheck. However, as discussed at length in sections 8 and 11 addressing presumptions of

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[334] This Comment provides an example of a 16-day loan. As we understand the proposed provision, we suggest an additional example of a loan longer than 45 days, but substantially due within 45 days, to help illustrate the provision.

unaffordability following balloon payment loans, we urge that this period be 60 days rather than 30 because 30 days is shorter than the likely monthly expense cycle for payday borrowers. The same rationale applies here.

The Bureau solicits comment on whether this proposed 30-day period should run from the last payment, even if that payment is not the highest payment. We strongly urge the last payment as the more relevant and appropriate point. Only upon making the last payment has the borrower fulfilled the loan obligation and felt the full impact of all of the payments. Measuring from the last payment is particularly important given that lenders could design a last payment that is only slightly smaller than a higher earlier payment in order to game the rule and start the clock running sooner.

In addition, as discussed in those sections, the Bureau should evaluate compliance with this provision not only by examining the lender's upfront underwriting requirements, but also by assessing whether consumers were in fact able to meet expenses during the full required period. Patterns of repeat loans shortly following the 30-day period are a strong indication that the ability-to-repay indication was deficient, suggesting the borrower stretched to defer expenses until the presumption period expired. Lenders whose loans reflect such patterns should be required to adjust their underwriting criteria going forward. The CFPB should conduct research to find out what happens to consumers and their ability to meet other expenses during the 30 days (or 60 days, as we recommend) following a short-term loan.

6.3.4. Lenders should be required to account for information known by the lender, including patterns of reborrowing: Comments 5(b)-2.i.E and 9(b)-2.i.E.

Proposed Comments 5(b)-2.i.E and 9(b)-2.i.E require the lender to appropriately account for information known by the lender, whether or not the lender is required to obtain or consider it.

We strongly support this requirement. Lenders cannot turn a blind eye to information that is relevant to the consumer's ability-to-repay. For example, if the consumer mentions that she has a medical condition and pays $300 per month for medicine, or that she has been having trouble paying for gas in light of her long commute, the lender must consider that information.

We emphasize in particular that a pattern of reborrowing is known by the lender, and an example should be added to the Commentary. In its discussion of the requirement to account for information known to the lender, the Bureau notes that a pattern of borrowing as soon as a 30-day cooling off period has passed may suggest lack of ability-to-repay and thus be information the lender should be required to account for.[335] We agree and urge that this and additional examples of patterns of reborrowing should be included in the Commentary, including:

- The borrower's history shows a pattern of repeat reborrowing shortly following 30 days after short-term loans or longer-term balloon payment loans.
- The borrower has repeatedly refinanced longer-term covered loans before making significant progress in repaying the loans; see section 11 for further discussion.

[335] 81 Fed. Reg. at 47947.

6.3.5. Lenders should explicitly be required to consider information from the credit report.

Currently, there appears to be no clear requirement that a lender consider a borrower's recent performance on other credit or in meeting other expenses.[336] This is striking, particularly in light of the Bureau's findings that borrowers are likely to have had recent delinquencies, and consideration of whether a borrower is already struggling with their expenses should be an important factor in an ability-to-repay determination.

While the rule does require lenders to obtain and review credit reports, to incorporate any major debt obligations revealed on those reports, and to account for information known by the lender, nowhere in the proposal are lenders directly required to account for information showing that consumers are struggling to manage their current obligations and expenses. This may be information reflected in the credit report.

Lenders should be required to assess the nature and extent of delinquencies revealed in the credit report and incorporate their findings into the assessment of whether the consumer has available residual income to cover the loan payment. It may be that the consumer was 30 days late on a loan or utility payment a few months ago but has since caught up. Or the consumer could have been evicted due to nonpayment but now has a new apartment at lower rent and is current.

But if the credit report reveals that the consumer has been unable to afford current debt payments and nothing has changed, an underwriting model that falsely shows that the consumer has available residual income would not be reasonable. Thus, we urge the CFPB to add comments with examples of information on the credit report the lender must consider, such as:

- delinquencies or defaults on any covered loans with any lender within the past year;[337]
- significant delinquencies on any credit within the past year;
- default on any credit within the past year; and
- any delinquency, currently.

6.3.6. A determination of ability-to-repay is unreasonable if it relies on an implicit assumption that the consumer will obtain additional credit or accumulate savings: Comments 5(b)-2.ii and 9(b)-2.ii.

Proposed Comments 5(b)-2.ii and 9(b)-2.ii provide that a determination of ability-to-repay is not reasonable if it relies on an implicit assumption that the consumer will obtain additional credit.

We support this standard and note its particular relevance to the rule's approach to refinancings of longer-term loans. Just as an upfront ability-to-repay determination should not assume new credit during the loan term, routine obtaining of new credit during the original loan term in the form of refinancings, particularly earlier in the loan, should signal that the borrower did not have the ability to

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[336] This could arguably be encompassed by –D. and –E., requiring that a reasonable determination be grounded in reasonable inferences and conclusions and that it account for any information known by the lender, but it's not at all explicit.

[337] We note that per the SBREFA outline, the Bureau was considering requiring lenders to assess whether a borrower had recently defaulted on any covered loan with any lender.

repay the loan without obtaining new credit. A lender that has a portfolio with a significant volume of refinancing, particularly without having substantially paid down the loan, may not be making reasonable determinations that consumers can repay without reborrowing. See section 11 for further discussion.

The Bureau solicits comment on whether there are any circumstances in which the lender may assume additional credit or accumulation of savings.[338] We urge the Bureau not to permit these possibilities. Permitting an assumption of additional credit is inconsistent with a "without reborrowing" definition of ability-to-repay, and accumulation of savings is not likely enough for borrowers of covered loans to warrant the risks of evasion such an approach would pose.

6.3.6.1. An example of unreasonable ability-to-repay determinations should be added based on portfolio-wide high rates of reborrowing and defaults.

As discussed in section 5.3 above, a reasonable ability-to-repay determination requires an assessment that consumers can repay loans according to their terms—i.e., without reborrowing. An example of a lender that is not adequate assessing ability to repay according to the loan's terms should be added showing repeat reborrowing or high defaults at the portfolio level.

Even if the rule does not impose a presumption of inability to repay for a given consumer, the fact that a high proportion of the lenders' borrowers do not repay their loans without reborrowing or defaulting provides evidence that the lender is not making reasonable determinations and should adjust its approach. Thus, an example of unreasonable ATR determinations could be added that says:

- A substantial portion of lender's borrowers do not repay their loans without becoming delinquent, defaulting, or reborrowing before the loan is fully repaid.

6.3.7. Performance compared to other lenders: Comments 5(b)-2.iii. and 9(b)-2-iii.

We strongly oppose Comments 5(b)-2iii. and 9(b)-2iii, which provide that evidence of whether determinations of ability-to-repay are reasonable may include the extent to which delinquency, defaults, and reborrowing rates are low, equal to, or high, including in comparison to the rates of other lenders making covered loans to similarly situated consumers. We discuss these at section 7, a separate section urging that these rates be required to be low in the absolute.

6.3.8. The examples of reasonable methods for projecting basic living expenses must be significantly strengthened to eliminate unfettered discretion and better prevent evasion: Comments 5(b)-4.i and 9(b)-4.i.

We strongly support inclusion of basic living expenses in the ability-to-repay determination. We do not disagree with the Bureau's assessment that requiring a "complete and accurate itemization of each consumer's basic living expenses" would be challenging. Thus, an approach short of individualized documentation may be warranted.

[338] For longer-term loans under proposed § 1041.9, the Bureau explicitly includes accumulation of savings as an "unreasonable" indication.

At the same time, we are concerned that the Bureau's proposed approach to basic living expenses leaves lenders far too much discretion in how they are projected. We fear that lenders will simply back into a basic living expenses projection based on what level of repayment (and defaults) they believe the rule will tolerate. Taken together, these concerns risk making the ability-to-repay standard circular and subjecting many borrowers to continued substantial harm.

Proposed Comments 5(b)-4.i and 9(b)-4.i provide a non-exhaustive list of reasonable methods for projecting living expenses. Two are relatively specific, while the third is far more general:

(A) Set a minimum percentage of income or dollar amounts based on statistically valid survey of expenses of similarly situated consumers, taking into account the consumer's income, location, and household size;
(B) Obtain additional reliable information about a consumer's expenses to develop a reasonably accurate estimate; or
(C) "Any method that reliably predicts basic living expenses."

Method (A): Surveys. With respect to method (A), the Bureau notes that several lenders have indicated they currently use this method. The Bureau further notes that this method is consistent with the recommendation of the Small Dollar Roundtable.[339] And the CFPB notes that the Bureau of Labor Statistics period survey may be useful for this purpose. The Bureau solicits comment on whether this method should, as proposed, require taking the consumer's income, location, and household into account.

Use of a well-researched independent government survey is the preferable statistical survey approach. The CFPB must be careful not to sanction the use of surveys that are not based on reliable independent evidence. Purported surveys by the lender, rather than by a credible independent entity, should be particularly suspect. When the lender uses a survey approach other than a well-researched government standard, we urge the CFPB to review the estimates against government surveys like the Bureau of Labor Statistics period survey.

We note that the Small Dollar Roundtable's recommendation was more limited than how the Bureau describes it in the proposed rule; that recommendation stated: "Use of third-party statistical proxies for expenses *may be* acceptable *in limited, specified circumstances*, where they have been deemed sufficiently robust and reliable. *Use of proxies poses greater risk for longer and larger loans*."[340]

Method (B): Information about the borrower's expenses. With respect to method (B), the Bureau notes that this method may be more convenient for smaller lenders. We support this method to the extent that it collects the actual expenses of an individual borrower supported by third-party reliable data. Without reliable third-party data, this method is highly vulnerable to abuse.

Analysis of checking account activity, which is currently one example of this Method B, should be included more explicitly as a "reasonable method" and encouraged. This is essentially the method required by the OCC/FDIC guidance for determining ability to repay for banks making payday loans. For

[339] 81 Fed. Reg. at 47949.
[340] Small Dollar Roundtable Consolidated Discussion Summary for the Consumer Financial Protection Bureau, Nov. 11, 2015, https://www.regulations.gov/document?D=CFPB-2016-0025-0046 (emphasis added).

any depository, this should be the method used. For other lenders, service providers make providing checking account activity, and analytical analysis thereof, a feasible option.[341]

Method (C): Any method that reliably predicts basic living expenses. With respect to method (C), the Bureau emphasizes that it wants to be clear that "innovative" and "data-driven" methods, though not "as intuitive" as other methods, may be used if they produce reliable estimates.[342] The Bureau notes that it "would expect to evaluate the reliability of such methods by taking into account the performance of the lender's covered [short-term or longer-term loans, as applicable] in absolute terms and relative to other lenders."[343]

We have significant concerns about this approach as giving an unwarranted degree of discretion to lenders. We do not foreclose the possibility that there could be other methods of reliably predicting basic living expenses other than those discussed above. However, given the perverse incentives at play and the historical evidence of evasion in these markets, this vague, open-ended approach is ripe for abuse.

Moreover, reliable estimates can and do produce outcomes that result in borrower hardship. Innovative underwriting may accurately predict default rates, but it does not necessarily reduce default rates. And as noted in 7.3 below, pricing and capital structure can result in a profitable portfolio at 40% default rates, but rates anywhere near that high indicate severe consumer harm.

Our concerns include the following:

- *The method must actually predict expenses.* Like a survey or an evaluation of a consumer's actual expenditures, a reliable method must be based on data that measures *expenses.* But the CFPB's plan for evaluating the lender's approach seems to focus primarily on loan performance, not on whether the method reliably predicts expenses. As the CFPB documents at length, the leveraged payment mechanism results in loans that are repaid despite unaffordability. Moreover, lenders who have a high tolerance for defaults may simply crank data to justify whatever level of basic expenses produces the loan approval rates their business model supports.

- *What is "reliable" and how is it judged?* "Reliable" is open to significant interpretation. For example, a crude percent of income that is unrelated to household or geography may be predictive for some consumers but be totally unreliable for others.

- *The benchmark must not be other covered lenders.* As discussed in section 7 below, we strongly oppose evaluating one high-cost lender's loan performance simply "relative" to other lenders. We do agree, however, that the lender's loan performance in absolute terms (measured looking at a number of different factors, as discussed in sections 7.4-7.7 below) is an important means of assessing whether ability-to-repay determinations are reasonable.

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[341] Our understanding is that service providers Intuit, Microbilt, Yodlee and Plaid, all offer these services and can provide transaction records for account held at most depositories. At least one lender that uses deposit account transaction records to determine residual income has indicated that it can analyze transactions at nearly every financial institution in the country.

[342] 81 Fed. Reg. at 47949.

[343] *Id.*

Other potential methods. The Bureau solicits comment on whether a borrower questionnaire should be required for basic living expenses and if so, how its completeness and correctness should be verified. It also asks whether any questionnaire should ask only about expenses that are "necessary" or also those that are "recurring and not realistically reducible" during the loan term. The Bureau acknowledges the risk of lender manipulation of borrower certifications and indeed its concern is warranted. If a borrower questionnaire is required or permitted, it (1) should be used in addition to an independent method; and (2) should under no circumstances permit lenders to use figures less than those indicated by verification evidence or, less frequently, reliable third party data, retained by the lender.

We understand that some industry participants have pushed for the Bureau to permit lenders to use a borrower's stated expenses (and income) "validated" against geography-based averages to determine whether they are reasonable along a "bell curve."[344] We are concerned that this method would permit lenders to game the ability-to-repay determination by, among other things, encouraging the stating of expenses that are at the lowest purportedly reasonable end of a bell curve.

The Bureau also solicits comment on whether it should provide a more prescriptive method or a safe harbor. As noted, we recommend the Bureau encourage review of actual checking account activity as it reflects a borrower's actual, individual circumstances. At the same time, we strongly oppose a safe harbor for any method or any expense level. A proxy applied to all households is likely to most disadvantage lower-income and higher-cost households—those most likely to struggle to repay. It is thus unlikely to provide reasonable assurance of accurate ability-to-repay determinations. Ultimately, a safe harbor would provide an unwarranted shelter for lenders while exposing borrowers to substantial harm.

Finally, we urge expense estimate be reported to the Bureau, and that lenders who routinely project lower expenses than research would support face close scrutiny.

6.3.9. The examples of unreasonable methods for projecting basic living expenses must also be strengthened: Comments 5(b)-4.ii and 9(b)-4.ii.

The Bureau further provides, in proposed Comments 5(b)-4.ii and 9(b)-4.ii, a non-exhaustive list of unreasonable methods for projecting basic living expenses:

(A) A method that results in no or implausibly low funds for basic living expenses, causing "substantially all of a consumer's net income that is not required for payments for major financial obligations is available for loan payments."

(B) A method of setting minimum percentages of income or dollar amounts that have yielded "high rates of default and reborrowing relative to rates of default and reborrowing of other lenders making similar loans to similarly situated consumers."

We agree with the statement in (A) above. Any estimate must be examined for plausibility. Certainly, assuming that a consumer needs no additional income for food, clothing, transportation or other basic expenses after paying rent and other documented major obligations would not be reasonable. But the

[344] FactorTrust Webinar, Filling the void: ATR & reporting alternatives for CFPB rule, hosted by American Banker, Aug. 30, 2016.

CFPB must take care not to set the bar too low. This example would be more helpful if it were less extreme. For example, a more specific example that describes the income needed for certain expenses, the amount left over, and why that is not plausible for a family of the consumer's size should be more helpful.

With respect to (B), we have two concerns. First, we oppose the suggestion that basic expenses take up the same percentage of income for every family, regardless of family size, how low their income is, or how much of it they need to devote to basic expenses. We fear that this approach permits the lender to arbitrarily select nearly any percentage it chooses without any external validation as we urge in the preceding section. It also likely disadvantages the lower income households, for whom expenses likely make up a larger portion of their overall income. Second, we oppose the notion that the sufficiency of a projection for basic living expenses may be based on whether it results in high rates of default and reborrowing relative to similar loans to similarly situated consumers. This issue is discussed in section 7 below.

6.4. Projections for Net Income and Major Financial Obligations Should Always Be Supported by Verification Evidence or, in Rare Circumstances, Other Reliable Third-Party Evidence: § 1041.5(c) and 1041.9(c).

6.4.1. In General.

Sections 1041.5(c) and 1041.9(c) set out requirements for projecting net income and payments for major financial obligations as part of the broader reasonable determination requirement. Generally, the lender must obtain two forms of evidence: (1) consumer's written statement of the amounts and timing of their income and payments on major financial obligations; and (2) third-party "verification evidence." The lender must then make a reasonable projection of both the amount and timing of income and payments on major obligations.[345]

Under the proposal, those projections may be based on the consumer's statement only to the extent the consumer's statement is consistent with verification evidence. In determining whether this consistency is present, the lender may reasonably consider other "reliable evidence" the lender obtains from or about the consumer, including consumer explanations.[346] The Commentary provides several examples of this scenario.

The lender's projection may also vary from the verification evidence (i.e., even if *not* consistent with the verification evidence) if the change versus the verification evidence is verified via written statement from the payor of income or payee of the obligation.[347]

Finally, this section sets out what constitutes "verification evidence" for both income and major financial obligations.

[345] Proposed § 1041.5(c)(1).
[346] Proposed § 1041.5(c)(1).
[347] Proposed § 1041.5(c)(2).

6.4.2. Claims that a consumer shares obligations jointly should require verification evidence: § 1041.5(c)(1).

The Bureau has asked whether additional rules are needed beyond the proposal permitting lenders to rely on the consumer's explanations for why they are responsible for only a portion of a debt for which they are jointly liable.

We are concerned that the proposal's current approach—permitting lenders to rely on consumer explanations and other evidence—is insufficient and will be easily gamed by lenders. Permitting unrestrained self-certification in this area risks entirely undermining the verification rules. The concern relates both to major financial obligations on a credit report and rental obligation. (For additional discussion of shared rent, see 6.4.4.3.2 below.)

We urge instead that, to the extent a consumer claims that another household member contributes to the payment of a major financial obligation, the lender must support that determination with verification evidence. The evidence either must verify that another household member does in fact contribute to the cost (for example, with respect to rent, with a lease, landlord receipt, or co-tenant statement) or that the household contains another income-earner whose income is sufficient to determine that the claimed contribution is reasonable (with proof of income).

This is a reasonable approach, particularly given that a fairly small minority of lower income individuals live in households with multiple earners—20-31% among earners with income in the $20,000-$34,999 range, nationally (see chart below).

In addition to requiring verification, the Bureau should consider providing guardrails that signal to lenders, as well as to supervision and enforcement, when the portion of a portfolio's borrowers considered to have joint obligations is more likely to be unreasonable. For example, the following figures show the portion of households with multiple earners, nationally. The Bureau might subject to heightened scrutiny portfolios that have more households with joint obligations or shared rent than these percentages would indicate is reasonable. Additional or other metrics that might serve as proxies for joint obligations and thus guardrails may also be useful.

Portion of households with multiple earners, nationally, by income:[348]

$20,000 to $24,999	$25,000 to $29,999	$30,000 to $34,999	$35,000 to $39,999	$40,000 to $44,999	$45,000 to $49,999
20%	28%	31%	37%	42%	49%

6.4.3. The projection for net income and payments for major financial obligations should always be based on verification evidence or, under very rare circumstances, other reliable third-party evidence: § 1041.5(c)(2) and § 1041.9(c)(2).

Permitting the lender to use income or obligation amounts that differ from verification evidence based on consumer explanations is not warranted in light of the Bureau's observation in its discussion of this

[348] CRL Tabulation of data from US Census Current Population Survey, 2014.

section: "Lenders have an incentive to encourage . . . misestimates to the extent that as a result consumers find it necessary to reborrow."[349] For this reason, all projections for net income and payments for major financial obligations should be based on verification evidence or, less often, verified via written statement from the payor of income or payee of the obligation.

We urge the Bureau to permit only variations based on consumer statements that result in conservative projections of income and payment of obligations. In other words, any variation from verification evidence that results in a higher income projection or a lower payments projection should be deemed inconsistent. To the extent that reliable third-party evidence supports such a projection, the lender may use the exception provided under 1041.5(c)(2) or 1041.9(c)(2), discussed below.

The examples in proposed Comments 5(c)(1)-1 and 9(c)(1)-1 support this position. Comments 1041.5(c)(1)-1.A, B, C, D, and G all provide that the lender use either the verification evidence figure, or the more conservative figure, when there is a variance between stated information and verification evidence.

Proposed Comment 1041.5(c)(1)-1.E and F, on the other hand (and proposed Comment 1041.9(c)(1)-1.E and F), provide that the lender may use stated information over verification evidence in two troubling circumstances when, in both cases, reliable third-party evidence could be obtained to support the variance.

In Example E, the consumer states the receipt of $1,000 in net income biweekly, but verification evidence shows income of $1,000, $1,000, and $800 in the previous three pay periods. The drop-off, per the consumer's explanation, is due to missing two days of work due to illness, and the Commentary provides that using $1,000 is reasonable. This approach is both problematic and unnecessary. It is problematic because lenders will always have an incentive to explain away income dips like this, which could instead be attributable to the normal volatility of an uneven work schedule. Missing days due to illness is also part of the normal income volatility that should be accounted for if an employee does not have sick leave. It is unnecessary because it is reasonable to require the borrower to provide third-party documentation, like a submitted timesheet, supporting the sick days, which would fall under the exception in 1041.(5/9)(c).

Example F permits the lender to use stated income when income from the last month has been zero, where the consumer explains that the consumer's manufacturing plant is temporarily closed. While we note that lenders do have some incentive to ensure that borrowers have sufficient income to cover each loan repayment, this example is, again, problematic and unnecessary. It is problematic because it is not clearly different from an example whereby the borrower would show minimal sufficient income to make the loan payment itself (regardless of income and expenses). There also may be no assurances that the plant will re-open. It is unnecessary because the lender should be able to obtain third-party verification that a manufacturing plant has been closed for a month. Requiring verification of an event having such a major impact on a consumer's income is critical. The CFPB should not sanction this type of deviation from the verification requirements.

Thus, in seven examples provided, the Bureau has provided none where this provision allowing consumer statements to override the evidence is needed, nor one where it would not be problematic.

[349] 81 Fed. Reg. at 47952.

We urge the Bureau to remove it. The Bureau notes that it believes projections "will generally be supported by objective, third-party documentation or other records."[350]

We do not categorically object to proposed § 1041.5(c)(2) and § 1041.9(c)(2), which permit lenders to use reliable third-party evidence to depart from verification evidence. The example provided in discussion is that a consumer was unemployed but has recently obtained a new job and presents an offer letter from the employer with pay. This example is reasonable, but we note that reductions in major financial obligations are likely less common, particularly if timed with when a borrower seeks a covered loan. To ensure this exception stays extremely limited, we urge the Bureau to require reporting of the number of originations as a percentage of total originations for which the lender relies on this exception.

6.4.4. Evidence of net income and major financial obligations: § 1041(c)(3).

6.4.4.1. Consumer statements: § 1041(c)(3)(i).

We are skeptical about the value of obtaining consumer statements, but we do not object to it so long as the lender is never permitted to take a less conservative figure from consumer statements than verification evidence indicates. We note that the Bureau explains that verification evidence may contain "ambiguous, out-of-date, or missing information." While we understand that this may be the case, the powerful lender incentives discussed throughout this comment to overstate ability-to-repay support preventing overstatement of residual income in this way. Placing any significant weight on consumer statements that result in net income higher or obligations lower than can be verified through third-party evidence provides a wide avenue for evasion. Experience across consumer credit markets shows that "consumer" statements can just as easily, in reality, be lender statements.

The proposal currently provides that lenders may accept oral statements. We urge that the lender be required to obtain written statements. Though perhaps not significantly, a written requirement may reduce the likelihood that lenders are gaming this portion of the rule by filling in blanks with whatever figures they choose and then directing the borrower to "sign here."

6.4.4.2. Verification evidence for net income: § 1041(c)(3)(ii)(A).

This section requires that the lender obtain "a reliable record (or records)" of an income payment covering sufficient history to support the lender's projection.

6.4.4.2.1. "reliable record"

The Commentary provides that examples of a reliable record include an income-payer-provided document, as well as deposit account transaction activity, prepaid account transaction activity, or check-cashing transactions.[351] The Bureau describes this provision as permitting a wide range of methods of verifying income, in response to concerns noted during the SBREFA process. We agree that all of these methods are reasonable.

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[350] 81 Fed. Reg. at 47952.
[351] Proposed Comment 5(c)(3)(ii)(A)-1.

We note, as the Bureau does, that it has made accommodations for cash-paid consumers here by including account transaction activity as a reliable record. We support the Bureau's approach not to make further accommodations that would permit lenders to rely on cash income that cannot be verified through verification evidence. We agree with the Bureau's conclusion that "the risk is too great that projections of net income would be overstated . . . resulting in the harms targeted by this proposal."[352] The same conclusion applies to whether lenders should be able to rely on cash income that is *supplemental* to income verified through verification evidence, which we urge the Bureau to reject.

We also support the proposed approach not to permit the use of predictive models designed to estimate consumer income or to "validate" the reasonableness of a consumer's statement of income.[353] First, these loans carry substantial risk of harm, coupled with substantial lender incentive to overstate income. Verification of an *individual* consumer's *actual* income, which the proposal would permit to be done fully electronically (through photocopies or cell phone image capture), is an entirely reasonable and prudent expectation under the circumstances. We also emphasize, as the Bureau notes, that the Small Dollar Roundtable, which included several lenders, supported an income verification requirement, not modeling or validation.

Second, as the Bureau notes, these models typically estimate *annual* income and lack the precision necessary to project income for a shorter period of time. Indeed, data showing the degree of income volatility supports rejection of an imprecise approach. Moreover, income estimates can be wildly inaccurate. A report by NCLC described the results when several NCLC employees sought copies of reports about themselves by big data purveyors that claim to be able to estimate income. Seven of the fifteen reports generated by one service contained significant errors in estimated income, nearly doubling the salary of one participant and halving the salary of another.[354]

6.4.4.2.2. "sufficient history": § 1041.5(c)(3)(ii)(A) and 1041.9(c)(3)(ii)(A).

These provisions require that the lender obtain reliable income records covering a "sufficient history" to support the projected income. The provision does not specify a minimum look-back period over which the lender must verify income. The Bureau notes that it "does not believe it is necessary or appropriate to require verification evidence covering a lookback period of a prescribed length."[355] The Bureau does not provide substantial elaboration, simply noting that what constitutes a "specific period" may depend on the source/type of income, the consistency of the income, and the length of the loan.

As we discuss in 10.4.5 below, we urge that for longer-term loans longer than 6 months, the Bureau require a specified lookback period the length of the loan term.

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[352] 81 Fed. Reg. at 47954.

[353] We are aware that some industry participants are still urging a "validation" over a "verification" approach; see FactorTrust webinar 8/31, *supra*.

[354]Persis Yu& Jillian McLaughlan, NCLC, Big Data A Big Disappointment For Scoring Consumer Credit Risk (March 2014), http://www.nclc.org/issues/big-data.html.

[355] 81 Fed. Reg. at 47954.

6.4.4.2.3. We support requiring obtaining both an RIS and a credit report: § 1041.5(c)(3)(ii)(B); § 1041.9(c)(3)(ii)(B).

The proposal requires lenders to use two different types of consumer reports in order to determine the consumer's debt obligations as part of an ATR analysis: (1) a report from a registered information system (RIS), a special type of consumer reporting agency (CRA) that the proposed regulation would govern; and (2) a report from a nationwide CRA (as defined in the Fair Credit Reporting Act, 15 U.S.C. § 1691a(p)), commonly known as a "credit report." Lenders would be required to obtain these consumer reports for both short-term loans and longer-term loans.

We support the requirement for lenders to obtain both a RIS consumer report and a credit report. Both types of consumer reports are necessary in order to conduct a meaningful ATR analysis. The CFPB is correct in noting that "most typical consumer debt obligations other than covered loans would appear in a [credit report]" but that most loans covered by the proposed rule are not reported to the nationwide CRAs.[356] Thus, lenders must have another source of information in order to be fully informed about the existence of other payday loans that the consumer may have borrowed. An approach consisting of only reviewing the lender's own information and the existing consumer reporting market (*i.e.*, the nationwide CRAs and existing specialty subprime CRAs) would not enable compliance with the ability-to-repay determination requirements.

We understand that lenders have raised a number of concerns about the requirements to obtain a credit report and a RIS report. We believe that these concerns are overstated and that the proposed requirements are both reasonable and not overly burdensome. For example, the American Banker reports that major concerns of covered lenders include: [357]

- the credit histories of covered loan borrowers are too threadbare or do not exist;
- the credit histories of these borrowers are too scattered among public or private sources to be unified; and
- no private company will be able or willing to building a registered information system from scratch.

With respect to the first concern, we note that the credit histories of borrowers of covered loans are not too threadbare or non-existent. In actuality, most covered loan borrowers do have credit history files at the nationwide CRAs. For example, the authors of a research study analyzing payday loan applications noted that the results of their matching payday borrowers to nationwide CRA files "imply that nearly all of the payday loan applicants had a credit record at the time they applied for their first payday loan."[358] Thus, payday borrowers appear more likely to be "thick file" than "thin file" consumers. Moreover, even if a particular covered loan borrower has a thin or no file at a nationwide

[356] 81 Fed. Reg. at 47955.

[357] Andy Peters, Who Will Fill the Credit Reporting Void in the CFPB's Payday Plan? American Banker, Aug. 1, 2016.

[358] Neil Bhutta, Paige Marta Skiba, & Jeremy Tobacman, Payday Loan Choices and Consequences (2014) at 12, available at http://www.calcfa.com/docs/PaydayLoanChoicesandConsequences.pdf. The authors matched 250,000 payday loan application files to credit report files in the Federal Reserve Bank of New York's Consumer Credit Panel (CCP), composed of Equifax data. Since the primary CCP dataset is a five-percent random sample, the authors had expected to match roughly 12,400 applicants to the CCP. Indeed, they were able to match 12,151 individuals, suggesting that most payday borrowers had a file with Equifax. *Id.* at 11.

CRA, that simply means the lender will not have any debt information from the credit report that it must include in its ability-to-repay determination.

With respect to the second concern, contrary to industry complaints, the proposal does not require the aggregation of information from different databases such as public records or tenant screening CRAs. The proposed rule only requires lenders to obtain two specific reports: a credit report and a RIS report. While establishing such an aggregated database might be *helpful* for a lender to determine other elements of the borrower's ability to repay, the proposal does not *mandate* the establishment or use of such databases.

Finally, we think the concern that no private company will be able or willing to serve as a registered information system is overstated. There are already several entities that have said they are willing to serve in this role, including Veritec and FactorTrust.[359] Indeed, FactorTrust has been marketing its ability to serve as a RIS, including holding webinars[360] and even mailing promotional materials to consumer groups such as NCLC.

For discussion of our recommendation that lenders be required to consider delinquency and default information shown on RIS and credit reports, see section 6.3.5.

6.4.4.3. Verification evidence for major financial obligations, including housing: § 1041.5(c)(3)(ii)(B)-(D) and § 1041.9(c)(3)(ii)(B)-(D),

6.4.4.3.1. Major financial obligations other than housing rent cost: § 1041.5(c)(3)(ii)(B)-(C) and § 1041.9(c)(3)(ii)(B)-(C).

The proposal requires that, for required payments under debt obligations (i.e., excluding rent), the lender must obtain "verification evidence" in the form of a national consumer report, the records of the lender and its affiliates, and a consumer report from a registered information system (RIS), if available.[361] The lender must also consult the national consumer report for court- or government agency-ordered child support obligations.

We support this general approach as proposed, with two recommendations.

First, we flag that it is not clear where property taxes and homeowner's insurance would be picked up for a consumer whose taxes and insurance are not escrowed. Should the current approach to housing costs be retained in the final rule, it should explicitly provide that, for homeowners, major financial obligations must include locality-based estimates, reasonably related to the size of the consumer's monthly mortgage payment, for both property taxes and homeowner's insurance.

Second, we urge that, if an RIS is not available, a lender must obtain information from any state database in the consumer's state that includes covered loans, if such information is available. The lender must include any payments reflected therein (whether obtained directly or estimated based on other loan information provided) in the projection of payments.

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[359] Andy Peters, Who Will Fill the Credit Reporting Void in the CFPB's Payday Plan? American Banker, Aug. 1, 2016.
[360] FactorTrust, Filling the void: ATR & reporting alternatives for CFPB rule, hosted by American Banker, Aug. 30, 2016.
[361] Proposed §§ 1041.5 (c)(3)(ii)(B), 1041.9 (c)(3)(ii)(B).

6.4.4.3.2. Housing: § 1041.5(c)(3)(ii)(D) and § 1041.9(c)(3)(ii)(D).

For housing expense other than a mortgage appearing on a national consumer report, the lender must:

> (1) obtain a "reliable transaction record (or records)" of recent housing expense payments, (which, per the Commentary, include a receipt, canceled check, or money order (or copy or image thereof) or depository or prepaid account activity),[362] or a lease agreement; or
>
> (2) use an amount determined under "a reliable method of estimating a consumer's housing expense based on the housing expenses of consumers with households in the locality of the consumer" (we call this the "locality-based estimate" below).

With respect to (2), Comments 5(c)(3)(ii)(D)-1.iii and 9(c)(3)(ii)(D)-1.iii add that a lender may estimate a consumer's share of housing expense based on the individual or household housing expenses of similarly situated consumers with households in the same locality. For example, the Bureau provides, the lender may estimate individual or household housing expense based on:

- the American Community Survey of the U.S. Census Bureau to estimate individual or household housing expense in the "locality (e.g., in the same census tract)", or

- "housing expense and other data" reported by applicants to the lender, provided that the lender periodically reviews the reasonableness of the estimates it uses by comparing the estimates to statistical survey data or by another method reasonably designed to avoid systemic underestimation of consumers' share of housing expense.

This Comment also provides that a lender may estimate a consumer's share of household housing expense by "reasonably apportioning the estimated household housing expense" by the number of persons sharing housing expense, "as stated by the consumer, or by another reasonable method."

We support requiring a reliable transaction record as defined by the proposal, acknowledging the Bureau's accommodations to lenders here to make this requirement less onerous since the SBREFA proposal. At the same time, we have significant concerns regarding (1) permitting the locality-based estimate approach in every case; (2) permitting lenders to use their own applicant data, which itself is vulnerable to lender manipulation, to develop the estimate; and (3) permitting lenders to apportion estimated household expense based solely on a consumer's statement.

We flag here that the Bureau notes that the locality-based estimate approach is consistent with the recommendation of the Small Dollar Roundtable, "which recommended that the Bureau permit rent to be verified through a 'geographic market-specific . . . valid, reliable proxy.'" The Center for Responsible Lending and Consumer Federation of America participated in the Small Dollar Roundtable (SDR). Our interpretation of the joint recommendation is narrower than presented here. The SDR recommendation provided that a market-specific proxy "*may*" be a reasonable substitute "*if direct*

[362] Proposed Comment 5(c)(3)(ii)(D)-1.ii.

evidence is not available." It also explicitly provided that, in those instances, rent should be the greater of the reliable proxy or as stated by the consumer.[363]

We recognize that the Bureau considers the locality-based estimate in part to be a response to lender concerns that verification evidence may not always accurately reflect the rent payment that the consumer actually shoulders in shared housing situations. At the same time, **the locality-based estimate** approach, which permits apportionment of household expense based solely on a consumer's explanation, does not appear to sufficiently limit the risk that lenders will assert that consumers share housing even when they do not.

Thus, we urge the following:

- Rental housing should generally be required to be verified using verification evidence.
- In the limited circumstances when verification evidence is not available, the greater of a reliable locality-based proxy or borrower statement should be used.
- To assume shared housing, lenders must obtain verification evidence (such as a lease or lender receipt or checking account activity) or other reliable third party evidence (like a co-tenant statement) of the shared arrangement.
- At the very least, on any loan where there is a presumption of inability to repay, and on a second refinance of a longer-term loan (as discussed in 11), verification evidence of rental housing should be required. Shared housing in these scenarios should be the greater of that indicated by reliable third-party evidence or a reliable locality-based estimate.

In addition to the above, the Bureau should consider providing portfolio-level guardrails that indicate whether (1) housing estimates not based on verification evidence and (2) lender assertions of shared housing, are more likely to be unreasonable, and subjecting portfolios that exceed those guardrails to higher scrutiny.

For example, the 1-year American Census Survey (ACS) by the U.S. Census Bureau provides data on the portion of renters, by income range, who are considered housing-burdened, meaning that their gross rent (rent plus utilities) accounts for more than 30% of their household income. (The 5-year ACS provides this portion by census tract, but not income.) At a $20,000-$35,000, this percentage is 75%; at $35,000-$50,000, it is 43%. The Bureau might provide that if a lender's portfolio shows a lower level of housing burden than the ACS for the census tract, then their housing estimates will be subject to heightened scrutiny. It might consider whether it is appropriate to discount the ACS guardrail figures by a modest percentage.

[363] In full, the Small Dollar Roundtable summary, which the Bureau published with supporting materials, states: "There may be circumstances in which third-part-provided consumer transaction information, from a reliable commercial or governmental database, may be a reasonable substitute for verification of expense against paper-based documents. . . . Any proxy for rent must be geographic market-specific. If direct evidence is available (e.g. rent receipts or bank statements) then that evidence should be used. If it is not available, then a valid, reliable proxy may be used. The determination for rent should be the greater of a reliable proxy as defined by the CFPB or stated housing cost." Small Dollar Roundtable, *supra*.

Portion of households housing-burdened, nationally, by income:[364]

"Burdened" means exceeding 30% of household income	Household Income $20,000-$34,999	Household Income $35,000 to $49,999
% of owners cost burdened	47%	34%
% of renters cost burdened	75%	43%

As mentioned, the ACS reports 5-year data on the portion of income that renters pay in rent.[365] This is not reported by income band, but it may be useful in establishing additional guardrails.[366]

Our discussion of potential guardrails for shared housing is provided in the context of joint obligations generally at section 6.4.2 above.

An additional concern with the housing figure is whether, and to what extent, stated rent may be permitted to be used as the estimate. The Bureau notes that the higher of the stated amount versus estimation method must "generally" be used, as required by section 1041.5(c)(1). We support this approach but question the use of the word "generally" here. The Bureau acknowledges the risk involved in permitting lenders to use a rent lower than either a "reliable record" or the estimation method provides, as it goes on to note:

> "The Bureau recognizes that in some cases the consumer's actual housing expense may be lower than the estimation methodology would suggest but may not be verifiable through documentation. For example, some consumers may live for a period of time rent-free with a friend or relative. However, the Bureau does not believe it is possible to accommodate such situations without permitting lenders to rely solely on the consumer's statement of housing expenses, and for the reasons previously discussed the Bureau believes that doing so would jeopardize the objectives of the proposal."[367]

We fully agree. We reference our opposition to § 1041.5(c)(1), discussed at 6.4.4.1 above, permitting lenders to use consumer stated information to the extent it is deemed consistent with verification evidence. Moreover, consumers who are staying temporarily with friends or a relative may be especially financially distressed, doing so because they lack the funds to pay for their own housing. We urge the Bureau to make explicit that unverified statements asserting housing lower than verified or statistical methods cannot be allowed. And we strongly support the Bureau's conclusion that the rule cannot accommodate situations where a consumer pays less rent than either method above would indicate or suggest without sacrificing the objectives of the rule as a whole.

[364] CRL Tabulation of data from US Census American Community Survey 2015, Table S2503.
[365] ACS Table DP04.
[366] The Bureau may need to consider the extent to which inflation impacts the 5-year data.
[367] 81 Fed. Reg. at 47956.

7. REASONABLE ABILITY-TO-REPAY DETERMINATIONS REQUIRE OBJECTIVELY LOW DEFAULTS, DELINQUENCIES, AND REBORROWING: Comments 5(b)-2.iii. and 9(b)-2.iii.

7.1. Overview.

The CFPB appropriately recognizes that it is not enough for a lender to have procedural requirements when processing a loan application. The lender's underwriting criteria must be continually evaluated and re-evaluated in light of consumers' actual performance. The ultimate goal of this rule is not an up-front checklist, but rather practices that actually result in consumers who are able to repay their loans.

This rule is necessary because high-cost lenders, especially (but not exclusively) those that use leveraged payment mechanisms, do not have the same incentive to ensure their borrowers' ability to repay. The CFPB's research as well as other studies have documented the high default rates of both short-term and longer-term high-cost lenders. This rule will only be successful if those default rates and other indicators that borrowers are struggling with their loans change dramatically.

We are concerned, however, that the CFPB appears to be planning on evaluating loan performance by comparing one lender to other high-cost lenders. That is an inappropriate metric given the predatory track record of this industry.

Instead, the CFPB should be requiring lenders to design their products, policies and practices so that the vast majority of a lender's borrowers actually, in practice, are able to repay their loans while meeting other expenses without reborrowing. This standard should be measured objectively, not relative to the performance of other predatory lenders. It should also be assessed using a number of metrics that indicate high numbers of struggling borrowers.

First, the CFPB should scrutinize closely any lender that has default rates above a threshold rate; we recommend 10%. The standard should be 5% or even lower for auto title loans and payroll deduction loans, which have *extraordinarily* little incentive to determine ability-to-repay,[368] and inflict especially severe harm upon default.

Second, if a lender's default rates exceed those levels—and even if they do not—the CFPB should consider a variety of factors to assess whether the lender is failing to make reasonable determinations of ability-to-repay. These factors include rates of late payments and delinquencies, failed payments, late payments, reborrowing, and debt collection practices, as well as uncontrollable events like unusually deep and unforeseen recessions. Loans with large payments relative to income should also be scrutinized. Both the level of unaffordable loans and the harm from those loans, measured by the cost of the loan and the lender's debt collection practices, should be factors in assessing whether the lender is engaging unfair, deceptive or abusive practices.

7.2. The Reasonableness of Ability-to-Repay Determinations Should Not Be Measured Based on Loan Performance Compared to Similar Loans to Similarly Situated Consumers: Comment 5(b)-4.ii.B and 9(b)-4.ii.B.

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[368] The Bureau recognizes this with respect to vehicle title loans in its discussion of how the value of the collateral in vehicle title loans typically far exceeds the loan amount.

Separate comments in the sections governing reasonable ability-to-repay determinations for both short-term loans (§ 1041.5(b)) and longer-term loans (§ 1041.9(b)) provide:

> "Evidence of whether a lender's determinations of ability to repay are reasonable may include the extent to which the lender's determinations . . . result in rates of delinquency, default, and reborrowing for covered [loans] that are low, equal to, or high, including *in comparison to the rates of other lenders making covered [loans] to similarly situated consumers.*"[369]

Similarly, the comments in both sections also state that an unreasonable method of estimating basic living expenses would be:

> "Setting minimum percentages of income or dollar amounts that, when used in ability-to-repay determinations for covered loans, have yielded high rates of default and reborrowing *relative to rates of default and reborrowing of other lenders making covered loans to similarly situated consumers.*"[370]

We strongly oppose these two comments, which are among the most dangerous parts of this proposal. Both comments strongly imply that the metric for evaluating loan performance is simply not to be the worst of the worst. This approach sets the bar far too low for an industry that has consistently made unaffordable loans, causing substantial harm to consumers. This standard risks providing lenders a cavernous loophole that, history has shown, we should expect them to exploit.

We take full note of the Bureau's discussion of its proposed Comments, which suggests that simply having average delinquency, default or reborrowing rates does not automatically mean that a lender's ability-to-repay determinations are reasonable. This discussion may aim to reduce the likelihood that the standard will be exploited. But we fear that the Bureau's discussion, however cautionary, will not counter formal staff interpretive comments that convey that the basis for comparison is simply whether a lender's loan performance is worse than other high-cost lenders.

The Bureau's discussion notes the following:

- Performance compared to similar loans may only be relevant where the lender's ability-to-repay determination is not facially unreasonable, such as by assuming a clearly insufficient amount needed for basic living expenses.[371] Put differently, even average loan performance does not excuse an unreasonable residual income analysis.

- There are factors that would make loan performance not necessarily indicative of the quality of an ability-to-repay determination. On one hand, the Bureau notes that these factors include a continual opportunity to work, willingness to repay, and financial management on the part of the consumer. On the other hand, the Bureau observes that the leveraged payment mechanism or vehicle title may result in repayment even when the loan is unaffordable, causing harm not evidenced by loan performance or reborrowing. We note that only the second of these two observations helps to contain the damage the Comment poses. We also caution that evidence suggests that the second scenario (repayment despite unaffordability) is

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369 Proposed Comment 5(b)-2.iii. and 9(b)-2.iii.B (emphasis added).
370 Proposed Comments 5(b)-4.ii.B and 9(b)-4.ii.B (emphasis added).
371 81 Fed. Reg. at 47948.

far more likely. The Bureau notes elsewhere in discussion that it believes unwillingness to repay is rare; by contrast, repayment despite unaffordability of the loan is a basic element of the business model.

- Loan performance comparisons would not be sole basis for determining whether a lender complies with the ability-to-repay determinations. For example, the Bureau notes:
  - one lender's default rates may be lower because of aggressive debt collection tactics;
  - one lender's default rates may be the same as another's because both lenders' determinations of ability-to-repay are similarly unreasonable.[372]

The Bureau proceeds to explain that, nonetheless, the comparisons among lenders will "provide important evidence that, considered along with other evidence, would facilitate evaluation" of the reasonableness of a lender's ability-to-repay determinations. The Bureau provides two examples:

Example 1: A lender uses estimates of basic living expenses that "initially appear unrealistically low," but loan performance materially better than its peers may help to show that the lender's ability-to-repay determinations are reasonable.

Loan performance should not be used to rebut unrealistically low estimates of basic living expenses. If estimates appear unrealistically low, good loan performance far more likely reflects aggressive debt collection practices or other factors unrelated to sufficiency of residual income rather the notion that one lender's borrowers (considering geography, household size, and income) have remarkably lower basic living expenses than another's.

Example 2: An online lender may have default rates significantly higher than those of peer lenders, but other evidence shows they used similar practices and the high rates resulted from a large number of fraudulent applications.

This suggests that fraud rates are not relevant to a reasonable ability-to-repay determination, when they are, particularly given that first payment defaults may be due to either fraud or inability to repay.[373]

A third, general example provides that if consumers with one lender experience systematically worse rates of delinquency, default, and reborrowing versus other lenders, then that fact may be important evidence of whether the lender's estimates of basic living expenses are unrealistically low. While that is true, we fear the implication of the converse: that average loan performance in an industry with high default, delinquency and reborrowing rates is acceptable when it is not.

The Bureau invites comment on whether and how loan performance should be factored into an assessment of compliance with the ability-to-repay determinations, including whether the Bureau should specify thresholds which presumptively or conclusively establish compliance or non-compliance and, if so, how they should be determined.

We strongly oppose any comments or other indication in the proposed rule that the standard of

[372] 81 Fed. Reg. at 47948.

[373] In addition, as discussed in section 7.6 below, even true fraud harms consumers because it may be the result of identity theft and result in debt collection against the wrong person.

comparison for lenders' loan performance is that of other high-cost lenders, as we discuss in detail below. We also oppose a comparison to "similarly situated consumers," which is also problematic. As discussed earlier, lenders making high-cost loans, whether covered or non-covered, often put consumers with lower incomes and/or lower credit scores into high-cost products they cannot afford. These should not be made benchmarks for a reasonable ability-to-repay determination.

These provisions put the integrity of the entire rule at risk. Instead, we urge that the Bureau provide that a reasonable determination require levels of reborrowing, delinquencies, and defaults that are low in the absolute, and subject higher rates to heightened scrutiny.

7.3. Lenders Making Covered Loans Have Extraordinarily High Default Rates Today, With Insufficient Incentive to Reduce Them Going Forward.

The Bureau finds the following default rates for covered loans:

Short-term payday loans	20% at the loan sequence level
Short-term car title loans	33% at the loan sequence level
Longer-term payday loans	38% at the loan sequence level, 24% at the loan level
Longer-term vehicle title loans	31% at the loan sequence level; 22% at the loan level

As discussed in the following section, these rates are far above those of lower-cost lenders and mainstream credit markets, even on unsecured credit cards for borrowers with comparable credit scores. Even under the rule, lenders will continue to lack sufficient business incentive to lower default rates to appropriate levels.

The Bureau appropriately refers to these default rates as "high." The Bureau observes the following in its discussion of the abusiveness standard:

> "[L]enders are of course aware of the high default rates on their loans and know that they have not made any attempt to match the payment terms they offer to the financial capacity of the consumer, so that there is a likelihood that the payments will prove unaffordable for a given consumer . . . Lenders also know that the defining loan features will enable the lender to extract payment from the consumer even if the payment exceeds the consumer's ability to repay and leaves her in financial distress."[374]

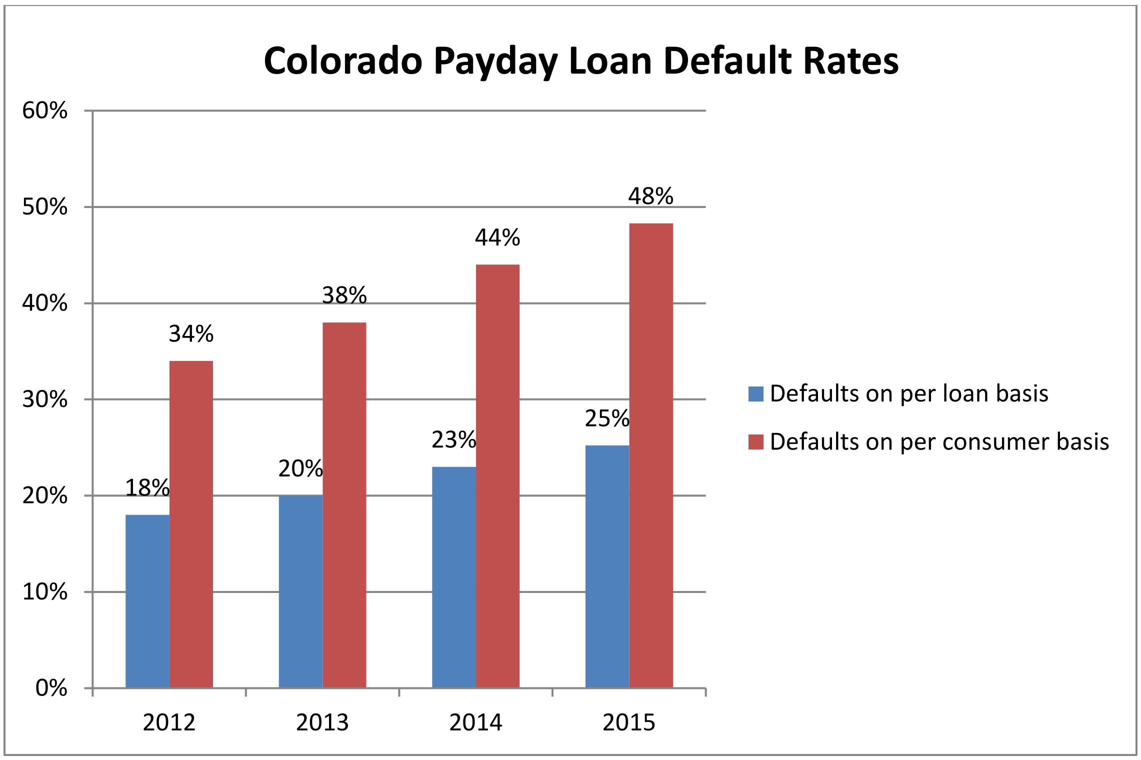
Default rates are high and appear to be rising in Colorado, despite laws that make that state's payday installment loans somewhat less dangerous than the high-cost installment loans in some other states. In Colorado, high-cost installment loans can be no more than $500 and must be at least six months in length, with rates capped.[375] These features push down payment size; one study puts the average

[374] 81 Fed. Reg. at 47999; *see also id.* 47989 "When a loan has a high total cost of credit, the total revenue to the lender, relative to the loan principal, enables the lender to profit from a loan, even if the consumer ultimately defaults on the loan…. Moreover, even if defaulted loans are not themselves profitable, lenders can weather such losses when the performing loans are generating such high returns.").

[375] Those limitations do not apply to traditional installment loans made under the state's 36% rate cap.

payment-to-income (PTI) ratio at roughly 5%,[376] although there are no legal limits on PTI and some borrowers may pay far more. (In contrast, an industry study of loans around the country found that the average PTI of payday installment loans is 11%.[377]) Yet Colorado has no requirement that lenders consider the borrower's ability to repay, and the data consistently show that the loans are still quite unaffordable.

Colorado lists the number of "defaulted"[378] loans and the total number of loans each year in its annual reports, which compile the unaudited reports submitted by licensed payday installment lenders. Those reports have shown the percentage of defaulted loans rising steadily from 18% in 2012 to 25% in 2015. Those reports also list the number of individual consumers to whom payday installment loans have been made,[379] making it possible to calculate a per-consumer default rate. The per-consumer default rate has also been rising, from 34% in 2012 to 48% in 2015.



These "defaults" may not reflect default rates as generally understood. The state does not have a standard definition of "default," and some lenders could be reporting consumers who are merely late as "defaulted." It is also possible that the same consumer may be reported as "defaulted" more than once, i.e. if the consumer was late more than once, or was late on more than one loan in a string of refinanced loans. (Refinancing rates are quite high in Colorado, as discussed in section 11.4.1.2 below.)

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376 Pew Charitable Trusts, Payday Lending in America: Policy Solutions (Oct. 2013), http://www.pewtrusts.org/~/media/legacy/uploadedfiles/pcs_assets/2013/pewpaydaypolicysolutionsoct2013pdf.pdf.

377 Beales/Goel, supra, at 27.

378 As discussed below, these defaults may not actually be defaults as traditionally understood.

379 The number of consumers is overstated to the extent that consumers have loans from more than one company. Thus, the per-consumer default rate may be understated.

Nonetheless, the trend of an increasing indicator of distress—during a time period when the economy has been improving—is notable.

Another measure of distressed Colorado borrowers is charge-off rates—i.e., the percentage of dollars loaned that are charged off each year. Given the high rate of refinancing, it is important not to double count refinanced loans when calculating charge-off rates. Taking into account the average number of loans per consumer as reflected in the annual reports,[380] the charge-off rates in Colorado have been fairly steady at about 20%.[381] However, per-consumer default rates are likely higher than that, because most consumers make some payments before defaulting. That is, the 20% charge-off figure indicates that *more* than 1 in 5 Colorado consumers actually defaulted,[382] while far more are struggling. Adjusting for refinancing rates, about 32% of balances are on loans that either have been charged off or have defaulted but have not yet been charged off.[383] Here again, the percentage of consumers in distress is likely higher—likely well more than a third of borrowers.

A different Colorado report, compiled from examination information and an analysis of a subset of loans, also gives indicators of distress.[384] The latest report shows that 72% of the loans transacted in 2015 were paid in full within six months. Another 18% of loans were "open" at the six-month mark; it is not clear if that is because the loan term was longer or for other reasons. A further 4.47% of loans had been charged off, and 4.9% were open in some state of delinquency. At a minimum, that indicates 10% of loans were in distress. With 3.29 loans on average per consumer in 2015, the data indicate that the per-consumer distress rate is above 30%.

Colorado payday lenders have also become more adept at keeping borrowers in long-term debt. Refinancing rates are discussed in section 11.4.1.2 below.

In short, even when they are limited to smaller loans and spread the payments on those loans out for six months, payday lenders in Colorado, who do not underwrite for ability-to-repay, are still making unaffordable loans. Metrics of distress like these should lead to the conclusion that a lender is not making a reasonable ability-to-repay determination, whether or not they are similar to those of other high-cost lenders.

While we appreciate that the rule will prevent some of the most egregious lender practices, including unceasing debiting of a borrower's account, two critical underlying realities will not change. Extraordinarily high interest rates like those on covered loans will continue to permit lenders to make a profit even off of loans that eventually default.[385] And lenders' use of a leveraged payment mechanism

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[380] The state's annual reports, which summarize unaudited lender reports, reflect fewer loans per consumer than the state's Demographic and Statistical reports, based on examinations.

[381] After dividing the loan volume by the average number of loans per consumer, we calculate that the follow percentage of dollars were charged off each year: 24% in 2011; 17.8% in 2012; 21.7% in 2013; 20.3% in 2014; 19.4% in 2015.

[382] For example, if a lender made five $100 loans and one defaulted after paying $50, the charge-off rate would be 10% ($50/$500 dollars charged off) but the per-consumer default rate would be 20% (1/5 consumers).

[383] This figure was calculated from the Colorado 2015 Demographic and Statistical Information by taking (1) the dollar value of defaulted loans minus the dollar value of defaulted but recovered loans (to get the dollar value of truly defaulted loans) and (2) dividing it by the total dollar value of all loans divided by the number of loans per consumer (to adjust for multiple loans per consumer).

[384] Colorado 2015 Demographic and Statistical Information at 18-19.

[385] See Misaligned Incentives.

or vehicle title will continue to compound the dynamic, enabling them to prevent many unaffordable loans from defaulting and to collect more unaffordable payments than they otherwise would before default ultimately occurs.

Indeed, one high-cost lender with extremely high charge-off rates has stated that it will not be significantly impacted by the rules as currently designed. [386] This should strongly signal that the rules must be designed better.

7.4. The Default Rates of Covered Lenders Are Far Above Those of Lower-Cost Lenders and Mainstream Credit Markets, Even for Loans to Borrowers With Comparable Credit Scores.

The default rates for covered loans are dramatically higher than those of lenders that do not charge triple-digit rates. While it is not possible to make a perfect apples-to-apples comparison between the default rates of covered lenders and those of other credit markets, the available data show a clear disparity.

There is no uniform method of reporting default rates. (Indeed, obtaining standardized and public data will be important to evaluation of covered lenders.) The default rates for covered loans discussed above tend to be either a percentage of loans or a percentage of loan sequences (a proxy for a per-consumer default rate). In contrast, mainstream credit markets tend to report charge-off rates—a term that we will use to refer to the percent of dollars charged off compared to dollars outstanding at a given time.[387] That is also the method that the CFPB has proposed for loans made under proposed § 1041.12 to evaluate whether the default rates are below 5%.

Charge-off rates appear to be roughly comparable to per-consumer or sequence level default rates. Calculating charge-off rates as a percent of credit outstanding avoids the problem of double counting a consumer who has refinanced or rolled over a loan, because only the latest loan is outstanding at any given time. Charge-off rates may be lower than a per-consumer default rate because consumers typically make some payments before defaulting, and thus less than 100% of the loan is usually charged off. On the other hand, if defaults are concentrated among larger loans with large charge-offs, then a per-consumer default rate could be lower than the charge-off rate. As shown in the 2014 California data displayed in the chart below, for some lenders the percentage of dollars charged off is higher than the percentage of loans charged off, and for others it is the opposite.[388]

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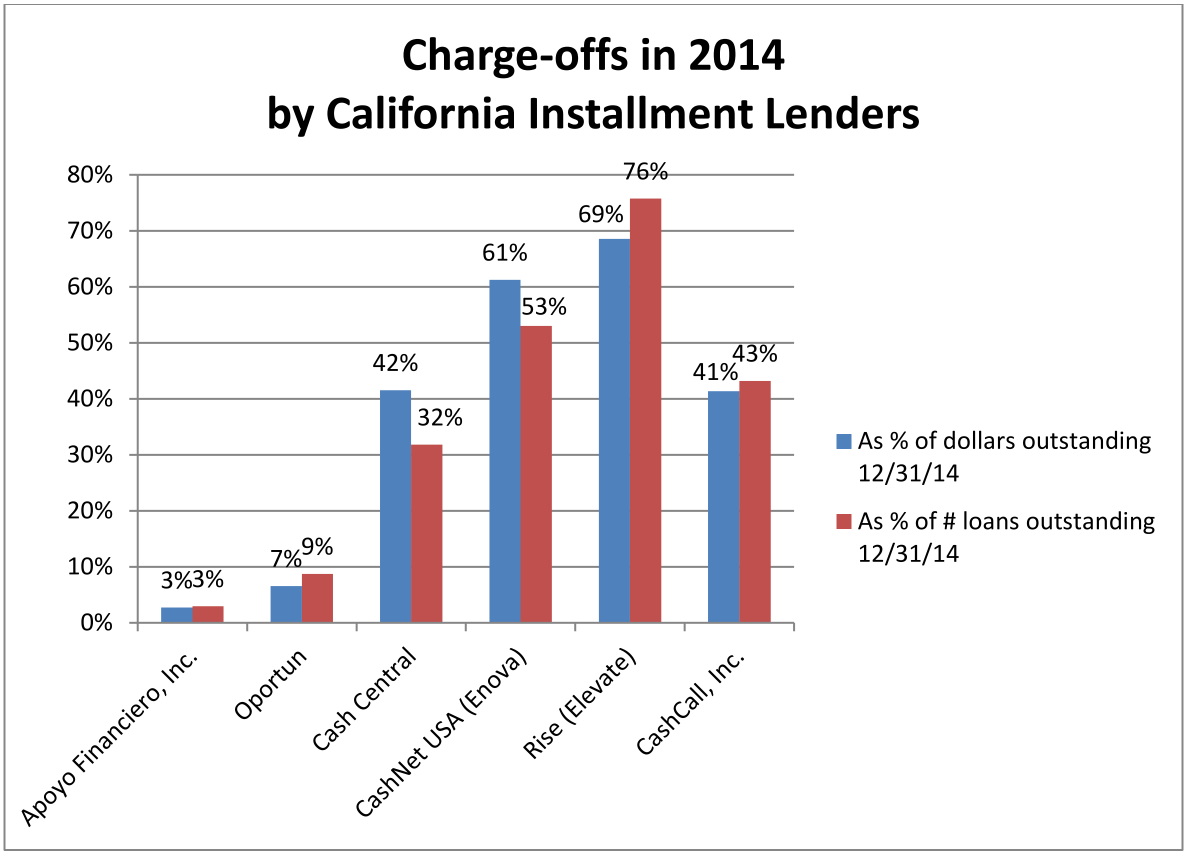
[386] Elevate's net charge-offs were 51% of revenues in 2014. Elevate SEC Form S-1 at 22. While Elevate noted that this charge-off ratio could go down with a more seasoned portfolio, the company stated that "we do not intend to drive down this ratio significantly below our historical ratios and would instead seek to offer our existing products to a broader new customer base to drive additional revenues." Id. at 78; see also 81 Fed. Reg. at 47886 & n. 246 (discussing Bureau calculation that Elevate's net charge-offs were over 50% of average balances).

[387] The fourth method used by NCLC in calculating California default rates (% of dollars based on loans outstanding at the end of 2014) is the closest to the charge-off rates discussed in this section. However, caution is required because of anomalies in the California data.

[388] As discussed earlier, the charge-off rates shown are based on unaudited data, and they also may reflect inaccurate charge-off rates due to anomalies such as rising or falling loan volumes or loans that were paid off before year-end.



While caution is thus required before making direct comparisons between different metrics of defaults and charge-offs, the overall disparities between high-cost lenders and lower-cost lenders and mainstream credit markets is quite clear, even compared to other lenders making loans to borrowers with subprime credit scores.

Credit card rates provide another point of comparison. The national credit card charge-off rate was only 3% in 2014.[389] Even at its peak during the Great Recession, the credit card charge-off rate was 10.8%.[390]

While most credit card borrowers have higher credit scores than do payday loan borrowers, credit cards are generally unsecured. They do not require a leveraged payment mechanism or vehicle title, and even those repaying via preauthorized payment likely do not have those payments tied to payday. Thus, if a borrower cannot afford a credit card payment, he will default.

A survey provided to the CFPB found that the charge-off rates for community bank loans that would be covered by the proposed rule are between 0.54% and 1.02%.[391] The loans in the survey have a total cost of credit above 36%, are under $1,000, and are repaid automatically. Another trade association

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[389] Averaging the nationally, seasonally adjusted charge-off rates for each of the four quarters in 2014, the national credit card charge-off rate was 3.16%. Board of Governors of the Federal Reserve System, Charge-Off and Delinquency Rates on Loans and Leases at Commercial Banks, *available at* http://www.federalreserve.gov/releases/chargeoff/chgallsa.htm.

[390] *Id.* (second quarter of 2010).

[391] 81 Fed. Reg. at 38045 n.756 (citing ICBA Letter Oct. 6, 2015).

survey of small dollar loans by banks of all sizes found that a third had no charge-offs at all. The remainder had charge-offs of only about 3%.[392]

The NCUA estimates that charge-off rate for loans under NCUA's Payday Loan Alternative program is 7.5%.[393] Notably, these loans are often made to subprime borrowers without detailed underwriting. As with credit cards, many of these loans do not use the same coercive repayment devices that payday installment loans do.

A survey by North Carolina Office of the Commissioner of Banks of lenders operating under the state's Consumer Finance Act found charge-off rates of 5.2% to 8.6%,[394] with some lenders having negligible or no charge-offs.[395] The average FICO score of consumer finance company borrowers was 578.[396] For all lenders, the average interest rate charged was 24%.[397]

A report on loans made under California's small dollar loan pilot program showed that only 3.9% of loans made in 2014 were 60 or more days delinquent.[398] Nearly two-thirds of the loans were made in lower- or moderate-income neighborhoods, with most of the remainder in middle-income neighborhoods. As shown in the graph above, we calculate charge-off rates of 2% to 9% for Oportun and Apoyo Financiero, two lenders that make loans under the pilot program at much lower cost than the other lenders graphed.

Thus, charge-offs are generally in the single-digits for lower-cost lenders. Charge-off rates are in that range even for lenders that serve consumers with subprime credit scores.

7.5. Default Rates Should Be Low in the Absolute, With Rates Above 10% on a Per-Consumer Basis (and Lower for Auto Title and Payroll Deduction) Receiving Heightened Scrutiny.

Instead of merely comparing the performance of covered lenders to each other, the CFPB should identify a rate for defaults and other indicators of inability to repay above which ability-to-repay determinations should be more highly scrutinized. We recommend a default rate threshold of 10% on a per-consumer basis for short-term and longer-term payday loans. We urge a lower default rate—5% or perhaps even lower—for auto title and payroll deduction loans in light of the especially poor incentives to determine ability-to-repay and the severe harm resulting from default. As discussed in section 7.6 below, exceeding these target default rates would not automatically result in a violation of the rules. But it would trigger heightened scrutiny of the lender's practices to determine whether the lender's ability-to-repay determinations are unreasonable.

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392 *Id.* (citing ABA Letter Dec. 1, 2015).
393 CFPB Payday NPR at 617-18.
394 North Carolina Office of the Commissioner of Banks, The Consumer Finance Act: Report and Recommendations to the 2011 General Assembly at 40 (Feb. 2011), available at http://ccc.sites.unc.edu/files/2013/02/NCCOB.CFA_.Report.pdf.
395 *Id.* at 48.
396 *Id.* at at 19 (summarizing 2009 report by Equifax covering the prior seven years).
397 *Id.* 34.
398 Calif. Dept. of Business Oversight, Report of Activity Under Small Dollar Loan Pilot Programs at 4 (June 2015), http://www.dbo.ca.gov/Licensees/Finance_Lenders/pdf/Pilot%20Program%20Report%202015%20Final.pdf.

Our proposed threshold is double the 5% charge-off rate that the CFPB has deemed safe enough to exempt lenders making loans at 36% interest plus an origination fee from the ability-to-repay requirements.

A 10% default rate target is also appropriate in light of the CFPB's appropriate concern for the harm caused by lending markets that result in 20% or more of consumers defaulting. Among the research that the CFPB cites in support of its conclusion that covered loans "often prove unaffordable to consumers, leading to significant consumer harm," the CFPB notes that "[p]ayday borrowers end up in default 20 percent of the time, either on their first loan or after reborrowing," and that "[o]ne-in-five single-payment auto title loan borrowers have their vehicle seized by the lender."[399] If the CFPB hopes to make a significant improvement in these markets, it must signal that the 20% default rate must be substantially reduced. Setting a target default rate of 10% achieves that goal.

A 10% default rate is significantly higher than the defaults that are considered appropriate or common in mainstream credit markets. As discussed in the previous section, lower-cost lenders tend to have charge-off rates in the low- to mid-single digits.

The combination of a high interest rate and a leveraged payment mechanism on covered loans makes it all the more important to limit their default rates. At higher interest rates, there is a perverse combination of greater consumer injury and lower lender pain from a default. As discussed earlier, lenders may even profit on loans that default, or have minimal losses, making them insensitive to consumer pain.[400]

In addition, most prime lenders do not rely on a leveraged payment mechanism as a significant component of their underwriting model. That repayment device makes an enormous difference. It increases the injury from unaffordable loans and substantially lowers the default rate that high-cost lenders would otherwise experience if they did not have the means to coerce repayment of unaffordable loans.

Due to the repayment device, the defaults on covered loans are only the tip of the iceberg of borrower harm. Many consumers who cannot afford the loans will struggle and be harmed even if they do not end up defaulting. Loan payments may be made, leaving payments for other essential obligations or expenses unpaid. Loan payments may trigger overdrafts and overdraft fees. Loan payments may initially bounce (generating a nonsufficient funds fee) but then go through when re-presented. Consumers may lose their bank accounts and be unable to get another one. Consumers who get behind may face aggressive debt collection practices and ultimately pay even though their ability to meet other expenses is further compromised. Consumers may also reborrow or refinance, disguising default rates, increasing costs, and prolonging their pain.

The CFPB appropriately found that short-term payday borrowers experience harm even if they do not default. "Even borrowers who eventually pay off their loans may incur penalty fees, late fees, or overdraft fees along the way, and after repaying may find themselves struggling to pay other bills or

[399] CFPB, Payday Loans, Auto Title Loans, And High-Cost Installment Loans: Highlights From CFPB Research at 1, 2, 3 (June 2, 2016), http://files.consumerfinance.gov/f/documents/Payday_Loans_Highlights_From_CFPB_Research.pdf.

[400] *See* Lauren Saunders et al., NCLC, Misaligned Incentives: Why High-Rate Lenders Want Borrowers Who Will Default (July 2016), http://www.nclc.org/media-center/report-why-high-rate-installment-lenders.html.

meet their basic living expenses."[401] Other harms the CFPB notes are that the loans do not function as marketed, there are very high reborrowing rates, and consumers do not expect lengthy loan sequences.

Similarly, borrowers of unaffordable longer-term loans also experience harm even if they do not default. As the CFPB observed:

> "Prior to reaching the point of default, borrowers are exposed to a variety of harms that are substantially increased in magnitude because of the leveraged payment mechanism or vehicle security relative to similar loans without these features . . . . In addition to the harms that result from default, lender use of leveraged payment mechanisms can reduce borrowers' control over their own funds by essentially prioritizing repayment of the loan over payment of the borrower's other important obligations and expenses, which can result in late fees under those obligations and other negative consequences, such as cut-off of utilities."[402]

The default rate, the Bureau is clear, represents only a subset of injured borrowers: "Some of these consumers may repay the entire loan at the expense of suffering adverse consequences in their ability to keep up with other obligations or meet basic living expenses."[403]

As with shorter-term loans, refinancing of longer-term loans causes harm even if the borrower does not default. Refinancings of high-cost loans, particularly those done before the initial loan has been substantially repaid, are strong evidence that the borrower did not have the ability to repay the initial loan. As discussed in section 11 below, refinancing increases the overall cost of borrowing while also increasing the risk of overdraft fees, nonsufficient funds fees, late fees, and difficulty paying other expenses. And as with rollovers of short-term loans, longer-term loans that are refinanced (especially repeatedly) do not function as marketed and consumers likely do not anticipate the time they will be in debt.

Thus, for lenders with a leveraged payment mechanism, a 10% default rate translates into far more than 10% of consumers who struggle with the ability to repay their loans. The CFPB found that 20% of short-term payday borrowers default at some point, but an additional 64% renew their loans one or more times without defaulting. Thus, as many as 84% of borrowers are unable to repay their loans without reborrowing, four times the number who default.

Similar numbers are not available for longer-term loans,[404] but one indication of the ratio between defaulting consumers and struggling consumers comes from data under California's small dollar loan pilot project. A report found that while only 3.9% of loans made in 2014 were delinquent for 60 days or more, 22.5% were delinquent for seven days to 29 days, and 7.3% were delinquent for 30 days to 59 days.[405]

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[401] 81 Fed. Reg. at 47920.
[402] 81 Fed. Reg. at 47987.
[403] 81 Fed. Reg. at 47988.
[404] The CFPB found that 37% of payday installment loans are refinanced, and 38% of loan sequences default. Supplemental Findings at 15. But these numbers cannot be added together because the refinanced loans may have defaulted, and the loan sequences include loans that were not refinanced. In addition, the refinancing rate may double-count consumers who refinance more than once.
[405] Calif. Dept. of Business Oversight, Report of Activity Under Small Dollar Loan Pilot Programs at 4 (June 2015), http://www.dbo.ca.gov/Licensees/Finance_Lenders/pdf/Pilot%20Program%20Report%202015%20Final.pdf.

Assuming that the 60-day delinquency group is the equivalent of defaults, the larger group of struggling consumers was more than eight times higher than the number of defaults. Even if we assume that all of the consumers who are 30 or more days delinquent will also default, the total number of struggling consumers is still more than triple the number that default. And the leveraged payment mechanism results in harm even for consumers who do not pay late.

Thus, even if covered lenders have only a 10% default rate, it is likely that 30% of borrowers or more will be trapped in unaffordable high-cost loans. That is already a very significant proportion, and the share of unaffordable loans gets even higher as the default rate goes up. Thus, any lender with a default rate in excess of 10% should face close scrutiny.

However, the target default rate should be far lower for payroll deduction loans and auto title loans. Loans that are secured by payroll deduction almost never default, regardless of whether or not they are affordable. Unless the borrower loses her job or has her income cut dramatically, the loan will be repaid. The loan is always the very first expense paid, and there is no possibility of the money being spent first and the payment bouncing. Nor, we understand, can consumers revoke authorization for automatic payments or stop payment with the bank.[406] Thus, default rates are not a good measure of the affordability of payroll deduction loans. In addition, the injury from an unaffordable payroll deduction loan is more severe than the injury from a loan secured by ACH or post-dated check, because the consumer has less ability to stop the payment or prioritize other expenses.

For similar reasons, the target default rate for auto title loans should also be well below 10%. The consumer injury from losing a car is far more dramatic than the injury from simply defaulting on another type of loan. The consumer may lose her job, as well as the transportation that she needs for getting her children to school, to medical appointments and for other family needs. The fear of losing her job also makes the repayment mechanism especially coercive. As with a payroll deduction loan, the consumer cannot escape the payment mechanism. Auto title lenders are also less sensitive to the impact of defaults, and have less incentive to make reasonable ability-to-repay determinations, because the car is typically worth far more than the loan and the lender may come out even or ahead.

The severity of the injury to consumers is one of the measures of whether a practice is unfair. A practice can be unfair if it inflicts severe injury on only a small number of consumers—say, five percent of vehicle title loan borrowers. For that reason, the tolerance for defaults of auto title or payroll deduction loans should be especially low. Thus, any auto title or payroll deduction lender that has defaults of 5% or potentially even less should face scrutiny.

7.5.1. The CFPB should measure the cumulative cohort default rate or a comparable charge-off rate.

When discussing default rates, the question arises how that default rate should be calculated. Rates can be calculated per loan or per consumer; on an annual basis or on a cumulative basis; or as a percent of loans or of dollars.

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[406] We understand that the wage assignment is typically not revocable. But even if it is technically revocable, that is not an adequate protection.

To the extent possible, the CFPB should attempt to determine the cumulative cohort, per-consumer default rate, taking into account any reborrowing. That is, for a given group of borrowers, following them to the end where they either default or repay the loan sequence without reborrowing, what share of them ultimately default, either on the original loan or after refinancing?[407] That is the best measure of what proportion of consumers ultimately default.

Clearly, focusing on a per-consumer default rate is essential. As the CFPB is well aware, reborrowing and refinancing can dramatically mask default rates. Per-loan default rates are artificially low and do not provide information on the proportion of consumers who ultimately default. In addition, serial refinancing of unaffordable loans poses substantial risk of harm to borrowers, whether there are upfront non-refundable fees or not; see section 11 for further.

If cumulative cohort default rates are too difficult to track uniformly across different lenders, then the CFPB should use an annualized charge-off rate (dollars charged off as a percent of dollars outstanding) calculated as the CFPB has proposed to evaluate for loans made under § 1041.12. In the California data that we analyzed for lenders making loans that were generally under two years in length, there was rough correspondence between the percent of loans charged off and the percent of dollars charged off. As noted above, as long as the denominator is loans outstanding at a given time (rather than total dollars of credit extended throughout the year), charge-off rates generally avoid double counting consumers who reborrow. However, the percentage of dollars charged off is generally lower than the percentage of consumers who default because most defaults make some payments before defaulting.[408] Thus, while we recommend a 10% default rate on a per-consumer basis, the CFPB may consider providing that a lower charge-off rate threshold trigger heightened scrutiny. The CFPB should also keep an eye on the cumulative cohort per-consumer default rate for longer loans, where the full extent of defaults may not show up in annual charge-off rates.

7.6. A Number of Factors Should Influence Whether an Elevated Default Rate Reflects Unreasonable Ability-to-Repay Determinations and Unfair, Deceptive or Abusive Practices.

We are urging only that the CFPB focus heightened scrutiny on lenders that have a default rate higher than 10%, not that it make a 10.1% default rate an automatic violation of the rules. If a lender exceeds that rate, a number of other factors would influence whether the CFPB concludes that the lender is making unreasonable ability-to-repay determinations or engaging in unfair, deceptive or abusive practices. The following factors—and especially the cumulative amount of consumer harm—are important to the Bureau's evaluation. We also note that the Bureau should always evaluate these factors, even if it does not adopt our suggestion to apply heightened scrutiny to portfolios with defaults over 10%.

The CFPB should assess four types of factors: by how much did the default rate exceed the target; the impact of unexpected events or unexpected results from initially reasonable ability-to-repay determinations; other indicators beyond defaults showing that large numbers of consumers are struggling; and the extent of consumer injury from defaults. As discussed in the following section 7.7, the Bureau should also scrutinize loans with high payments relative to borrowers' incomes.

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[407] By "refinancing," we are referring both to loans made within 30 (or, ideally, 60) days of a balloon payment, as well as loans that are repaid early and reborrowed within 30 days.

[408] See example in footnote 382, *supra.*

First, of course, it matters whether the default rate is 10.1% or 20%. The factors listed below will carry more weight when the default rate only slightly exceeds the target than if it is way off.

Second, the CFPB should look beyond default rates to other indicators that consumers who do not default nonetheless do not have the ability to repay their loans without reborrowing. The CFPB should monitor the percent of loans with these indicators, among others:

- Failed payments;
- Late payments, including how late;
- Requests for forbearance;
- Reborrowing rates, including at what stage consumers reborrow and whether presumptions of inability to repay (or exceptions to those presumptions) have been triggered;
- The extent and aggressiveness of the lender's debt collection practices;
- Any indications that consumers are incurring overdraft fees or having trouble paying other expenses. (The CFPB should conduct further research on this point.)

Third, the extent of consumer injury (both from a default and from consequences before default) is an important factor in assessing whether a lender that has an elevated default rate is engaging in unfair, deceptive or abusive practices. Several factors influence injury, including:

- *The interest rate and whether the lender stops charging interest at some point*. Debt compounds more slowly at lower rates than at higher rates. It can also grow extraordinarily larger than original principal when lenders continue charging interest post-default or post-judgment.
- *Late fees*. Consumers who struggle to pay on time are injured more by lenders that pile on late fees.
- *Debt collection practices*. A credit union that makes minimal efforts to collect on a defaulted loan is very different from a lender that hounds the consumer mercilessly.
- *Whether the lender sells or sues on its debt*. Consumers who are exposed to debt buyers or wage garnishments suffer more injury than those whose loans are simply charged off with no further activity.

Plausible indications that many of the defaults are the result of consumer fraud rather than inability to repay are also a factor in whether the default causes consumer injury. For example, the CFPB may wish to consider whether there was a spike in fraud losses—that the lender has taken steps to address—when the lender began marketing through a new channel. However, the CFPB must be careful to limit reliance on this factor, and "fraud" losses should not be excluded from the default rate. A first payment default may reflect either fraud or inability to repay. Moreover, even fraud losses can impose consumer injury if identity theft is involved, because the consumer whose identity was stolen suffers from the negative credit report and debt collection efforts.

Fourth, the CFPB should consider any reasons why default rates were unexpectedly high despite reasonable efforts to underwrite for ability to repay. Reasons that the lender cannot control, such as an unusually deep and unforeseen recession, would get the most deference. But the CFPB may also consider other reasons that are consistent with a lender that is genuinely attempting to comply. A lender newly entering the market might not have enough experience to solidly predict loan performance.

The CFPB must be careful not to give lenders too much leeway to experiment or come up with excuses. It must insist on ability-to-repay determinations that are reasonable at the time; on reasonable efforts to predict default rates; and on a commitment to make changes if something goes awry. But the Bureau need not insist on perfection or penalize reasonable efforts that do not work out as planned.

Finally, all of these factors should also influence the appropriate course of action if a lender's default rates exceed the target rate. The CFPB should expect the lender to take steps to reduce the default rate. It might also require the lender to mitigate the injury to consumers by refunding late fees, waiving back interest, or reducing loan principal. And in appropriate circumstances, enforcement action may be warranted.

7.7. The CFPB Should Scrutinize Loans with Large Payments.

As discussed in section 12.8 below, we strongly support the CFPB's approach not to exempt certain loans with a payment-to-income (PTI) ratio of 5% or lower. Assessment of ability-to-repay requires consideration of expenses. Substantial harm will not be prevented by permitting lenders to assume that a fixed ratio of income is free and available, regardless of how low the consumer's income is, how high expenses are, or how much difficulty the consumer is already having making ends meet.

While all loans should be subject to income and expense-based underwriting, we do agree that payment size matters. All things being equal, a loan that takes a large percentage of a borrower's income is more likely to be unaffordable than one that takes a low share. We share the concern of The Pew Charitable Trusts that permitting too much discretion in the ability-to-repay determination risks sanctioning as "affordable" loans with unreasonably large payments.

We urge the CFPB to closely scrutinize lenders that purport to comply with the ability-to-repay requirements but make loans with high PTIs. Reviewing not just the procedural ability-to-repay requirements but also the results of that process is essential, especially given the potential weaknesses in the ability-to-repay requirements. Further research on what PTIs are presumptively unreasonable would also be useful.

7.8. High Default Rates Should Not Be Tolerated in the Name of Access to Credit.

The payday industry will claim that setting a 10% default rate target will cut off access to credit. But it is appropriate to limit unaffordable credit. As discussed above, the default rate is the tip of the iceberg of unaffordable loans, especially when lenders use a leveraged payment mechanism. Even with a 10% default rate, a substantial proportion of borrowers will struggle to repay their loans. When the default rate gets even higher, the harm to large numbers of borrowers outweighs any benefit from the credit for others, and it is appropriate to ask the lender to take steps to reduce that harm. Setting a default rate threshold will encourage lenders to improve their underwriting to screen out borrowers who cannot repay. They will have every incentive to continue lending to those who can.

8. PROPOSED ANTI-FLIPPING PROVISIONS COULD STILL PERMIT HARMFUL LONG-TERM INDEBTEDNESS IN "SHORT-TERM" LOANS: § 1041.6.

8.1. Overview.

Section 1041.6 establishes additional requirements lenders must comply with in order for an ability-to-repay determination to be reasonable. We strongly support the Bureau's position that additional protections are needed to augment the basic ability-to-repay determination. We agree with the Bureau's interpretation of its data showing high levels of reborrowing shortly following a short-term covered loan: that the most likely explanation is that the borrower did not have the ability to repay the loan while meeting other major financial obligations and basic living expenses.[409] We further agree that a presumptions framework is a reasonable way to structure addressing repeat loans. And we strongly support the Bureau's conclusion that a disclosure-based approach would not provide sufficient protection.[410]

At the same time, the proposed rule viewed as a whole would permit lenders to put borrowers into more than ten short-term loans in twelve months without ever triggering a presumption of unaffordability. This is largely due to two significant shortcomings in the provisions of § 1041.6 addressing repeat lending: (1) the lack of a limit on the cumulative days of annual indebtedness, which would be supported by federal and state precedent; and (2) the use of only 30 days rather than 60 days as the relevant time period determining what constitutes a renewal/reborrowing/refinance.

Thus our highest priority recommendations for this section are

- requiring a cumulative indebtedness limit of 90 days indebtedness in "short-term loans" in twelve months, and
- providing any loan within 60 days of the prior loan, rather than 30 days, be part of the same loan sequence.

We address these two priorities first in the discussion below.

In addition, we urge the following:

- "Outstanding loan" should be defined more broadly to ensure that they trigger presumptions when appropriate. It should exclude only loans with no payments or collections activity for 365 days;
- The exception from a presumption of unaffordability for a loan with smaller payments should be eliminated;
- The definition of a balloon payment should include any payment 10%, not 100%, large than another payment;
- The presumption of unaffordability during an unaffordable outstanding loan should be broadened, including prohibiting lenders from making a loan if their own loan to the borrower is in default (i.e., +120 days delinquent). In addition, the rule must ensure that loans from the same or affiliate service providers are covered by this provision;
- The presumption of unaffordability should only be rebuttable with verification evidence;

[409] 81 Fed. Reg. at 47959.
[410] 81 Fed. Reg. at 47959-60, 48149.

- The prohibition after consecutive loans should apply after the second loan instead of the third; be extended from 30 to 90 days; and apply to any combination of balloon-payment loans whether short-term or longer-term;
- The prohibition after a short-term exemption loan should be extended to 60 days;
- Bridge loans should include all non-covered loans and should reset, rather than toll, presumption periods;
- Finally, but importantly, we urge that the proposal close a large loophole that permits flipping through a short-term open-end line of credit. Any advance that must be substantially repaid in full within 45 days should be treated as a new loan subject to short-term closed-end flipping rules.

8.2. Lenders Should Not Be Permitted to Put Borrowers in More Than 90 Days' Worth of "Short-Term" Loans In 12 Months.

The Bureau notes that, in addition to its current approach to § 1041.6, it considered alternatives, including (1) a limit on the number of loans, which it noted could be less complex and more flexible (noting the example of three loans in 120 days for a 15-day loan, with a longer time period for longer loans); (2) cooling-off periods of varying lengths depending on how long the borrower has been in debt; and (3) an indicia approach, where certain factors are indicia of unaffordability, with countervailing factors that might support a determination of ability-to-repay despite those indicia. The Bureau solicits feedback on alternative approaches to addressing reborrowing, including whether it should apply presumptions or a cooling-off period based on a total number of loans or total period of time in debt, as well as how such frameworks would address reborrowing on loans of different lengths.

We urge the Bureau to combine a total days' indebtedness limit of 90 days in 12 months with the general presumptions approach it has proposed. The Bureau notes that it has considered limits based on days' indebtedness, but the example it provides is three 15-day loans within 120 days, or approximately a four-month period. This approach would permit 12 short-term loans in a year, or 135 days' total indebtedness. This is an extremely high number of purportedly short-term loans. In addition, these higher limits have no precedent of which we are aware.

On the other hand, a limit of 90 days' annual indebtedness is rooted in significant precedent, as the Bureau notes in its discussion of this limit in the context of the short-term exemption. Most notably, the FDIC has advised since its 2005 payday loan guidelines that lenders keep borrowers in payday loans for no more than three months' total indebtedness in any 12-month period. This limit, which translates to about six two-week loans annually, is generally consistent with limits of comparable amounts established by other regulators. These include what the Bureau describes as a "supervisory norm" of no more than six loans annually per the OCC/FDIC deposit advance guidance, as well as state limits of eight in Washington and five in Delaware.[411]

The Bureau recognizes the usefulness of, and precedent for, a 90-days' indebtedness limit in the context of the short-term exemption.[412] The Bureau appears to have omitted the 90-day limit for loans made under proposed §1041.5 because those loans, unlike those made under proposed § 1041.7, are subject to an ability-to-repay determination.

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[411] We note that the state limits are not coupled with ability-to-repay requirements and thus leave substantial room for unaffordable loans.

[412] See discussion at section 9.8.2.5 below.

But critically, the 90-day limit should be an outer limit to help ensure that ability-to-repay determinations at the outset are meaningful for all short-term loans—not an option in lieu of determining front-end affordability. Indeed, the OCC/FDIC deposit advance guidance establishes this limit *coupled with* an ability-to-repay requirement, as we urge here. If a borrower is made more than 90 days' worth of short-term loans—likely six two-week loans—in 12 months, it is very unlikely that the lender or lenders' ability-to-repay determinations have been consistently reasonable. The Bureau relied on similar rationale to determine that a cooling-off period after three consecutive loans, even subject to ability-to-repay determinations, is appropriate.

With respect to 30-day loans, we are aware that the 90-day limit would permit only three such loans. This is appropriate given the more vulnerable profile of many borrowers paid monthly as well as the more intense reborrowing patterns these loans demonstrate, as the Bureau found and we discuss in section 2.3.2 above. A 90-day limit applied to 30-day loans is also consistent with the Bureau's current approach to short-term exemption loans (which we oppose as a general matter).

In addition, to prevent lenders from merely shifting borrowers into longer-term loans after the 90-day limit on short-term loans has been reached, we further urge that a lender be prohibited from making a longer-term loan to a borrower who has exceeded the 90-day limit in 12 months, if that lender is the same lender who made the last short-term loan to the borrower. See section 11 below for further discussion of this requirement in the context of longer-term loans.

8.3. Any Loan Within 60 Days of the Prior Loan Should Be Part of the Same Sequence: § 1041.6(b)(1).[413]

We generally support the approach that loans taken within a relatively short time of a previous loan should be treated as part of the same borrowing episode. Indeed, banking regulators have long recognized that a payday loan taken out within a short time of repaying another one is the economic equivalent of a refinancing (where the borrower uses the proceeds from a new loan to pay off an existing loan) or a rollover (where the borrower pays the finance charge essentially to extend the loan term).[414]

That said, the Bureau's proposed definition of loan sequence—and thus the loans to which a presumption of unaffordability will apply—should encompass loans made within 60 days of a previous loan, as proposed in the SBREFA outline, rather than 30. While some consumers may have expense cycles of 30 days or less, the evidence suggests that payday borrowers are more likely to have longer cycles. For those borrowers, a 30-day period puts them at significant risk of being made unaffordable

[413] Proposed § 1041.2(12), defining "loan sequence or sequence."

[414] The FDIC's 2005 payday loan guidelines note that "[w]here the economic substance of consecutive advances is substantially similar to 'rollovers' - without appropriate intervening 'cooling off' or waiting periods - examiners should treat these loans as continuous advances . . . ." FDIC Financial Institution Letters, Guidelines for Payday Lending, FIL 14-2005, February 2005, *available at* http://www.fdic.gov/news/news/financial/2005/fil1405a.html. The OCC's 2000 payday loan guidelines note that payday loans are repaid when the borrower "'roll[s] over' the loan by renewing the old loan (or taking out another loan)," essentially equating the two. OCC Advisory Letter, Payday Lending, AL 2000-10 (Nov. 27, 2000), *available at* http://www.occ.gov/static/news-issuances/memos-advisory-letters/2000/advisory-letter-2000-10.pdf.

loans on a repeat basis. And the Bureau should err on the side of protecting the borrowers most likely to be harmed by unaffordable loans.

8.3.1. A borrower's monthly expense cycle is likely more than 30 days.

We understand that with the 30-day time period, the Bureau aims to capture a typical monthly expense cycle.[415] We agree this would be a reasonable approach, were a 30-day expense cycle the reality for most borrowers of covered loans. Our concern is that a typical expense cycle for payday and car title borrowers, who are likely to be struggling to make ends meet and are often behind on their bills, is likely longer than 30 days. This is especially true because the 30-day period after an unaffordable loan may result in further deferral of expenses until a new loan can be made without a presumption of unaffordability. Thus, a 60-day time period would more effectively address the Bureau's concerns that a consumer's inability to repay a covered loan resulting in a subsequent covered loan.

Evidence supporting that a longer monthly expense cycle is typical is provided both by detailed spending information from surveys, as well as national delinquency data on unsecured debt.

8.3.1.1. U.S. Financial Diaries detailed spending information suggests expense cycle of longer than 30 days.

The U.S. Financial Diaries provide detailed week-by-week expense payments for three months in a year, usually consecutive, for four out of ten of their household profiles of low- and moderate-income families. Every one of these four profiles indicates an expense cycle longer than 30 days for recurring expenses (such as rent, cable bill, and cell phone).

A common theme in the discussion of cash flows for the ten profiles is the frequency of paying regular bills late in months where cash flow is tight. The four household profiles that show three months of detailed expenses appear to bear out that theme, with time between payments for apparent regular monthly expenses extending *from five to seven weeks long*. The amounts of deferred payments range from $180 to $1,760, and from 8% of average monthly expenses to 52%. Brief descriptions of the extended expense cycles for these four households follow:[416]

- **Mateo and Lucia.** In month three, Mateo and Lucia appear to have paid rent ($1700) and their cell phone bill ($60) in Week 4 instead of Week 1, most likely due to lower income early in that month because of illness. This resulted in an expense cycle that was seven weeks long (from the 1st week of Month 2 to the 4th week of Month 3) rather than four weeks long. The deferred expenses paid in Week 4 of Month 3 represented 52% of their average total monthly expenses for the three months.

- **Elena.** In month two, Elena pays her cell phone bill ($180) in Week 4, compared to Week 3 of the prior month. This resulted in an expense cycle of five weeks compared to the usual four weeks. Her cell phone expense represents approximately 8% of her average monthly expenses.

[415] 81 Fed. Reg. at 47958.
[416] Calculated by CRL based on the profiles at Household Profiles - U.S. Financial Diaries: http://www.usfinancialdiaries.org/households.

- **Sandra.** In month three, Sandra does not appear to pay her cell phone bill (which averages $232) at any point, compared to this expense being paid monthly in several prior but non-consecutive months (Week 3 in both cases). This would imply an expense cycle of at least six weeks. This expense is about 10% of her average monthly expenses.

- **Lauren.** Lauren appears to pay her recurring bills in the same weeks every month. However, in Month 3, Lauren pays a $139 cable bill in Week 4. If this is a new monthly expense for Lauren, using prior months' regular expenses would result in an underestimate of regular monthly expenses going forward after Month 3. The cable bill is about 7.5% of her average monthly expenses. (This example is not included the total dollar figures or percentages of deferred payments in the paragraph introducing these examples, as it is not clear that Lauren's cable payment is deferred rather than new. But if they were included, they would fall within those ranges and would not change the lower or upper bounds.)

8.3.1.2. National delinquency data on unsecured debt, by credit score, suggests the monthly expense cycle often exceeds 60 days.

The prevalence with which financially struggling households defer regular monthly expenses is evident in the national level data collected by Experian on delinquencies for unsecured debt obligations.[417] The chart below plots the percentage of accounts 30+ days delinquent for bank cards and personal loans (based on the weighted averages from 2011-Q2 2016, by credit score bucket). Delinquency data for bank cards is particularly relevant to efforts to estimate a typical expense cycle of payday borrowers. Bank cards are often used for everyday essential expenses such as food and transportation and are billed monthly. Most studies estimate that over half of payday borrowers have a bank card;[418] on average, payday loan applicants are 30+ days delinquent on at least one credit card account.[419]

The Experian data graphed below show that for individuals with Vantage Scores[420] <540, 30+ delinquency is very common, ranging from a high of 95% at the lowest category of the credit score range to 20% at the highest part of the range (520-540). Median credit scores for payday borrowers are approximately 525-532.[421] Thus, at any one point in time, we would expect that payday borrowers in the lower half of the credit score range that use a credit card for monthly expenses would have a

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[417] Experian-Oliver Wyman Market Intelligence Report.

[418] Robin Howarth, Delvin Davis, & Sarah Wolff, *Shark-Free Waters: States Are Better Off without Payday Lending*, Center for Responsible Lending (Aug. 2016), *available at* http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_shark_free_waters_aug2016.pdf [CRL, *Shark-Free Waters*].

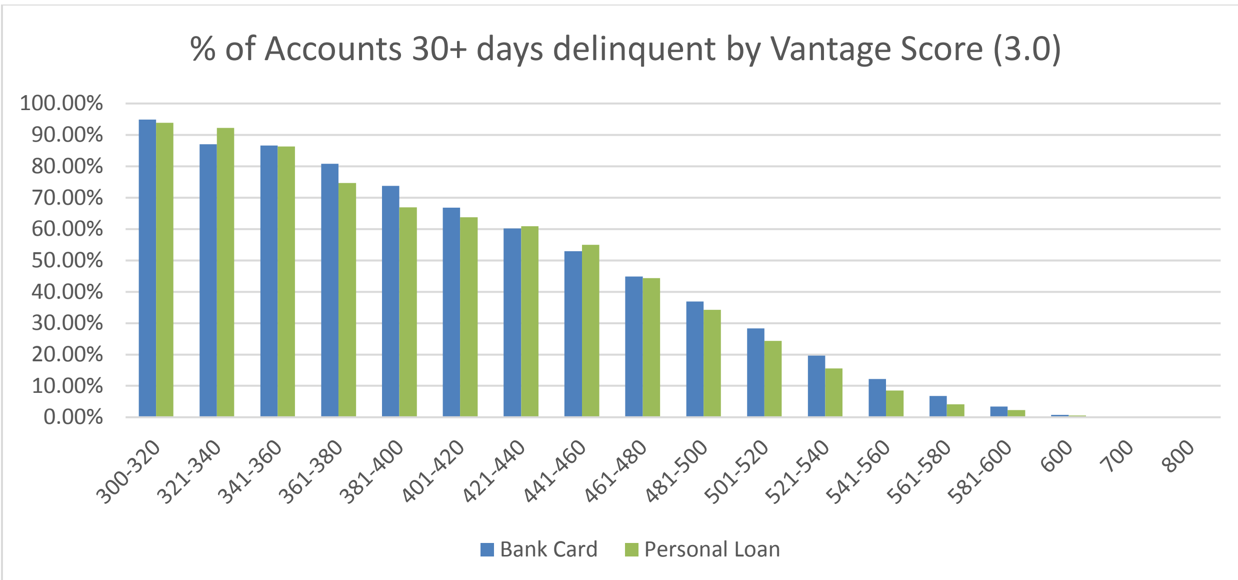
[419] *See, e.g.,* Neil Bhutta, Paige Marta Skiba, & Jeremy Tobacman, *Payday Loan Choices and Consequences* (2014) at 231-33, *available at* http://www.calcfa.com/docs/PaydayLoanChoicesandConsequences.pdf. We note the following from that paper, at 13: "Payday loan applicants tend to have nearly four open credit accounts compared to five for the general population, but, on average, applicants with at least one account are reported delinquent by at least 30 days on half of their accounts."

[420] VantageScore® is a registered trademark of VantageScore Solutions, LLC.

[421] As the Bureau notes, nonprime 101 has found median VantageScore 3.0 scores of 525 for online borrowers and 532 for storefront borrowers. 81 Fed. Reg. at 47921.

very high likelihood (almost 100% for the lower scored individuals and over 20-28% for those closer to the median score) of being in an expense cycle that likely *exceeds 60 days*,[422] much less 30 days.

This data indicate that a 30-day period following repayment of a short-term high-cost loan is not sufficient to measure whether a borrower was actually able to pay other obligations and expenses without reborrowing. Relatedly, the data also indicate that the period the upfront residual income analysis should consider is 60 days beyond the loan's due date, not 30, as we urge in 6.3.3 above.



8.3.1.3. OCC/FDIC bank payday lending guidance provides precedent for a period between loans longer than 30 days.

The OCC/FDIC guidance addressing bank payday loans provides a cooling-off period of an entire statement cycle following the cycle in which the previous loan was taken—thus, a period typically longer than 30 days.[423] And those guidelines prohibit a hard prohibition, not a presumption of unaffordability, further supporting the need for a period longer than 30 days in the context of this rule.

8.3.1.4. The Bureau's data showing extent of reborrowing between 30- and 60-days does not adequately support a period of 30 days rather than 60.

A 60-day period rather than 30 is also essential to prevent foreseeable evasion. We note that the Bureau's data show that 82% of loans are followed by another loan within 30 days, while 85% are followed by a new loan within 60 days. This data indicate that the portion of loans *currently* reborrowed between 30 and 60 days after the previous loan is not an overwhelming portion of loans that are reborrowed. But this data does not support a period of 30 days over 60 days.

[422] It likely also exceeds 60 days assuming 30 days of spending, plus 2 weeks to pay the credit card bill, plus at least 30 days' delinquency.

[423] OCC/FDIC Deposit Advance Guidance, *supra*.

Under *current* law, there are rarely limits that prohibit a new loan within 30 days of another. Lenders do, however, encourage lending as soon as existing state cooling-off periods expire.[424] With a regulatory framework in place that carries no presumption of unaffordability after 30 days, lenders will likely encourage more reborrowing at the 31+ day mark.

8.3.2. "Outstanding" loans should be defined more broadly.

As discussed at sections 3.7 and 6.2.2 above, the definition of outstanding loan is too narrow. As proposed, it would exclude any loan with no payments for the last 180 days. As a result, these loans will not be treated as relevant to whether there is a presumption of unaffordability under § 1041.6. The Bureau flags the issue and asks whether additional protections are warranted here. As noted at section 3.7 and 6.2.2 above, we urge a definition of "outstanding loan" that excludes only loans with no payments and no collection activity for over 365 days.

Relatedly, the Bureau also asks if the rule should prohibit a new loan for the purpose of satisfying a delinquent loan with the same lender. In general, this type of refinancing should be covered by the presumption of inability-to-repay in § 1041.6(c), because a delinquent loan will still be "outstanding." However, if the loan was made more than 180 days ago and there have been no payments in the last 180 days, then it would be no longer "outstanding" and the presumption would not apply.

In order to prevent lenders from benefiting from their own prior unaffordable loans and misusing the collections process to push the consumers into new unaffordable loans, we urge the following:

- If the delinquent loan is in default (which the Bureau should define as 120+ days delinquent) and has not been sold or forgiven, the lender may not refinance the loan.
- If the loan was written off or forgiven (so that the consumer no longer owes a debt to the same lender), a presumption of inability to repay the new loan should apply for 365 days since the last attempt to collect.

A longer discussion of these recommendations is in sections 11.4.2.2 and 11.4.2.5 below, and our related/additional recommendations for the definition of "outstanding loan" are at section 3.7 above.

8.4. The Lower Payment Exception from the Presumption of Unaffordability For Back-to-Back Loans Will Permit Harm and Should Be Eliminated: § 1041.6(b)(2).

Section 1041.6(b)(2) provides an exception whereby a loan made within 30 days of a prior loan does not trigger a presumption of unaffordability if the total cost of the new loan is less than half the total cost of the preceding loan, with a loan term at least as long as the prior loan.[425]

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[424] Leslie Parrish and Uriah King, *Phantom Demand: Short-term due date generates need for repeat payday loans, accounting for 76% of loan volume*, Center for Responsible Lending (2009), *available at* http://www.responsiblelending.org/payday-lending/research-analysis/phantom-demand-final.pdf.

[425] Specifically, the proposed regulation provides that the exception applies if:

(i) Either:

(A) If the borrower would not owe on the new loan more than 50 percent of the amount paid on the prior loan (the borrower has to have repaid the prior loan in full, including any charges excluded from the total cost of credit; the amount paid on the prior loan, for comparison purposes, excludes any charges excluded from the cost of credit);

We understand that the Bureau has provided this exception to respond to lenders' requests, heard through the SBREFA process, that the anti-flipping provisions be more flexible.

We strongly oppose this exception, which gives lenders an incentive to make unaffordable loans and will permit many loans that are in fact unaffordable to be followed by loans with no presumption of unaffordability. The result is that lenders are given the incentive to make loans larger than borrowers can afford at the outset, and then flip the clearly unaffordable portions, extracting excess costs each time. As discussed in section 11 below, we also strongly object to a similar exemption for longer-term loans that are made within 30 days of a short-term or longer-term balloon-payment loan. Both of these exemptions encourage evasions and bait-and-switch tactics.

The following example assumes an initial loan of $500 with $75 in fees. This is a conservative estimate, as the scenario would pose greater risk of harm assuming a larger starting loan size of $1,000 or $1,500 or higher, as the exception has no cap. The borrower repays $575 and immediately receives a second loan for $250, with another $37.50 in fees. This strongly suggests that, on the original loan, the borrower could only afford, at most, $250 in principal, not $500, but the lender gets the windfall of the fees on the additional, unaffordable $250 loaned originally and then rollover over. (Moreover, the consumer may not even have been able to afford the $250 that was not reborrowed. The loan reduction will most likely be the result of lender policies intended to evade the presumption of unaffordability, not the fact that the borrower could afford the initial $250.)

The Bureau asks whether the exception should use a threshold different than 50% or a time period different from "at least as long" as the prior loan, like repayable over a period that is proportional to the prior payment history. We oppose the exception, regardless of the threshold or time period used.

The Bureau also asks whether the loan should be eligible for the exception if the prior loan had been paid in full but had triggered late fees or was delinquent. A presumption of inability to repay is especially critical in this situation. If the smaller payment exception is retained, this limitation should be made explicit.

8.5. A Covered Short-Term Loan Following a Longer-Term Balloon Loan Should Have a Presumption of Unaffordability for 60 Days, and "Balloon" Should be Defined Much More Broadly: § 1041.6(c); §1041.2(a)(7).

Section 1041.6(c) would trigger a presumption of unaffordability for a covered short-term loan while a covered long-term balloon-payment loan is outstanding and for 30 days thereafter.[426] We strongly support this provision but, for reasons noted above, urge a 60-day period rather than 30. Balloon payments, whether on a single-payment loan or a longer-term loan, are typically designed to impose payment shock that results in a subsequent loan.

(B) If, in a rollover transaction, the borrower would not owe more on the new loan than paid on the loan being rolled over; and

(ii) The new covered short-term loan would be repayable over a period at least as long as the period over which borrower made payments on the prior covered loan. Proposed § 1041.6(b)(2).

[426] Proposed § 1041.6(c).

The effectiveness of the Bureau's approach, however, depends largely on the scope of loans that are considered "balloon" loans. We fear that the proposed definition of balloon payment—more than twice the size of another payment—will miss many loans that create unaffordable payment shock. As discussed in our Definitions section at 3.2, we urge a far broader definition of balloon payment, consistent with state laws governing smaller installment laws rather than the much less relevant mortgage context. We urge that balloon payment be defined as a payment 10% larger than any other payment.

As we also note in section 3.2, this broader definition is essential to prevent foreseeable evasions. While there may not be many covered loans on the market today with balloon payments between 10 and 50% greater than the other loan payments, we should expect there will be if this definition is not broadened.

8.6. The Presumption of Unaffordability during an Unaffordable Outstanding Loan Should Be Significantly Broadened: § 1041.6(d).

Section 1041.6(d) creates a presumption of unaffordability for a covered short-term loan for a borrower who has a covered or non-covered outstanding loan from the same lender or its affiliate and any of the following indicia of unaffordability are present:

(1) The consumer has been delinquent more than 7 days in the previous 30 days on the outstanding loan;
(2) The consumer has expressed inability to make a payment on the outstanding loan;
(3) The new loan would permit the consumer to delay or skip a payment;
(4) The new loan would not result in any disbursement of funds to the consumer or the disbursement would not substantially exceed the payments on the outstanding loan due in the next 30 days.

We strongly support the inclusion of a provision with this aim, and we thank the Bureau for its general recognition that lenders may use non-covered loans as gateway loans into covered loans. At the same time, we have significant concerns that these indicia are far too limited and will miss a significant number of loans that are unaffordable.

The four indicia above are also proposed for longer-term loans, and we discuss our concerns in detail in the context of longer-term loans at section 11.4 below. Our comments in that section apply to the short-term provision as well.

In addition, we note that, for longer-term loans, there are two exceptions to the four presumptions of unaffordability (for loans with smaller payments and loans with a lower total cost of credit) that are not included for short-term loans. We oppose those exceptions for longer-term loans, urging that they be eliminated or significantly narrowed (see section 11.5 below). The Bureau notes that exceptions are not provided for short-term loans because of the Bureau's general concerns about short-term loans. We strongly agree that those exceptions would be wholly inappropriate in the short-term context in light of the Bureau's concerns and findings about the likelihood that short-term balloon loans will be unaffordable. For the same reason, we oppose the proposed exception of § 1041.6(b)(2)(i)(B) as discussed at section 8.4 above.

Finally, we flag the concern we discuss in the definition of "lender" at section 3.4.2: These provisions do not readily seem to account for loans made by unaffiliated lenders but through the same or an affiliated service provider, like a CSO or CAB. We urge that any same lender/affiliate scenario explicitly apply to the same service provider as well, so that CSO/CAB models are appropriately subject to the provisions.

8.7. A Presumption of Unaffordability Should Only Be Rebuttable with Verification Evidence: § 1041.6(e).

Section 1041.6(e) states that the lender may only rebut the presumption of unaffordability if it reasonably determines, based on reliable evidence, that the consumer will have sufficient improvement in financial capacity to have the ability to repay the new loan, despite the unaffordability of the prior loan.[427]

The proposal permits two ways a lender can determine sufficient improvement in financial capacity, both of which must be supported with reliable verification evidence: (1) a decline in income not reasonably expected to occur, and (2) an increase in net income or decrease in major financial obligations during the upcoming period.

We support these approaches as reasonable while emphasizing that these should be the only permitted scenarios. It is also critical that the improvement in financial capacity be supported with reliable verification evidence as described in section 6.4 above (meaning not consumer statements or other "reliable evidence" that is not verification evidence). Once an initial loan has been unaffordable, only the highest standards of verification should apply to a subsequent loan in a sequence.

The Bureau notes that it considered a third way to rebut the presumption that it did not include for fear of its swallowing the rule: an unusual, non-recurring expense occurring during the previous loan term, noting an emergency car repair and an unexpected medical expense as examples. We strongly support the Bureau's exclusion of this approach. Unexpected expenses occur far too commonly for this to be an exception; indeed, evidence suggests that unexpected expenses should in fact be expected. As the Bureau notes, an expense shock does not mean a prior ability-to-repay determination was reasonable; the loan may be a substantial reason the borrower could not absorb the shock. We further agree with the Bureau's concern that permitting this approach would have substantial implications for the treatment of basic living expenses and accounting for potential volatility of them in the context of the ability-to-repay determination. Indeed, it would significantly undermine the sound logic requiring a cushion in the context of the longer portion of the rule.

To emphasize the limited scenarios that permit overcoming a presumption, the Bureau should define the phrase "improvement in financial capacity" and make clear that it means only an improvement in "net income" or "major financial obligations." The proposed Comments and discussion consistently lead to that conclusion, but the rule should be clearer. See section 11.6 below for additional discussion of overcoming a presumption of unaffordability.

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[427] § 1041.6(e). It further requires that the lender must compare the consumer's financial capacity during the period for the new loan to the consumer's financial capacity since obtaining the prior loan or, if the prior loan was not a covered short-term or covered longer-term loan balloon payment loan (i.e., a loan under 1041.6(d)), during the 30 days prior to the lender's determination.

8.8. The Prohibition after Consecutive Loans Should Be Extended to 90 Days § 1041.6(f).

Section 1041.6(f) prohibits a loan sequence of more than three covered short-term loans subject to § 1041.5. The proposal prohibits any covered short-term loan during an outstanding loan and for 30 days thereafter if it would be the fourth loan in a sequence.

We urge that a prohibition apply to a third loan in a sequence rather than the fourth; that it last 90 days instead of 30; and that it be coupled with a cumulative annual indebtedness limit of 90 days.

We strongly agree with the Bureau's assessment that, after returning twice, it is "extremely unlikely" that a borrower will be able to afford a fourth loan within a reborrowing period. Indeed, at that point, "three consecutive ability-to-repay assessments have proven inconsistent with the consumer's actual experience." But this rationale is true of third loan in a series as well. A second loan was only made after a presumption of unaffordability was purportedly rebutted. It is extremely unlikely that the borrower will be able to afford a third loan within the same reborrowing period.

The Bureau solicits comment on the necessity of the proposed prohibition and whether a presumption would be sufficient—either the same one applied to a second and third loan, or a different one instead. We strongly oppose weakening this prohibition by making it a presumption. We support the Bureau's rationale that this "backstop," in the form of a prohibition, is needed, and that indeed relatively few borrowers will ever encounter this backstop. If they do, they surely need its protection.

This hard backstop is essential to enforce the requirement of reasonable initial ability-to-repay determinations and required rebuttals of presumptions of unaffordability. The chances are overwhelmingly high that borrowers who receive consecutive loans are not miracle borrowers who have unexpected shortfalls, followed by a sufficient improvement in circumstances, time after time after time, but rather are borrowers whose lender is repeatedly making unreasonable ability-to-repay determinations, trapping the borrower in debt.

The Bureau further solicits comment on whether the prohibition period should be longer than the presumption period, and we strongly recommend a period of 90 days.

Merely imposing a hard 30-day cooling off period at this point is not enough. As discussed above, 30 days is not sufficient to cover a typical monthly expense cycle for a borrower. Lenders may encourage borrowers to return 31 days later, having deferred bills in the interim, and the cycle of debt will not be broken. The Bureau found that two-thirds of loans that reach a fourth loan end up having at least seven loans, and 47% reach at least 10 loans.[428] Thus, borrowers who reach that point are clearly struggling with unaffordable loans, and their finances likely need more time to recover from three such loans than they needed to recover from one or two.

Finally, the Bureau solicits comment on whether a prohibition should be triggered by a pattern of reborrowing on a mix of covered short-term and longer-term balloon payment loans, and if so, how it should be tailored. We urge that the hard backstop be triggered by any combination of balloon-payment loans, whether short-term or longer-term. Thus, if the Bureau retains the three-loan trigger, it would encompass three short-term loans, three longer-term balloon loans, or two of one type and one of the other.

[428] 81 Fed. Reg. at 47967.

8.9. The Prohibition on a Covered Short-Term Loan Following a Short-Term Exemption Loan Should Also Be Extended to 60 Days: § 1041.6(g).

Section 1041.6(g) prohibits a covered short-term loan made under the ability-to-repay requirements while a short-term exemption loan is outstanding and for 30 days thereafter. While we oppose the short-term exemption loan altogether, we agree with the Bureau's conclusion that this prohibition is necessary to prevent undermining the principal reduction requirements of short-term exemption loans. We urge that it be extended to 60 days; see section 8.3 above.

8.10. Non-Covered Bridge Loans Should Include All Non-Covered Loans, and They Should Reset, Rather Than Toll, The Relevant Time Period: § 1041.6(h).

Section 1041.6(h) provides that non-covered bridge loans may not be considered in determining whether 30 days have elapsed between covered loans. We strongly support the Bureau's effort to prevent evasion of the rule with non-covered bridge loans. As the Bureau notes, a bridge loan could mask the borrower's inability to repay the prior loan.

We support rules to prevent pawn loans from being used as bridge loans. However, we urge the CFPB:

- To prohibit use of *any* non-covered loan as a bridge loan;
- To require a full 30 (or 60, as we propose) <u>consecutive</u> days without borrowing, unless 90 days have elapsed between covered loans and 30 consecutive days have elapsed since the last balloon payment loan (covered or not).

The proposed definition for non-covered bridge loan is a non-recourse pawn loan made by the same lender and substantially due within 90 days.[429] We support inclusion of these loans; as the Bureau notes, many lenders offer both covered loans and pawn loans.

But we should expect lenders to offer other non-covered, and covered, loans as well. Lenders will attempt to use all of those loans to keep borrowers indebted while evading the anti-flipping provisions of the short-term rule.

The Bureau solicits comments on whether the proposal is sufficient to address concerns about lenders making loans of different lengths to avoid the presumption, such as a short-term loan followed by a 46-day covered longer-term balloon payment. In particular, the Bureau asks whether the rule should impose tolling requirements on covered long-term balloon payment loans with a duration of 90 days or fewer.

We appreciate these questions, yet urge the Bureau to broaden even further the conception of what types of loans will keep borrowers in debt by setting them up for unaffordable payments. Depending on loan size and terms, a longer-term loan without a balloon payment can be just as unaffordable as a longer-term balloon loan. We note that payday lenders have long made lower-cost loans—free loans, as the Bureau notes—[430]to lure borrowers into what becomes a debt trap. Thus, we urge that any loan from the same lender, regardless of price, payment mechanism, security, or whether or not it has a balloon payment, be considered a bridge loan.

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[429] Proposed § 1041.2(13).

[430] 81 Fed Reg. at 47871, n.58.

In addition, we urge the CFPB to require the days without a loan from the lender to be consecutive. That is, a bridge loan should not simply toll the counting of the 30 (or as we propose, 60) days; it should reset the clock so that another 30 days without a loan is required in order to avoid a presumption of unaffordability.

A tolling rule does not sufficiently protect borrowers from the impact of unaffordable balloon payment loans. For example, assume that the lender makes the borrower another loan 15 days after the second consecutive short-term loan. The lender offers a 46-day balloon payment loan at 300% APR but with no leveraged payment mechanism. After aggressive debt collection calls, the consumer repays that loan. A tolling rule would permit a new covered loan 16 days later without any presumption or ban, notwithstanding the fact that only 16 days have elapsed since the last balloon payment. Instead, another 30 days should be required.

For further discussion of concerns about non-covered bridge loans, see section 11.10; those concerns generally apply here as well.

8.11. The Loophole Permitting Flipping With Short-Term Lines of Credit Must Be Closed.

The provisions of § 1041.6 as proposed do not appear to apply to subsequent draws on open-end lines of credit, but only to individual new loans (including rollovers). The Bureau solicits comment on whether the presumptions, mandatory cooling-off periods, or additional limitations should apply for (1) increases in the credit line; (2) an advance on the line; and (3) in other circumstances, and how they should be tailored.

As discussed at 6.3.2.2 above, every draw on a short-term credit should be treated as a new loan. Short-term lines of credit are uncommon products; likely exist primarily to exploit some loophole or another; and are appropriately treated as closed-end products. The fact that the lender has given the consumer advance permission to reborrow (either during or after the 45 days) does not diminish the need to reassess the ability to repay when such reborrowing occurs.

As a result, every advance, if made within 60 days of the prior advance, should trigger a presumption of unaffordability. All other provisions of § 1041.6 should also treat each advance as a new loan. Indeed, we note that in the Bureau's explanation for excluding open-end loans from the short-term exemption of § 1041.7, it states that, if open-end loans could be exempted, a borrower could repeatedly draw down credit without the lender ever determining ability-to-repay and could reborrow serially on a single exemption loan. This concern would seem to translate to subjecting advances on short-term open-end loans (even when subject to an initial ability-to-repay determination) to the reborrowing limitations of § 1041.6.

The Bureau also solicits comment on whether the reassessment of ability-to-repay currently required at 180 days should carry a presumption. In light of our recommendation that every advance be treated as a new loan, the presumption approach applied to closed-end loans should apply to open-end as well.

If the Bureau does not adopt this approach, some recommendations we make in section 11 in the context of refinancing longer-term open-end loans may be applicable here.

8.12. Lenders Must Consult State Databases When Available, if No RIS Is Available: § 1041.6(a)(2).

Section 1041.6(a)(2) requires that, to determine borrowing history to comply with § 1041.6, lenders must consult an RIS, and that if an RIS is not available, they must still consult their own and affiliate records. We urge that, in addition, lenders must obtain information from any state database in the consumer's state that includes covered loans, if such information is available, and include any loans reflected therein in their determination of whether a presumption or prohibition applies.

8.13. Additional Reporting Requirements Related to Flipping Should Be Required.

We appreciate the Bureau's statement that if a "substantial percentage" of consumers "return" within 30 days to obtain a second loan, "that pattern may provide persuasive evidence" that the lender's ability-to-repay determinations were not consistent with a reasonable determination of ability-to-repay.[431] The Bureau also notes that it expects that a borrower receiving a third loan will be a "relatively unusual case."[432]

To that end, as noted at 16 below, we urge that lenders be required to report the following related to this section:

- All applications for loans during each presumption period as a portion of total loans and total borrowers;
- All applications for whom a first and second presumption of unaffordability is overcome;
- All applications who take advantage of the exception to the presumption, if provided.

9. AN EXEMPTION FROM ABILITY-TO-REPAY FOR ANY SHORT-TERM LOAN WILL PERMIT SUBSTANTIAL HARM TO CONTINUE: § 1041.7.

9.1. Overview.

Section 1041.7 would provide what the Bureau calls a "conditional exemption" for certain covered short-term loans from the finding of abusive and unfair practices and from the requirements of the ability-to-repay determination and the anti-flipping provisions of section 1041.6. We strongly oppose this exemption as wholly inconsistent with the fundamental ability-to-repay principle of the proposed rule and likely to permit substantial harm to persist. We note that this harm should be expected to impact a very large number of consumers, as the Bureau states that it expects that majority of short-term loans will be made pursuant to the exemption.

Section 1041.7(a) sets out the exemption generally. Section 1041.7(b) establishes principal amount limitations for the exempted loans, establishing an initial limit of $500 on a first loan, two-thirds the initial loan amount on a second loan within 30 days of the prior, and one-third the initial loan amount on a third loan within 30 days of a second loan. The loans must be fully amortizing,[433] may not be

[431] 81 Fed. Reg. at 47966.

[432] *Id.*

[433] In addition, the payment schedule must provide for the lender to allocate payments to outstanding principal and fees as they accrue only by applying a fixed periodic rate of interest to the outstanding balance of the unpaid loan principal every scheduled repayment period for the term of the loan.

open-end, and may not be secured by a vehicle title. Section 1041.7(c) establishes borrowing history requirements, requiring that, in order for a lender to make a short-term exemption loan, the consumer (1) may have no other covered loan outstanding other than a longer-term exemption loan; (2) may not have had a covered short-term loan or covered longer-term balloon payment loan subject to an ability-to-repay requirement outstanding during the last 30 days; (3) may not have more than three short-term exemption loans in a sequence; and (4) may not have more than six covered short-term loans (whether ability-to-repay or exemption loans) or more than 90 days' worth of such loans outstanding over a consecutive 12-month period. Section 1041.7(d) provides that a non-covered bridge loan may not count toward the 30-day time periods between short-term exemption loans. Finally, § 1041.7(e) sets out required disclosures for the first and third loans of any sequence under the exemption. All of the provisions of §1041.7 apply on a cross-lender basis.

In the sections that follow, we object to the exemption on the following grounds, among others:

- The principal stepdown approach will not prevent substantial payments due in short order;
- Data strongly suggest that the loan payments will often be unaffordable;
- One unaffordable loan can cause substantial harm;
- The Bureau's offered justification for the exemption is unpersuasive in light of the rule as a whole;
- Vehicle title loans are appropriately provided no exemption, for reasons that also discredit the exemption for payday loans;
- The exemption threatens state laws with no payday lending; and
- The Bureau offers no meaningful precedent for the exemption.

We next address the details of the exemption, including responses to the Bureau's specific requests for comment. We note that the following elements of the exemption make it particularly harmful:

- The first loan in a series as high as $500;
- A loan sequence/reborrowing construct that permits excessive unaffordable lending:
    - A 30-day time period is entirely insufficient to expect recovery from a $500 balloon loan, yet lenders may push borrowers to wait to day 31 to reset the loan amount at $500. A stepdown on every loan within 12 months would be most appropriate.
    - Short-term exemption loans should not be permitted after a longer-term exemption loan from the same lender;
    - A 30-day time period is insufficient after a covered balloon loan with an ability-to-repay requirement before an exemption loan;
    - Permitting two series of three consecutive unaffordable loans is particularly unwarranted;
    - A limit of six loans and 90 days is too high, particularly considering it permits additional short-term covered loans outside the exemption;
- The lack of an income verification requirement encourages lax lending and will prevent the Bureau from having supervisory data it should have to analyze the effectiveness of the exemption.

We agree that under no circumstances should the exemption be permitted for vehicle title loans; when an RIS is unavailable; or for open-end loans. And we agree that the proposed off-ramp the Bureau considered would not have successfully mitigated harm.

9.1. The Principal Stepdown Approach Will Not Prevent Substantial Payments Due in Short Order.

The Bureau proposes structural requirements that it notes will protect against the harm from making covered loans without a reasonable ability-to-repay determination. But the initial loan limit of $500 and subsequent principal stepdown do not achieve this aim; rather, they continue to permit substantial payments due on the borrower's next payday, with no evidence of affordability. Below we review what a typical exemption loan sequence with a first loan of $500 may look like, first at a price of $15 per $100 and then at $25 per $100.

Two series of three exemption loans at $15 per $100:

Cost of $15 per $100 (400% APR)	Principal	Interest	Effective Principal Repayment, Net of Next Loan	Total Payment
Loan 1	$500	$75	$167	$242
Loan 2	333	50	167	217
Loan 3	167	25	167	193
Sequence 1 Total [1]	**$500**	**$150**	**$500**	**$650**
Loan 4	$500	$75	$167	$242
Loan 5	333	50	167	217
Loan 6	167	25	167	193
Sequence 2 Total [1]	**$500**	**$150**	**$500**	**$650**
Grand Total [2]	**$1,000**	**$300**	**$1,000**	**$1300**

Two series of three exemption loans at $25 per $100:

Cost of $25 per $100 (650% APR)	Principal	Interest	Effective Principal Repayment, Net of Next Loan	Total Payment
Loan 1	$500	$125	$167	$292
Loan 2	333	83	167	250
Loan 3	167	42	167	209
Sequence 1 Total [1]	**$500**	**$250**	**$500**	**$750**
Loan 4	$500	$125	$167	$292
Loan 5	333	83	167	250
Loan 6	167	42	167	209
Sequence 1 Total [1]	**$500**	**$250**	**$500**	**$750**
Grand Total [2]	**$1,000**	**$500**	**$1,000**	**$1500**

[1] Because the loans in a three-loan sequence are made in quick succession, they are effectively rolling over portions of the original $500 principal; thus we consider each sequence to total $500 in credit.

[2] While two three-loan sequences separated by less than 60 days are best considered one six-loan sequence where no new credit beyond the original $500 is extended, we treat them as two sequences here in the interest of a conservative presentation, and thus two $500 loans totaling $1,000.

Another, more expensive scenario, not illustrated here, could occur whereby a lender encourages a borrower to return 31 days later, at which point the lender could avoid the principal stepdown requirement and make the borrower another $500 loan. It could do this six times throughout the year, resulting in total amounts paid of $961 in interest to borrow $500 at a cost of $15 per $100, and $1,250 in interest to borrow $500 at a cost of $25 per 100. (For this scenario, we do not include churned principal, which we count here as including a loan made within 60 days of another loan, consistent with our position explained at section 8.3 above.)[434]

In other contexts in the rule, the Bureau recognizes that the size of a payment can be as significant as the loan's structure as installment or single-payment. For example, the Bureau notes in its discussion of market concerns on longer-term loans that a longer-term balloon loan can be as challenging as a single payment loan, but that even amortizing installment loans "are as capable of producing unaffordable payments as short-term loans."[435] The same is true of a series of short-term loans with a principal stepdown requirement. As discussed further at section 9.2.4 below, this is not an installment loan; it is three balloon loans, each due on the borrower's next payday. But even if it were a true installment loan, given the short-term nature of the entire episode, the most relevant factor to the loan's affordability is the size of each of the three payments. These payments, though reducing over time, are likely to be unaffordable for many borrowers, as illustrated in the following section 9.2.

Even the third loan in the series—which above would require a $193 to $209 payment after only two weeks—is a huge payment for a lower-income, credit-challenged consumer, especially after having made even larger payments twice over the previous four weeks.

The Bureau solicits comment on the proposed principal stepdown over three loans, and whether it should be a 25% reduction over four loans instead. The risk of substantial harm, already great over the course of three loans, is likely greater over the course of four loans. It would permit more loan churn, higher total finance charges, and more days' indebted in likely unaffordable debt.

9.2. Data Strongly Suggest That Exemption Loan Payments Will Often Be Unaffordable.

Various data indicate that exemption loan payments will often be unaffordable. As discussed below, relatively small payments are often unaffordable for payday borrowers; industry simulations estimate that most single-payment payday borrowers will not qualify for installment loans with payments even smaller than exemption loan payments; and default data on early loans show that a three-loan series will often be unaffordable.

9.2.1. Relatively small payments are often unaffordable for payday borrowers.

Various data show that relatively small payments are often unaffordable for payday borrowers. These include the Bureau's online payments study, CRL's analysis of payday loan payments in the Lightspeed

[434] We note that the current median short-term payday loan size is about $350. Even using a starting loan of $350 in the two charts above, the effective biweekly payments would be as follows – At a cost of $15 per $100: $169, $152, and $134, averaging $152. At a cost of $25 per $100: $204, 175, and $145, averaging $175. Though smaller than the payments in the above charts, our objections, throughout this section 9, to any assumption that loan payments under the exemption will be affordable are warranted for payments of these sizes as well.
[435] 81 Fed. Reg. at 47986.

checking account database; performance data on relatively small payday loans; and borrowers' descriptions of their inability to repay even relatively small payday loans.

9.2.1.1. The Bureau's online payments study shows that many payments smaller than typical balloon payments bounce.

The Bureau's online payments study of nearly 20,000 accounts with online payday loans (whether single-payment or longer-term) offers an instructive look at average payment sizes that are significantly smaller than the typical single-payment payday loan. The mean payment sizes of failed payments were $172 on an initial failed payment request; $152 on a second; $175 on a third; $322 on a fourth; and $198 on a fifth. All but the fourth of these payment sizes are smaller than we would expect the typical effective exemption loan payment to be, even at the lower end of the price range, $15 per $100.[436] (The successful payment sizes were generally in the same range.)[437]

Yet even at these payments sizes, bounced payments rates were extremely high. Over the course of the 18 months studied, half of all accounts had at least one payment resulting in overdraft or NSF fee, *and those on average incurred $185 in fees*[438] (*suggesting roughly five such overdraft/NSF fees on average*, at $34 each).[439] These figures suggest that the unaffordability of one relatively small payment was not an isolated incident for most borrowers, but that the payments were unaffordable on a sustained basis. The Bureau's findings of low success rates on re-presentments, as well as the high rate of account closures,[440] further show that borrowers do not easily bounce back from having insufficient funds for relatively small payday loan payments.

9.2.1.2. 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 different database of consumer checking account activity for its 2015 paper, *Payday Mayday*.[441] The payday loan payment sizes in this panel were typically much smaller than a typical payday balloon payment:

[436] CFPB Online Payday Loan Payments, Table 1.
[437] *Id.*
[438] CFPB Online Payday Loan Payments at 11.
[439] This is a conservative figure given the Bureau's finding that 13% of the payday requests that resulted in overdraft or failure due to NSF did not incur fees. *Id.* at n.10.
[440] CFPB Online Payday Loan Payments.
[441] CRL, *Payday Mayday*, *supra*. 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.

Distribution of payday loan payment amounts in Lightspeed panel

Range	Percent of payments in this range
1 (<$108)	54.11%
2 ($108-$158)	15.54%
3 ($158-$275)	11.77%
4 (>$275)	18.58%
Grand Total	**100.00%**

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: The median size of such payments was only $90, and 65% of the payments were $158 or less—still less than even the smallest effective repayment on a series of exemption loans, starting at $500, at $15 per $100.

Distribution of the payday payment amounts followed closely by an overdraft

Range	Percent of payments in this range
1 (<$108)	58.54%
2 ($108-$158)	6.10%
3 ($158-$275)	12.20%
4 (>$275)	23.17%
Grand Total	**100.00%**

9.2.1.3. Performance data even on relatively small payday loans is very poor.

California has a short-term payday loan size limit of $300, including the fee. In 2015, the average transaction was $237.[442] Yet its performance data indicate high rates of unaffordability: The Bureau found that 82% of its loans are reborrowed within two weeks, and 90% within 60 days.[443]

9.2.1.4. Borrowers' descriptions of their inability to repay relatively small loans further demonstrate they are often unaffordable.

Borrower narratives routinely describe extreme distress even from payday loans of relatively small sizes. See, for example, a number of borrower experiences in Appendix A that describe distress from unaffordable payday loans of $200 or less.[444]

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[442] Kristin Broughton, American Banker, "Payday 'Debt Trap' Fueled by Repeat Customers: Calif. Regulator" (May 6, 2016), http://www.americanbanker.com/news/consumer-finance/payday-debt-trap-fueled-by-repeat-customers-calif-regulator-1090068-1.html.
[443] Supplemental Findings at 108, Table 21.
[444] Appendix A, narrative #s 1, 10, 26, 27, 28, 29, 30, 58, 65, 78, 81, 91, 92, 105, 107, 115, 124, 139, 142.

9.2.2. Industry data suggest that most current short-term payday borrowers cannot afford an exemption loan payment*, or even a payment half that large.*

Industry analysis also suggests that most current short-term payday borrowers cannot afford a $200 payment in two weeks' time. To estimate the portion of balloon payment borrowers who could qualify for longer-term payday loans, Nonprime101 applied Clarity's residual income model to balloon payday borrowers.[445] It found that 40% of current storefront borrowers would qualify for a $350, three-month, fully amortizing loan, at both 200% and 400% interest[446]—indicating the inverse: 60% of payday borrowers *cannot* afford such loans. These loans carry bi-weekly payments of $75-$93—only 31-48% of the sizes of the effective payments due over the course of a three-exemption-loan series starting at $500 at a cost of $15 per $100—*not even half as large.*

9.2.3. Public data on lower-income families' income and expenses suggest that even exemption loans are likely to be unaffordable.

The following chart shows biweekly income and very limited expenses for an individual earning $25,000, based on data from the Bureau of Labor Statistics Consumer Expenditures Survey.[447] It shows that even assuming the borrower pays only for housing, food, transportation, and healthcare, a borrower with a $500 exemption loan at $15 per $100 will end up with a net deficit of $135 during a two-week period.

Biweekly income/expenses for payday borrower earning $25K annually	
Income before taxes	$962
Income after taxes	**946**
Housing expense (including utilities)	(455)
Average effective loan repayment on a $500 exemption "stepdown" loan at $15/$100	(217)
Total "major financial obligations" and utilities	**(672)**
"Residual Income"	**$274**
Typical expenses in a very limited number of categories	
Food	(169)
Transportation	(123)
Healthcare	(116)
Total limited expenses	**(406)**
Net Deficit	($135)

[445] Findings from Rick Hackett, Can Storefront Payday Borrowers Become Installment Loan Borrowers? Nonprime101 Report 8 Dec. 2, 2015), https://www.nonprime101.com/can-storefront-payday-borrowers-become-installment-loan-borrowers/.

[446] *Id.*

[447] Using figures for a household earning $15,000-$29,999 annually.

9.2.4. Default data on early loans suggest that exemption loans will often be unaffordable.

Limiting exemption loans to three in a series does little to increase the likelihood that the loans are affordable. The Bureau's data show that 20 percent of payday loan sequences default, either on the first loan or later. Thirty-one percent of defaults are on the first loan and 27% are two or three loans long. As the Bureau notes, this means that 58% of all defaults occur on loan sequences of three loans or less.[448]

As or more importantly, the Bureau convincingly explains why default data can significantly underrepresent harm. Repeat loans mask unaffordable loans, and even consumers who do repay often do so because of the power of the leveraged payment mechanism, not because the loan was affordable.

While the loans in the CFPB's study did not have required principal stepdowns, the presence of that requirement does not necessarily mean defaults, or unaffordable repayments, would be lower. Indeed, those first loans may well be larger than today if lenders are required to reduce them for loans two and three. In addition, as discussed above, smaller second and third loans will often still be unaffordable.

Further, the Bureau has found that short-term payday borrowers are typically flipped into loans of the same amount or more.[449] This likely staves off default to later in the loan sequence, despite the unaffordability of the initial loan. Moreover, though principal stepdowns are required on exemption loans, those apply to a subsequent loan entirely (except in states with rollovers). The stepdowns do not change that the amount debited from the consumer's account on payday is the full amount due on the existing loan—not the full amount due less the stepped-down principal to be extended on the subsequent loan. This means that borrowers will still need the funds on payday to cover the entire loan repayment, which—as evidenced by existing high default rates on early loans—is often not the case.

9.3. One Unaffordable Loan Can Cause Substantial Harm.

It only takes one unaffordable loan to cause substantial harm, in the form of bounced payments on that loan itself, default and collections activity on that loan, or repayment of that loan that causes collateral harm. As the Bureau notes, when borrowers default, the leveraged payment mechanism often increases the degree of harm. See sections 2.2.2 and 2.2.3 for further discussion of these harms.

9.4. The Bureau's Offered Justification for This Exemption Is Unpersuasive in Light of the Rule as a Whole.

The Bureau posits, essentially, that making any covered short-term without a reasonable ability-to-repay determination is abusive and unfair, unless the "screening and structural" protections of the

[448] 81 Fed. Reg. at 47939.
[449] CRL Data Point at 4.

proposed exemption are in place to "reduce the likelihood and magnitude of the harm from unaffordable payments," including "sequences of reborrowing."

The Bureau offers various data points and rationales in an effort to justify this exemption. But the effort ultimately fails because it sets out to do the impossible: reconciling an extremely well-founded determination that making a covered loan without a reasonable ability-to-repay determination is abusive and unfair, with an exemption that permits lenders to make *those very same loans* with no such determination. While this may be one way to try to address concerns about access, it is both unnecessary in light of an appropriately broad view of "access," (see section 19 below) and, ultimately, in light of the tension just described, illogical.

9.4.1. The Bureau's data show that exemption loan payments will likely be unaffordable.

The Bureau offers data on reborrowing to support the notion that some consumers will have the ability to repay these exemption loans. For example, the Bureau cites one study finding that 22% of borrowers had no reborrowing using a 30-day loan sequence definition. But this leaves 78% who did reborrow.[450] Of those who did reborrow, 16% ended with repayment within 3 loans in a 30-day period. Again, this means that 84% of those who did reborrow did not end with repayment within 3 loans. Thus, 66% of all borrowers—two out of every three borrowers—both did reborrow and did not repay within four loans. In the Bureau's data, using a 30-day loan sequence, 50 percent of loan sequences had at least four loans.

The Bureau also finds that most consumers do not reduce their loan amounts from one loan to the next, and that this lack of "self-amortization" is correlated with higher rates of reborrowing and default. It thus posits that consumers who reborrow might do so less if they could pay down gradually.[451] But the Bureau does not determine the extent to which this lack of "self-amortization" is due to a borrower's lack of financial ability to do so. Second, reborrowing "less" does not translate to affordability.

Relatedly, the Bureau notes that these requirements are intended to permit paying of the original loan amount "in *more* manageable increments,"[452] but it does not offer compelling support for why these increments will in fact be manageable.

With respect to mitigating harm, the Bureau notes that the proposed maximum loan and principal stepdown requirements "would limit the harm to consumers in the event they are unable to repay the initial loan." We are not sure we follow this reasoning. As noted in section 9.3 above, one unaffordable loan can cause cascading substantial harm.

9.4.2. The Bureau's evidence clearly shows that significant payments in short order pose substantial difficulty to consumers.

Finally, the Bureau often acknowledges the difficulty that significant payments in short order may pose: "[W]ithin the space of a single expense or income cycle, a consumer with little to no savings cushion and who has borrowed to meet an unexpected expense or income shortfall, or who chronically runs

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[450] 81 Fed. Reg. at 47939.
[451] Supplemental Findings at 133; CFPB Data Point at 16.
[452] 81 Fed. Reg. at 47974 (emphasis added).

short of funds, is unlikely to have the available cash needed to repay the full amount borrowed plus the finance charge on the loan when it is due and to cover other expenses." Yet the Bureau offers no convincing rationale for why this would not hold true for a three consecutive exemption payments averaging $217 each.

Further, the Bureau notes critically that the size of a single-payment loan repayment relative to the borrower's next paycheck gives some sense of how difficult repayment may be, noting that an average payday loan payment today amounts to 37% of a bi-weekly paycheck for the average storefront borrower. Yet for a $500 exemption loan series, this percentage is still substantial and nowhere justified as likely to be affordable. At $15 per $100, the first loan would take 28% of a paycheck, the second 25%, and the third 22%.[453] At $25 per $100, the percentages are 34%, 29%, and 24%, respectively. Notably, the Bureau found that *about half* of online payday installment loans default when (monthly) payments exceed 20% of a borrower's monthly income.[454]

9.4.3. The Bureau recognizes that even a $167 principal payment is significant.

The Bureau recognizes that an added $167 debt burden for which there is no affordability assessment may be problematic for borrowers. In its justification for limiting the initial loan to $500, the Bureau explains that it believes that loans with a principal amount larger than $500 "would carry a significant risk of having unaffordable payments."[455] It offers a comparative example of a $1,000 loan, noting the significant difference between a $333 principal payment plus finance charge, as would be required on a $1,000 loan, versus a $167 payment plus finance charge. It then states: "For consumers who are turning to covered short-term loans because they are already struggling to meet their major financial obligations and basic living expenses, the difference between payments of $333 and $167 may be quite substantial and distinguish a loan with affordable payments from a loan with unaffordable payments."[456]

The Bureau's recognition that $167 is a substantial amount for a struggling family applies to a $167 payment on a $500 loan as well. The Bureau's sound reasoning thus should also prohibit making a $500 loan without assessing its affordability.

9.4.4. The Bureau's analysis throughout the rule acknowledges the harm caused by even a relatively short series of payday loans.

The Bureau often recognizes the harm caused by even a relatively short series of payday loans that are repaid, which would seem to contradict its sanctioning a series of three loans with no ability-to-repay requirement.

For example, the Bureau notes the following:

> "[Consumers whose loan sequences are shorter may still suffer meaningful injury from reborrowing beyond expected levels, albeit to a lesser degree than those in longer sequences.

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[453] Assuming the median storefront borrower income of $22,476 per CFPB White Paper, resulting in 26 bi-weekly paychecks of $864.
[454] Supplemental Findings at 25 (Figure 6).
[455] 81 Fed. Reg. at 47974.
[456] *Id.*

> Even a consumer who reborrows only one or twice [meaning three loans total] will still incur substantial costs related to reborrowing or rolling over the loans."[457]

Similarly, the Bureau notes the following:

> "[A]pproximately 22 percent of payday loan sequences . . . are repaid after the initial loan is reborrowed once or twice. But even among this group, many consumers do not anticipate before taking out a loan that they will need to reborrow. These consumers cannot reasonably avoid their injuries,[458] and while their injuries may be somewhat less severe than the injuries suffered by consumers with long loan sequences, their injuries can nonetheless be substantial, particularly in light of their already precarious finances."

The Bureau also notes that while "dramatic negative outcomes" result from long sequences, there is harm from short sequences as well. It provides the example that for a $350 loan with a $15 fee, each reborrowing costs $45, so "after just three reborrowings, the borrower will have paid $140 simply to defer payment of the original principal amount by an additional six weeks to three months."[459] We note that, likewise, with a $500 loan at $15 per $100, the borrower may defer an original $167 for two weeks and another original $167 for four weeks, paying $77 to do so.

Finally, the Bureau's unfairness analysis finds that "substantial injury" includes a "large number of consumers [who] suffer a lower but still meaningful degree of harm."[460] As noted throughout this discussion, the harm caused by unaffordable exemption loans likely exceeds a "low degree." But even if it were low, given the high number of consumers exposed to it, it would still be substantial injury.

9.4.5. The notion that lenders will have incentive to screen out borrowers without the ability-to-repay is unconvincing.

The Bureau notes that lenders' concern about being repaid will likely motivate screening procedures that may mitigate harm.[461] But any mitigation this might provide should not be expected to be sufficient.

A lender's concern about being repaid does not equate to concern that a loan is affordable. The lender will be concerned that the borrower's incoming deposit on payday provides enough funds from which the lender can skim off the first $167 plus finance charges, which will often be the case, even on an unaffordable loan.

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[457] 81 Fed. Reg. at 47936.
[458] As noted in our discussion of the unfairness test at section 5.5 above, we object to conditioning the "not reasonably avoidable" prong on whether or not the borrower predicted the need to reborrow.
[459] 81 Fed. Reg. at 47925.
[460] 81 Fed. Reg. at 47936.
[461] 81 Fed. Reg. at 47941.

The Bureau often acknowledges that lenders may be consistently repaid, even while the loans are not affordable, leaving the borrower with insufficient funds to meet other obligations and expenses.[462] It acknowledges this even for periods much longer than the relatively short six weeks likely here.

9.4.6. The exemption is inconsistent with the Bureau's conclusions regarding borrowers' ability to predict their ability to repay.

Since it requires so little of the lender, the exemption ultimately puts the onus on the borrower to determine whether or not a three-loan series will be affordable. Yet the Bureau provides ample support throughout the rule for why borrowers cannot be expected to "self-underwrite," including tunneling and optimism bias. It also cites a study that generally supports that borrowers do not predict long sequences of payday loans. But that study also found that predictions about needing to reborrow one time versus not at all were also overly optimistic—that 60% predicted they would not reborrow within one pay cycle, but only 40 percent actually did not. The Bureau concludes that "[e]ven borrowers who believe they will be unable to repay the loan immediately—and therefore expect some amount of reborrowing—are generally unable to predict accurately how many times they will reborrow and at what cost."[463] This does not support an exemption that ultimately relies on a borrower's ability to predict affordability.

9.4.7. The costs of the exemption clearly outweigh the benefits.

In favor of the exemption, the Bureau primarily notes furthering the Dodd-Frank objective of facilitating access, largely by reducing compliance costs, particularly for small lenders.[464] The Bureau also notes that the exemption will permit loans for people who lack the necessary verification evidence to qualify. These two purported benefits clearly do not outweigh the costs of the substantial harm the exemption is likely to permit.

First, we are not aware that anyone has ever posited that the "access" objective means preserving access to unaffordable credit. What's more, "access" is appropriately construed broadly, as discussed at section 19.2 The Bureau's task is to consider access to credit generally, but it need not bend logic to permit lenders to continue making unaffordable, harmful payday loans.

We note that, in proposing the exemption, the Bureau invokes its exemption authority. We agree that Dodd-Frank provides the Bureau broad exemption authority, as necessary or appropriate to carry out the purposes and objectives of Title X. Where we object is that this particular exemption unnecessarily prioritizes one objective – access—by gravely undermining another—preventing unfair and abusive

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[462] 81 Fed. Reg. at 47998: "[s]uch consequences could occur prior to default – if the lender for a time was able to extract unaffordable payments from the consumer's account – or could occur in lieu of a default, if the lender is able to consistently extract payments that are not affordable."

[463] 81 Fed. Reg. at 47928.

[464] 81 Fed. Reg. at 47970, n.585. With respect to profitability, SERs reported that the SBREFA outline was not sufficiently flexible and would not allow for sufficient loan volume to sustain profitability (with an 82% reduction in loan volume, five of six SERs would be unprofitable). Yet the Bureau notes: "The Bureau is sensitive to the impacts that the proposed rule would have on small entities. To the extent small lenders are relying on repeated reborrowing and long loan sequences, however, the Bureau has the same concerns it has expressed more generally with this market." 81 Fed. Reg. at 47970.

practices.[465] (The Bureau seeks comment on whether, rather than relying on its exemption authority, it should use its UDAAP rulemaking authority instead. We would suggest that either way, the Bureau would be unable to reconcile these rules with the fundamental ability-to-repay principle central to the rulemaking.)

The Bureau suggests that the exemption appropriately balances the interest of providing strong consumer protections "with the aim of permitting access to less risky credit" that is "less likely to prove harmful." The Bureau notes that the protections "reduce the risk of harms from reborrowing, default, and collateral harms" from unaffordable payments.

It may well be true that credit extended under the short-term exemption is "*less* risky" than covered short-term credit today and that it "less likely to prove harmful." But we have seen no evidence that suggests that the risk of it is *acceptably low*, or that the loans are *unlikely* to prove harmful, which seem the only appropriate bars.

Second, the Bureau notes that this exemption may preserve access for those who cannot easily provide income documentation. This may be true, but it seems overemphasized relative to the impact of the exemption as a whole. The Bureau notes that it expects that storefront lenders will make covered short-term loans primarily under the exemption. This indicates that the exemption will be exploited to prevent underwriting, not that it is a narrowly tailored exemption for borrowers who cannot provide income documentation.

Finally, the Bureau's cost/benefit analysis of the rule as a whole only seems to affirm the inappropriateness of the exemption. The Bureau is required to discuss alternatives considered, and it notes that it considered a rule without the short-term exemption. It states that, without an exemption, payday loans would be less available because "[b]orrowers who had not recently had a payday loan but could not demonstrate an ability to repay the loan would be unable to take out a payday loan. It would also make taking out a second loan within 30 days of a prior loan more difficult, as this would only be an option for borrowers who could document an improvement in their financial capacity." This indicates only that *unaffordable* payday loans would be less available, which is exactly the purpose of the rule.

9.5. Vehicle Title Loans Are Appropriately Provided No Exemption, for Reasons That Also Discredit the Exemption for Payday Loans.

We strongly support no exemption from an ability-to-repay determination for vehicle title loans. Loss of a borrower's car can cause particularly severe harm, including an inability to get to work, school, or medical appointments. We further note that the 20% rate at which borrowers do lose their cars on short-term vehicle title loans makes an exemption from an ability-to-repay determination for this product wholly imprudent, particularly when, as the Bureau notes, a lender could repossess the car if the loan were not paid in full, even after the first loan in the sequence. But even if the repossession rate were lower, the harm is so severe that lenders should not ever be allowed to make a vehicle title loan without assessing ability-to-repay.

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[465] The Bureau also cites the objectives of facilitating innovation and, with respect to disclosures, ensuring consumers are provided timely and understandable information.

At the same time, we note that in important respects, the Bureau's rationale for excluding vehicle title loans strongly supports providing no exemption for payday loans either. The Bureau acknowledges with respect to vehicle title loans that it "is concerned that some consumers obtaining a loan under [the proposed exemption] would not be able to afford the payments required to pay down principal over a sequence of three loans." This concern is clearly applicable to both types of loans.

Further, the Bureau notes that borrowers may take extraordinary measures to repay vehicle title loans and, as a result, fail to meet other major financial obligations and basic living expenses. We agree, and the same is true for payday loans. Moreover, payday loans are often repaid unless the borrower takes extraordinary measures *to stop them from being repaid*, which often, even despite extraordinary measures, proves impossible.[466]

9.6. This Exemption Threatens State Laws in States with No Payday Lending.

Fourteen states plus the District of Columbia do not permit high-cost payday lending. Those state laws are particularly threatened by an exemption from an ability-to-repay determination for high-cost payday loans. We reference the letter, which the Bureau cites in the proposal, signed by several hundred national and State advocates urging the Bureau not to create any alternatives to the ability-to-repay requirement that would sanction a series of repeat loans.[467]

The Bureau's suggestion that three back-to-back balloon-payment loans made without underwriting with very high payments are "less likely to prove harmful" is very destructive to the efforts of the non-authorization states to preserve their protections. The Bureau's words may be used to claim that these loans are safe, when instead they are likely to cause substantial harm.

We do appreciate the Bureau's emphasis that it is not suggesting that any state, local, or tribal law should encompass only the exemption provisions,[468] and that these provisions would not preempt any state, local, or tribal.[469] But that emphasis is not likely to sufficiently defuse lender claims in state legislatures that the Bureau has sanctioned a safe framework for making high-cost, unaffordable payday loans.

9.7. The Bureau Offers No Meaningful Precedent for This Exemption.

As discussed at section 5.2 above, despite ample precedent for an ability-to-repay determination, the Bureau cites none for any analogous exemption from that requirement.

We note that the Bureau cites the FDIC Affordable Small Loan Guidelines as support for encouraging principal reduction, but we are unconvinced that those guidelines are appropriately invoked here. The FDIC guidelines prioritize affordability, including an APR no greater than 36% and a minimum loan term of 90 days (i.e., true installment loans)—hardly comparable to an approach sanctioning 650% APR or

[466] See, generally, our discussion of the proposed payments protections at section 13 below.
[467] See Letter to CFPB from groups in 13 states without payday lending, May 2016, *available at* http://www.neweconomynyc.org/2016/04/news-release-new-economy-project-allies-urge-cfpb-issue-strong-payday-lending-rule/.
[468] 81 Fed. Reg. 47971.
[469] 81 Fed. Reg. 47971.

higher loans being made with no ability-to-repay determination and structured as individual short-term single-payment loans.[470]

9.8. Other Details of Section 7, Including Responses to Bureau's Specific Requests for Comment.

Though we categorically oppose the exemption, there are several elements of its design that make it particularly harmful. We address those here, particularly in response to the Bureau's requests for Comment on specific elements of the exemption.

9.8.1. The maximum loan size of $500 is too high: §1041.7(b).

The Bureau solicits comment on the limit of $500. In its explanation of the limit, the Bureau notes that $500 is a common state law limit, while also noting that median loan amounts are in the $350-$375 range.[471] Median loan sizes much smaller than $500 do not support a maximum loan size of $500.

9.8.2. The loan sequences/borrowing history requirements are too weak: § 1041.7(c).

The loan sequence definition and limits and the borrowing history requirements each pose heightened risk of harm.

9.8.2.1. A 30-day time period defining loan sequence is insufficient here, just as it is insufficient in the ability-to-repay context. A stepdown on every loan within 12 months would be most appropriate: § 1041.7(d).

As we discuss at section 8.3 above, a 30-day proxy for an expense cycle is inappropriate for high-cost loan borrowers. A 30-day period can also be easily evaded; lenders could encourage borrowers to come back 31 days later and receive an additional loan of $500 rather than require the stepdown, leading to six loans of $500 each in a 12-month period.

A more appropriate period is clearly 60 days. But we would offer that in the context of an exemption permitting six loans per year with no ability-to-repay determination and exposing borrowers to excessive risk of harm, the most appropriate approach to loan sequence would be treat all loans within a rolling twelve months as part of the same loan sequence, requiring a principal stepdown on each of the six loans.

9.8.2.2. A short-term exemption loan after a longer-term exemption loan from the same lender should be prohibited: § 1041.7(c)(1).

The Bureau solicits comment on the proposed requirement that no short-term exemption loan be made when a covered short-term loan (other than the previous exemption loan in the series) or a

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[470] We note further that the Bureau's study of the Texas stepdown ordinances, though extensive discussion is not provided, does not seem to offer support for a principal reduction approach here. In studying a modest reduction in loan volume following concurrent implementation of statewide disclosure requirement, the Bureau found that the ordinances in Texas and Austin did not explain the decrease. CFPB Supplemental Findings at 67.

[471] The Bureau appropriately emphasizes that in states with a lower maximum limit, that lower limit would prevail.

covered longer-term loan (other than a longer-term exemption loan) is currently outstanding, regardless of the lender. This limitation is prudent as it reduces the risk of lenders moving borrowers into short-term exemption loans in order to mask lenders' lack of reasonable determinations of ability-to-repay on the outstanding loans, a clearly foreseeable evasion tactic that should be prevented.

But this prohibition should be expanded to bar a short-term exemption loan after a longer-term exemption loan from the same lender made under proposed § 1041.11 or § 1041.12 as well. The SBREFA outline did include a prohibition on a short-term exemption loan with a longer-term exemption loan outstanding. In explaining its removal of this prohibition in the proposal, the Bureau notes that it does not believe lenders or consumers have incentives to move from longer-term to short-term exemptions.

We disagree and urge that lenders be prohibited from making a short-term exemption loan when a longer-term exemption loan from the same lender is outstanding. First, we expect many lenders will in fact have incentive to make any additional loans they can to borrowers that do not have to be underwritten for ability-to-repay. This will be quick, easy money for many lenders.

Second, they may use longer-term exception loans as bridge loans to interrupt loan sequences and avoid presumptions of unaffordability. As discussed in section 8.10 above, we urge the Bureau to restart the presumption period if the lender makes any new loan, covered or not, exemption loan or not.

Third, the fact that a borrower seeks additional credit when another high-cost loan, with no ability-to-repay determination, is outstanding, suggests that a short-term exemption loan will be more difficult for that borrower to manage. A lender that made an unaffordable longer-term exemption loan should not be permitted to refinance that loan into a high-cost short-term loan with no ability-to-repay determination. Even if it is not from the same lender, if a consumer cannot afford to pay a longer-term exemption loan—likely designed far more affordably than a short-term exemption loan—the likelihood that a short-term exemption loan will be unaffordable is too great.

In explaining its removal of this prohibition from SBREFA, the Bureau also notes that information about longer-term exemption loans is less readily available than information on other covered longer-term loans. We recognize that under the current proposal (unlike SBREFA), longer-term exemption loans would not be required to report to RISs. But this would not prevent a lender from being able to check their own records and those of their affiliates and apply this important restriction on a same lender/service provider/affiliate basis.

The Bureau solicits comment on whether the rule could, alternatively, permit both exemption and ability-to-repay loans to occur within the same sequence while retaining the integrity of both. We strongly recommend against this as it is difficult to conceive how this would be achieved, and the exemption poses enough concerns as it is.

9.8.2.3. The proposed prohibition when a covered balloon loan has been outstanding in the last 30 days should be extended to 60 days: § 1041.7(c)(2).

Proposed § 1041.7(c)(2) prohibits short-term exemption loans within the reborrowing period following a covered short-term loan or longer-term balloon loan. That prohibition is appropriate, as lenders could easily use the exemption loan to evade the purpose of the cooling-off period and mask the unaffordability of the loans subject to the ability-to-repay determination. Consistent with our recommendation throughout, we urge this period be 60 days rather than 30.[472]

9.8.2.4. The limit of three loans in a sequence will not prevent harm: § 1041.7(c)(3).

Proposed § 1041.7(c)(3) prohibits a "loan sequence" of more than three covered short-term exemption loans, regardless of lender.[473] The Bureau justifies permitting three loans in a row based on its finding that 38% of new loan sequences end by the third loan without default.[474]

While a limit of three is better than a higher limit or none, we note that the Bureau appears to be sanctioning a repayment pattern that 62% of loan sequences do not meet. This data strongly suggest that a similar portion of borrowers cannot afford to repay a payday loan sequence of three loans—particularly since the leveraged payment mechanism coerces repayment of unaffordable loans from consumers who do not default. While the loans in the CFPB's study did not have principal stepdown requirements, those loans also often started at loan amounts less than $500 and often at prices lower than many exemption loans will carry.

9.8.2.5. Limit of six loans and 90 days' indebtedness is too high: § 1041.7(c)(4).

Section 7(c)(4) prohibits an exemption loan if it would result in the borrower having more than six covered short-term loans or more than 90 days' indebtedness in such loans over 12 consecutive months, including both ability-to-repay loans and exemption loans. These limitations, as the Bureau's discussion demonstrates, are well-rooted in precedent. But importantly, none of these precedents provide another framework whereby lenders may make additional loans *not* subject to the limits, as they could here. In this context, these limits are too high.

With respect to the six-loan limit, the Bureau notes that it is informed by the OCC/FDIC deposit advance guidance, which, with its limit of one advance per statement cycle coupled with a prohibition on another advance during the subsequent statement cycle, establishes a "supervisory norm" of no more than six loans in a year.[475] The Bureau also cites Washington State's limit of eight loans per year and Delaware's limit of five loans per year. We would add NCUA's limit of three loans per six months applicable to loans as short as 30 days long. In addition, the limit of three months' indebtedness in payday loans in 12 months according to the FDIC's payday loan guidelines equates to roughly six two-week loans.

With respect to the 90 days' limit, the Bureau cites the FDIC's payday loan guidelines just mentioned.

It is appropriate that these limits apply to both types of covered short-term loans (if the exemption is retained)—meaning that, when making an exemption loan, the lender must consider both exemption

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[472] Longer-term balloon loans can have particularly large final payments, extremely likely to affect a borrower's finances for far longer than 30 or even 60 days following. For example, a $2,500 Cash Time title loan in Arizona paid biweekly has 12 payments of $17, followed by a final payment of $2,673. On file with authors.
[473] We discuss the definition of "loan sequence" in section 3.5 above.
[474] 81 Fed. Reg. at 47979, n.628.
[475] 81 Fed. Reg. at 47980.

loans and non-exemption loans in the total days' indebtedness. But we note that the effectiveness of this approach in actually *restricting* total short-term loans will be limited because, as the Bureau expects, lenders will typically exhaust the six exemption loans before moving to ability-to-repay loans.[476]

None of the precedents cited apply limits for certain payday loans while permitting others to be made. We note in particular that the OCC/FDIC's deposit advance guidance limit of six is coupled with an ability-to-repay requirement based on a review of the borrower's actual income and expenses, as we urge the Bureau to do in this rule.

We agree that two overlapping limits—one based on number of loans, and one on days' indebtedness—is important, particularly to address 30- or 45-day loans, six of which could keep the borrower indebted in short-term exemption loans for most of the year. As the Bureau notes, borrowers of 30-day loans are more likely to live on a much lower, fixed income, typically Social Security, and are more vulnerable to long series of loans.[477]

While we have clear concerns about permitting any exemption loans, permitting the three-loan series to occur *twice* in twelve months is particularly unwarranted in light of all the data discussed throughout this section.

With respect to both the six-loan and the 90-day limit, the proposal would permit an exemption loan to be made even if the borrower is close to the limit due to earlier loans made in the previous 12 months, with the result that additional stepped down loans would not be permitted.[478] This approach seems inconsistent with the weight the Bureau places on the principal stepdown requirements. To reflect the intent of that protection, no loan should be permitted unless all three would fit within the prescribed limits. In the alternative, the loan should have a maximum principal value that corresponds to its place in the series (thus, if only one more loan is permitted, it would have a maximum principal of $167; if two, then $334).

The Bureau solicits comment on whether the limits should include loans with a term that falls partly within the 12-month period, as proposed, or whether they should count only loans consummated during the 12-month period. Given the significant harm the exemption already poses, the limits should include any loans that fall partly within the 12-month period.

The Bureau also solicits comment on whether the 90-days indebtedness limit, which is currently being measured by "contractual indebtedness," should be measured some other way. We recommend it be measured as the longer of contractual or actual indebtedness, both of which should be clearly identifiable in RIS data. Some unaffordable short-term loans may remain outstanding for a very long time when the borrower cannot afford them, and those days outstanding are clearly relevant to a 90-day limit. We note that Kentucky requires reporting of average days of indebtedness and uses actual indebtedness.

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[476] 81 Fed. Reg. at 48129.

[477] See discussion of the Bureau's findings in our discussion of the impact of payday loans on older Americans at section 2.3.2 above.

[478] E.g., Proposed Comment 7(c)(4)(ii): "A lender may make a loan that would satisfy the requirement under § 1041.7(c)(4)(ii) even if the 90-day limit would prohibit the consumer from taking out one or two subsequent loans in the sequence."

9.8.2.6. Clarify how the 12 months are counted, and that loans that defaulted over 180 days ago are still counted as "outstanding" in the past 12 months.

Proposed § 1041.7(c)(4) prohibits a short-term exemption loan that would result in the consumer having, during any consecutive 12-month period, more than six covered short-term loans "outstanding" or covered short-term loans "outstanding" for an aggregate period of more than 90 days. Proposed comments 7(c)4-1; 7(c)(4)(i)-1 and -2; and 7(c)(4)(ii)-1 and -2 give explanations about how those provisions apply.

There are two areas where additional comments are needed to prevent confusion. The first involves a loan that was "outstanding" within the past 12 months but is no longer considered "outstanding" under the proposed rule because the consumer has not made a payment in the previous 180 days. The second area of confusion involves how the 12-month look-back period is calculated.

Defaulted loans

The definition of "outstanding loan" could create confusion for implementation of these limits.[479] Because the proposed definition of "outstanding loan" excludes loans that have gone over 180 days without a payment, lenders might think that they do not need to count these in the six-loan or 90-day limit even if the loans were outstanding at earlier points within the past 12 months. There may also be confusion about how to count the number of days that loans are outstanding if they were not repaid on time.

To clarify the application to loans that are no longer "outstanding" by the rule's definition, a comment should be added addressing loans that were "outstanding" within some point in the previous 12 months but are no longer. We note that both examples in proposed comment 7(c)(4)(ii)—2 assume that each previous loan was repaid on its contractual due date. The Bureau should add additional examples of loans that were not repaid on their due date.

For example, if the consumer took out a 14-day loan 300 days ago and defaulted on it, that loan met the definition of "outstanding" only for 180 days from the day it was made.[480] Those 180 days were within the past 12 months, and thus the loan counts towards the six-loan limit, even though the loan is not currently "outstanding."

In addition, those 180 days when the defaulted loan was outstanding should count towards the 90-day aggregate period during which a consumer may have covered outstanding short-term loans. The consumer already had a covered short-term loan outstanding for more than 90 days in the previous 12 months, and thus, no additional short-term exception loan may be made until additional time has passed.

We also note that this situation would be much less confusing if the CFPB accepts our recommendation in section 3.7 above to expand the definition of "outstanding loan" to, at a minimum, any loan with a payment in the previous 365 days, not 180.

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[479] Proposed Comment 7(c)(1)-1.

[480] As discussed in section 3.7 above, we have recommended a clarification to ensure that loans without any payments are still considered outstanding for 180 days.

Calculating the look-back period

A second confusion arises involving the treatment of older loans. Proposed comments 7(c)4-1, 7(c)(4)(i)-2, and 7(c)(4)(ii)-2 all use any example of a lender making a 14-day loan. The examples state that the lender need look back only 351 days, not 365 days. That is, the examples are looking back 12-months from the end of the new loan, not from the beginning.

However, lenders must do both: ensure that *even the first day* of the new loan does not result in the consumer exceeding six loans or 90 days of aggregate debt rule in the previous 12 months, and also that *all additional days of debt* from the new loan will count toward the limits. In addition, lenders should not be allowed to look back only 320 days just because they make a longer 45-day loan.

Thus, we believe there is a two-step process:

- First, the lender must look back 365 days from the first day of a new loan. If the consumer has already had six loans or 90 days of aggregate debt, the loan may not be made.
- Second, if the first day of the loan does not violate the rule, the lender should consider whether the additional days in debt during the term of the loan will result in the consumer being in aggregate debt for more than 90 days in the previous 12 months. To make the calculations simply, lenders should use calendar months.
    - If the aggregate days in debt during the previous 365 days together with the new days for the term of the loan do not exceeds 90 days, the lender satisfies the requirements of this provision and the loan may be made. For example, if the consumer took out five previous 14-day loans and now seeks a sixth 14-day loan, the total aggregate debt will be no more than 86 days, regardless when the previous loans were made.
    - If the days the consumer is in debt in the previous 365 days together with the term of the new loan will exceed 90 days, then the lender can still satisfy the requirements of this provision if there are older loans that will roll off and the consumer will not have a period with more than 90 days of debt during any consecutive 12-month period. For example, assume a consumer seeks a new 45-day loan on March 1, 2017. The consumer has been in debt for 74 days in the past 12 months. But 30 of those days were in March of 2016. The lender can make a new 45-day loan because the 90 days will not be exceeded during any consecutive 12 months (not April 2016-March 2017, nor May 2016-April 2017).[481]

9.8.2.7. Non-covered bridge loans should be treated as we recommend for non-exempted short-term loans (§ 1041.7(d)).

The rule here again would not permit non-covered bridge loans to be counted in the 30-day periods in this section. This is prudent to prevent evasion. But as discussed in section 8.10 above, we urge (1) a broader definition of non-covered bridge loan to include any loan, covered or not, from the same lender/service provider or affiliate; and (2) that the loan reset, rather than toll, the time period (of 60 days).

[481] The lender should not be allowed to simply deduct the loan term from 365 days. If on March 1, 2017 the consumer had been in debt 88 days in the previous 12 months, but 45 of those days were March 1, 2016 through April 15, 2016, a deduction rule would allow the lender to ignore those days, even though the new loan would cause the borrower to exceed the 90-day limit during the April 1, 2016-March 31, 2017 period.

9.8.2.8. No income verification requirement.

The Bureau solicits comment on the removal of an income verification requirement since the SBREFA outline, which the Bureau notes is in response to concerns heard from SERs.[482] The Bureau notes that lenders will have a strong incentive to verify that consumers have sufficient income.

We oppose not requiring income verification. Requiring income verification is consistent with the principle that capacity to pay should be documented for all loans, even if such documentation will be significantly incomplete in this case. It may deter some lending when there is not reasonable income to suggest affordability. And it will provide important data to CFPB in evaluating lending under the exemption.

9.8.3. Other details of short-term exemption.

RIS requirement. Section 1041.7(a) would prohibit making an exemption loan if there were no RIS available.[483] This is important given that virtually any limits to this exemption are based on borrower history. Without the RIS requirement, the exemption would only be limited on a lender-by-lender basis. That would increase the risk posed by the exemption, particularly given the significant rate at which multiple lenders make loans to the same consumer.[484]

Open-end loans. The Bureau solicits comment on its exclusion of open-end loans from the exemption, noting this exclusion was not included in the SBREFA outline.[485] In light of the problems with short-term open-end loans generally (see section 6.3.2 above), we strongly oppose any exemption from ability-to-repay for those loans. We further note that we agree with the Bureau's concerns about providing an exemption for these loans—that a borrower could repeatedly draw down credit without the lender ever determining ability-to-repay and could reborrow serially on a single exemption loan. (We add that this concern about serially reborrowing are warranted for open-end loans even when the initial line is not exempt from an ability-to-repay determination, and should support subjecting each advance on short-term open-end loans to an ability-to-repay determination and to the closed-end reborrowing limitations of § 1041.6, as we suggest at section 8.11.)

Multi-payment loans with multiple finance charges. The Bureau solicits comment on the proposal to permit multi-payment loans with multiple finance charges to be exemption loans, unlike in the SBREFA outline. It would require that these loans be fully amortizing with substantially equal payments. Given the 90-day limit, permitting these does not appear to increase the risks the exemption poses beyond the unacceptably high level of risk it already presents. It does make the loan and indebtedness limits particularly critical. We agree that permitting a multi-payment loan with balloon payments would be inappropriate.

No-cost off-ramp approach. The Bureau explains why it rejected an off-ramp approach to the exemption, which would have permitted a consumer, if unable to repay a third loan, to repay it in an

[482] 81 Fed. Reg. at 47973.
[483] Proposed § 1041.7(a).
[484] Nonprime101 Report 7-A, "How Persistent is the Borrower-Lender Relationship in Payday Lending?", September 10, 2015.
[485] Fed. Reg. at 47977 (discussing proposed § 1041.7(b)(4).

additional four installments at no cost. The Bureau solicits comment on its decision not to include this off-ramp. We agree with the Bureau's concerns and conclusions regarding the off-ramp,[486] most significantly that it likely could not be designed in way to ensure borrowers are given a real opportunity to use it.[487]

9.8.4. Disclosures (§ 1041.7(e)).

We support the proposed disclosures if the short-term exemption loans are retained, while we note that even very well-designed disclosures, as these seem to be, will not significantly mitigate the harm caused by receiving an unaffordable loan.

We support requirements that the disclosures be clear and conspicuous, retainable, segregated, contain only the specified information, contain machine readable text, and be substantially similar to the model forms.

The Bureau solicits comment on, among other questions, the following:

- *Whether disclosures should be required on the second loan in a sequence in addition to the first and third.* We recommend so.
- *Whether disclosures should be required before consummation, as proposed, or whether they should be required sooner.* We recommend they be required at application and just before consummation.
- *Whether there are any circumstances in which foreign language disclosures should be required (as proposed, they are permitted if English is also made available upon request).* We recommend that the lender be required to provide disclosures in the language in which the transaction is conducted and, if that language is not English, in English as well.
- *Whether electronic disclosures, which the proposal permits for any loan, should only be permitted for an online loan.* Any in-person transaction should require paper disclosures; otherwise the likelihood is too great that the consumer does not see the disclosures in a timely manner or at all. Electronic disclosures should be permitted in addition to those paper disclosures, but not as a substitute.
- *Whether electronic disclosures should be permitted via text or mobile-app.* Disclosures via text or mobile-app should be permitted in addition to, but not instead of, disclosures on paper or by email. The requirement that the disclosures be retainable is important, and text and mobile notices are not easily retainable.
- *Other requirements for electronic delivery.* If any URL link is used, it should be at a persistent URL that is available to the consumer for at least three years after the final scheduled payment of the loan. However, we urge the Bureau to require that the full text of the disclosure be provided in the email itself so that consumers do not need to click through to see it. If the consumer revokes consent for electronic communications, or if an email is returned undelivered, the lender should be required to provide a paper disclosure by mail or in person.

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[486] The Bureau notes here that consumer advocates "have expressed supported" for the principal reduction approach. 81 Fed. Reg. at 47975. We clarify that while the undersigned consumer groups did not support the exemption in any way, shape, or form, we expressed a preference, should the Bureau proceed with an exemption, for the principal reduction approach over the off-ramp approach.

[487] The Bureau cites state regulator reports evidencing how rarely borrowers have actually been given off-ramps in states that provide for them as well as anecdotal evidence suggesting lenders discourage them, which is consistent with the experience that we have observed as well. 81 Fed. Reg. at 47975.

We have made similar suggestions in connection with the disclosures under proposed § 1041.15 (see section 13 below).

- *Whether E-SIGN requirements, not currently required, should be.* E-Sign should be followed for electronic communications and disclosures. While the proposed rule replicates much of the E-Sign Act, it does not require that consumers confirm their ability to receive and view electronic communications. Without that confirmation, all of the important disclosures and notices required through this rule may go to an incorrectly entered email address or an email address that is not actually available to a consumer without electronic access. It is not a difficult step to require consumers to simply click on a link in an email to confirm that they are able to receive information electronically.

10. LONGER-TERM LOANS WARRANT ENHANCED UNDERWRITING REQUIREMENTS: § 1041.9.

10.1. Overview.

High-cost longer-term loans pose particularly high risk of harm to consumers, including particularly high risk of inability to repay. Longer-term loans are not only longer by definition, they are likely to be even longer than the sequences of short-term loans. Longer-term loans are also likely to be much larger. The larger size combined with the longer term make the costs and potential harm much higher. The longer term also increases the risks of both default and collateral harms.

In some ways, the Bureau clearly recognizes these risks, but we fear that in others the proposal does not sufficiently account for them. This is particularly concerning as the Bureau often references lenders' ability to simply move borrowers into longer-term loans (as permitted by state law) with smaller, purportedly more affordable payments, if the borrower does not qualify for a short-term loan with a larger payment.[488] These references risk understating the difficulty many borrowers will have *sustaining* payments—even smaller ones—over time and should be accompanied by substantive provisions that more fully recognize that challenge.

As we discuss early in these comments, lenders are already shifting to longer-term loans (section 2.5.3) and are pushing for state legislative authorizations for longer-term high-cost loans (section 2.5.4). In addition, we discuss that evidence suggests that tomorrow's longer-term market will look more like the short-term market than it does today. Short-term covered loan borrowers are even more distressed than longer-term borrowers, and they are the longer-term borrowers of tomorrow (section 2.5.5).

Below, we discuss in more detail why longer-term loans can be even more harmful than short-term loans (section 10.2), and why particularly long-term loans (i.e., those longer than 6 months) pose particular risk of harm (section 10.3). We also discuss how lenders exploit weaker laws applied to open-end loans and are shifting to these as well (sections 10.6.1 and 10.6.2).

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[488] E.g., in its discussion of the ability-to-repay determination for short-term loans: "Thus, even if a lender concludes that there is not a reasonable basis for believing that a consumer can pay a particular prospective loan, proposed § 1041.5(b)(2)(i) would not prevent a lender from making a different covered loan with more affordable payments to such a consumer, provided that the more affordable payments would not consume so much of a consumer's residual income that the consumer would be unable to meet basic living expenses and provided further that the alternative loan is consistent with applicable State law." 81 Fed. Reg. at 47950.

Beginning at section 10.4, we discuss the proposed ability-to-repay determination requirements unique to long-term loans and offer the following feedback and recommendations:

We strongly support requiring a cushion to account for the significant income and expense volatility that should be expected over the course of a longer-term loan. But we urge the following to make the requirement more meaningful:

- The "term of the loan" for determining a cushion should include the actual loan term and the anticipated period by which refinancings will extend the original term;
- Require lenders to consider not only volatility experienced by similarly situated consumers, but also other clear indicators of volatility for the particular borrower, including a credit report showing delinquencies within the past year.
- Modify the Comments to make clear that the cushion should never be zero and that seasonal fluctuations should be considered.
- For loans longer than six months:
    - Require a cushion based on lookback the length of the loan term.
    - For open-end lines of credit, the period should be how long it takes the full credit line to be repaid making the minimum payments.
    - In the alternative, require an additional income cushion of 25%, a common measure of income volatility.

For verification evidence for longer-term loans for income and major financial obligations, require a lookback the length of the loan term.

Longer-term balloon loans should be required to be underwritten for 60 days following the last payment, not 30 days.

For open-end lines of credit:

- We support requiring a new determination both before opening the credit line and before increasing it. (In addition, as discussed in section 11.4.9, an increase in the credit line should also trigger a presumption of inability to repay if there are any indicia that the borrower is struggling to repay the existing credit line, such as a single missed payment, bounced payment, or sustained high credit utilization.)
- We also support requiring a new determination if the prior determination was more than 180 days ago.
- We support the proposal to require lenders to assume, when considering ability to repay, that an indefinite line of credit will be repaid in full within 180 days.

10.2. Longer-Term Loans Can Be Even More Harmful Than Short-Term Loans.

The harm from traditional two-week payday loans comes not only from their high rate but also their very short term and balloon payment structure. The CFPB has rightly focused many of its proposed protections on the particular problems that are triggered by short terms and by balloon payments.

But, as the scope of the proposed rule reflects, severe consumer injury can also come from longer-term installment loans even if they lack balloon payments. Indeed, in many ways, longer-term high-cost loans pose even greater risk of harm than short-term loans.

It is critical that the CFPB fully consider the severe harm that can come from longer-term loans even if the payment size is considerably smaller than with a balloon-payment payday loan. If the primary impact of this rule is merely to focus on the size of the payment in relation to the consumer's current, identifiable income and expenses, then it will fail to address the many other ways in which longer-term loans can be unaffordable and pose dangers to consumers.

Longer term loans tend to be larger than short-term loans. If a lender does not need to recoup the entire loan from a single paycheck, it can more easily increase the loan size. The median short-term loan in the CFPB's studies is $350.[489] The CFPB found that the median storefront payday installment loan is $1,000 and the median online loan is $2,400.[490] There is less difference in loan size between single-payment and installment vehicle title loans; both have a median of $700, but the average is higher for installment loans ($1,098) than for single-payment loans ($959).[491] But lenders may move into larger vehicle title loans in states where they cannot charge high rates for other installment loans. Pushing consumers into bigger loans pushes them deeper into debt. It also makes it harder for them to escape, either through their own means or through the assistance of friends, family members, charities or lower cost lenders—which research shows is often how borrowers ultimately escape unaffordable payday loans.

Longer-term loans can result in a longer high-cost debt trap. The median single-payment payday borrower gets stuck in 10 loans in 12 months, taken on a nearly continual basis.[492] The median days' indebtedness in 12 months is 199 days.[493] Consumers experience considerable harm in that time period, including collateral harms discussed above from sustained unaffordable payments. On a longer-term loan, the median consumer may be stuck making unaffordable, high-interest payments even far longer. The most common payday installment loan in the CFPB's survey had 12 biweekly payments—almost six months even if the consumer takes out only a single loan.[494] But refinancing of installment loans is common and will extend the time that the consumer is in a high-cost loan. For example, as discussed in section 11.4.1.2 below, while the vast majority of loans in Colorado have a term of six months, consumers took out an average of 3.29 loans per year, and 15% are in perpetual debt 365 days a year.[495] Moreover, payday installment loans with terms of a year or longer are also common.

Larger and/or longer loans can mean higher overall costs taken from the budgets of struggling families. As payday lender push consumers into bigger and longer loans, the fees and interest charges

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[489] CFPB Payday White Paper at 15.
[490] Supplemental Findings at 13.
[491] CFPB Report on Single-Payment Vehicle Title Lending at 6; Supplemental Findings at 13.
[492] CFPB Payday White Paper at 23, 25.
[493] CFPB Payday White Paper at 23.
[494] Supplemental Findings at 29. An industry study came to a similar result, finding a median term of 167 days (5.5 months) for storefront payday installment loans and 203 days (6.7 months) for online payday installment loans. Beales/Goel, *supra*, at 15. While that study also found that the majority of borrowers either repay their loans early or default before the maturity date of the original loan, even if they have refinanced, the study did not separate out the impact of early defaults on those averages.
[495] Administrator of the Colorado Consumer Credit Union, Colorado Payday Lending – Demographic and Statistical Information: July 2000 through December 2015 at 15, 22, 25 (Aug. 22, 2016) ("Colorado 2015 Demographic and Statistical Information"). Colorado's unique rebate structure lowers the cost of loans when they are financed early. That is unlikely to be the case in other states, where the opposite is more likely.

from those loans will mount. Even if the loan is the same size, a longer loan can be more expensive. A consumer who takes out a $300 balloon payday loan, pays $15 per $100, and rolls it over nine times pays $450 in fees. Speedy Cash offers a $300 loan at 430% APR with 39 biweekly payments. The interest on that loan is $1,635.

The high interest rates on longer-term loans compound when the loan is delinquent or defaults in ways that balloon payday loans do not. Installment loans that are priced with periodic interest may explode as interest and late fees are continually added to a delinquent balance. High rates can cause even tiny debts to mushroom astronomically.[496] Indeed, even 36% is a very high rate that can prove unaffordable for larger and longer loans. As mentioned earlier, Congress was driven to enact significant reforms to the credit card market due to the widespread harm caused by penalty rates that averaged 27% in 2008.[497] Though defaulting balloon loans cause cascading costs of their own, these do not typically include ballooning interest, given the fee per fixed dollar amount pricing structure.

A longer, multi-payment loan means longer exposure to the harms of a repeatedly-used leveraged payment device. A longer-term loan gives the lender repeated opportunities over an extended period of time to debit the consumer's account. With each payment, the consumer has the potential of suffering overdraft fees, NSF fees, late fees and returned item fees—both from the loan payment itself and from difficulties handling other expenses after the payment has been deducted.

In addition, as discussed in the next section, loans with especially long terms pose additional risk of harm.

10.3. High-Cost Loans With Especially Long Terms (i.e., More Than Six Months) Pose Particular Risk of Harm.

All of the harms discussed in the previous section are compounded if a loan has an especially long term. The longer the loan term, the larger the principal can be for a given payment size; the higher the overall cost; and the more likely that at some point the consumer will experience harm from the leveraged payment mechanism or aggressive debt collection tactics. In addition, longer loans pose their own unique dangers.

The longer the loan term, the greater the likelihood of significant income or expense volatility. The cornerstone of this rule is assessing a consumer's ability to repay a loan by looking at documented, identifiable income and major financial obligations. While the rule also requires lenders to leave a reasonable cushion for basic expenses and potential volatility, there are no specifics in the rule. The longer the loan term, the higher the probability that something will happen in the consumer's life that is either unexpected or unplanned and is not adequately accounted for in the residual income analysis. The U.S. Financial Diaries Project found that households experienced an average of 2 expense spikes and 2.5 income dips each year—an average of one or the other every 2.7 months.[498] While these spikes and dips do not occur at predictable, even intervals, clearly the longer the time period, the

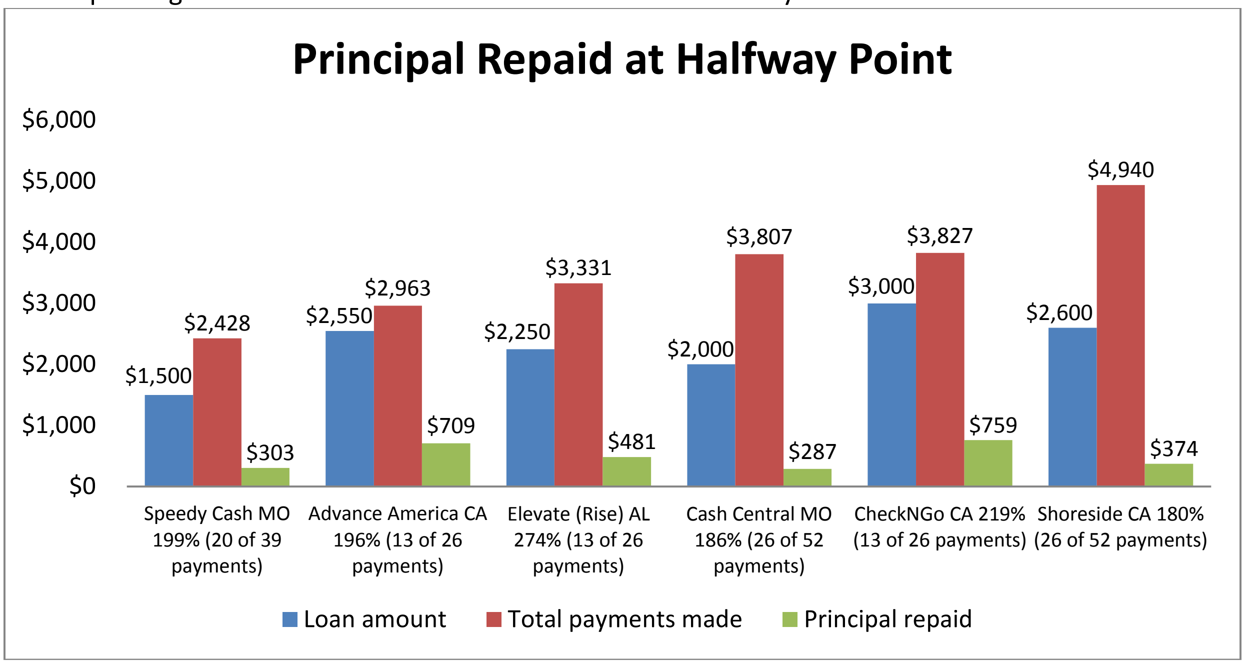
[496] See section 4.6.2 above.

[497] "2008 Credit Card Survey." Consumer Action, July 23, 2008. http://www.consumeraction.org/downloads/english/2008_Summary.pdf.

[498] Anthony Hannagan and Jonathan Morduch, "Income Gains and Month-to-Month Income Volatility: Household Evidence from the U.S. Financial Diaries" at 10, 25 (2015), http://www.usfinancialdiaries.org/paper-1.

greater the likelihood of an expense spike or income dip. For more, on income/expense volatility, see section 10.4 below.

Larger and longer loans are more likely to have payments for many months that cumulatively exceed the loan amount and yet do not significantly reduce the loan balance. Consumers have reasonable expectations that their payments will make progress in repaying a loan.[499] Many complaints in the CFPB's database are from consumers who are upset that they have been making payments for a long time with little to show for it.[500] While some of these complaints involve interest-only loans, payments that are nearly interest-only for many months can also result from high-rate loans with longer terms. As shown in the following chart, consumers can make hundreds or even thousands of dollars of payments with very little principal reduction. Not only do these loans frustrate consumer expectations, but a stubbornly high principal that does not go down can also make it more difficult for the consumer to escape a high-rate loan with a tax refund or funds from a family member.

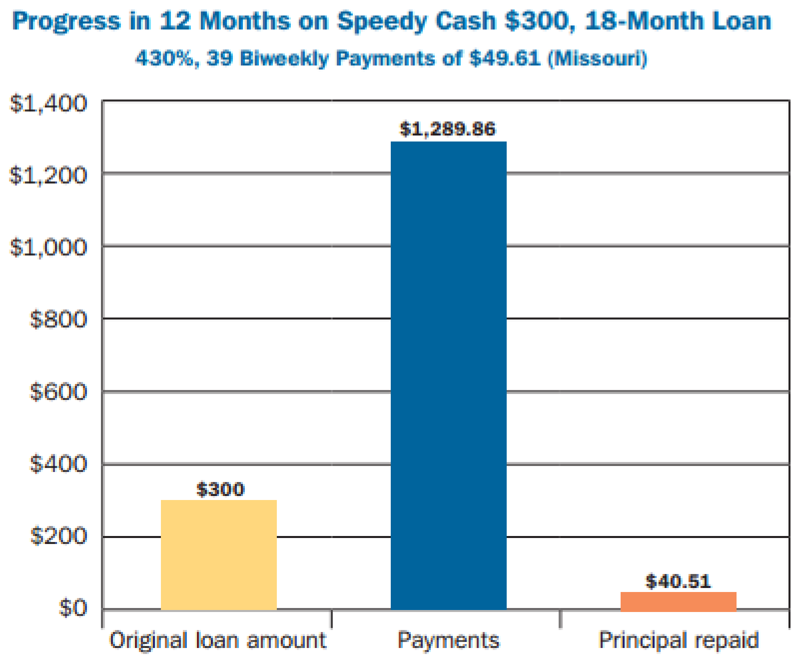


[499] With a very large balance and a very long term, as with a 30-year mortgage, nearly interest-only payments can also result from lower rate loans. But consumers who take out a 30-day year mortgage expect to be paying for years and do not expect significant principal reduction in the early years. Consumers who take out much smaller and shorter loans likely do not expect that they can make hundreds or thousands of dollars of payments without significantly reducing loan principal.

[500] See, for example, excerpts from the following three complaints from the CFPB's database:

- "I took a $500.00 personal loan with a company called Insta Loan …. When i looked at my balance it never decreased it only increased each time i made a payment. [A man in the office] told me that these kinds of loans are not set up for you to get out of, and that i 'll be making endless payments for years."
- "She took out a $3000.00 installment loan…. Paid [$4800.00] to the lender. However, only $700.00 of that has actually gone toward her principle and she still has an outstanding debt of $2100.00. At times there was not enough money in her bank account to cover those payments and she accrued about $200.00 in overdraft fees."
- "Niece took out loan with Castle Payday [for $800.00]… [Payments] were made to Castle Payday, for a total of $1100.00 …. They told me that all the payments I made were for interest, and that I still owed $1300.00."

While the biggest disparities happen on large loans, even smaller loans can have nearly interest-only payments for long periods of time if the term is long enough. For example, after making $1,289.86 in payments on a $300 Speedy Cash loan with 39 biweekly payments, the loan has only been reduced by $40.51.



Loans with terms longer than six months are more likely to default. An industry study found that the median storefront installment payday loan has a term of 167 days (5.5 months) and the median online loan has a term of 203 days (6.7 months).[501] Loans with a term above the median had significantly higher charge-off rates (36.90%) than those with terms below the median (30.74%).[502] The study concluded longer loans may perform more poorly due to debt fatigue or a higher likelihood of unexpected income or expense changes that make repayment more difficult.[503] Even if the borrower does not default, the longer that a vulnerable borrower has to cover a loan payment on top of other expenses, the greater the chance that it will not be sustainable.

The longer the term of the loan, the greater the likelihood that the consumer will, at some point, become delinquent and suffer from aggressive debt collection practices. For example, litigation against CashCall in California showed that borrowers struggled with their loans but almost always made some payments. While defaults were 35% to 40%, two-thirds of borrowers were late by 30 days or

[501] Beales/Goel, supra, at 15.
[502] Beales/Goel, supra, at 25.
[503] *Id.* at 25-26. The paper characterized debt fatigue as "at some point, borrowers are no longer willing to continue making payments." *Id.* at 25. But debt fatigue is more properly understood as the cumulative impact of unaffordable payments – an unwillingness or inability to continue letting the loan payment interfere with other obligations and basic expenses. Consumers may be especially unwilling to continue struggling with an unaffordable payment if they cannot see progress in repaying the loan and the end is not in sight.

more at some point.[504] Another case revealed that CashCall made 84,371 debt collection calls to its 292 West Virginia borrowers—an average of more than 288 calls per person.[505]

Longer terms increase the chance of other collateral consequences of unaffordable payments. The Bureau's payments data clearly show the impact of unaffordable payments—even those far smaller than typical balloon payments—on longer-term loans. See section 9.2.1.1 for further discussion. In addition, narratives of complaints filed with the Bureau provide evidence of the collateral harms that high-cost longer-term loans cause, including trouble meeting other expenses and overdraft fees.[506]

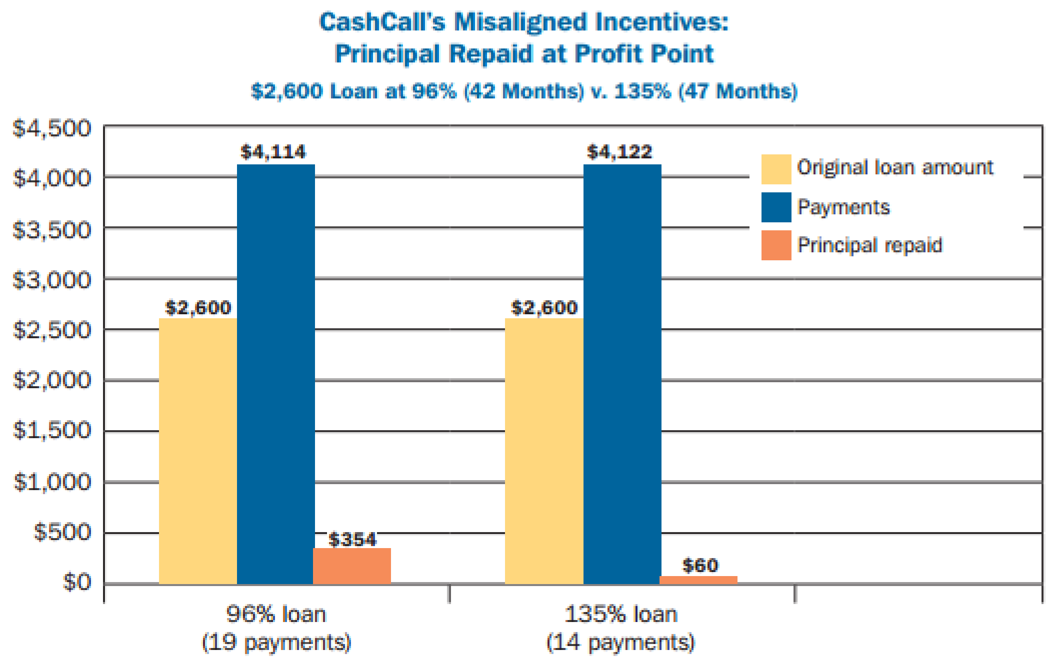
Long terms increase misaligned incentives because there is a higher possibility that the lender will recover the loan amount, and maybe a profit, even if the consumer eventually defaults. As the CFPB has recognized, with high-cost loans, lenders may be able to profit even if the consumer eventually defaults.[507] NCLC illustrated in its report on high-cost installment loans, when a loan has an especially long term, it is more likely a consumer who defaults well short of full term can still be a profitable customer. For example, as shown in the following chart, litigation against CashCall exposed that the lender started making a profit at month 19 on its 42-month loan, and could turn a profit after only 14 months once it increased the interest rate and lengthened the term to 47 months.

[504] Expert Report of Margot Saunders at 14, Attachment 2 to Declaration of Arthur D. Levy in Support of Response to Motion for Summary Judgment on Unconscionability Claim filed by Eduardo De La Torre, Lori Saysourivong, De La Torre v. CashCall, Inc., Case # 3:08-cv-03174-MEJ (N.D. Cal. filed Oct. 21, 2013).

[505] West Virginia *ex rel.* McGraw v. CashCall, Inc. et al., Final Order on Phase I of Trial: The State's Debt Collection Claims, Sept. 10, 2012, at ¶¶ 24 (number of calls), 49 (number of consumers), *available at* http://www.nclc.org/images/pdf/unreported/cashcall_phase_I_debt_collection_decision.pdf.

[506] CRL, *Migration*, *supra*, at 5, n.45-48 (citing CFPB Complaint Database complaint numbers and excerpts from several borrowers harmed by longer-term loans).

[507] "When a loan has a high total cost of credit, the total revenue to the lender, relative to the loan principal, enables the lender to profit from a loan, even if the consumer ultimately defaults on the loan. For example, for a $1,000, 12-month loan with a 300 percent interest rate and typical amortization, a lender would typically have received $1,608 after only six months. Moreover, even if defaulted loans are not themselves profitable, lenders can weather such losses when the performing loans are generating such high returns." 81 Fed. Reg. at 47989.



The precise profit point for other lenders is less clear. But even generously assuming that the lenders need to recover 150% of the loan in order to cover their expenses, several loans on the market today that have terms of one year or longer may turn a profit with fewer than half of the payments:

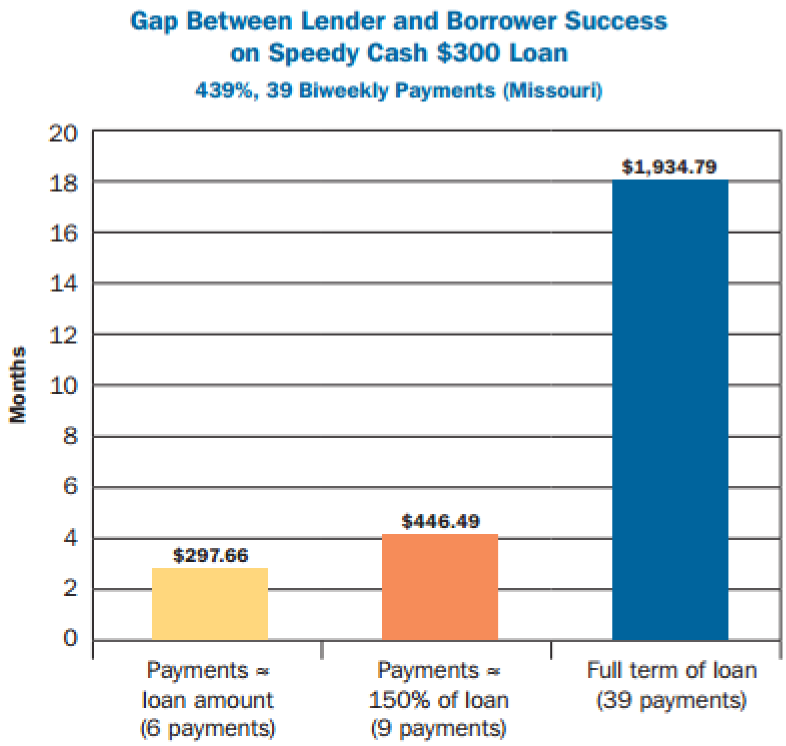
- On Elevate's Rise $2,250 loan at 274% in Alabama, lender success could require only 14 of 26 biweekly payments.
- Cash Central (a subsidiary of Community Choice Financial) could begin turning profits after 10 months of payments on a 2-year loan of $2,000 at 185% in Missouri.
- Advance America recovers 150% of the amount loaned after only 16 of 26 biweekly payments on its $2,550, 196% loan in California.[508]

Small loans with disproportionately long terms put consumers in an extended debt trap with potential harm that likely outweighs the possible benefit. A larger, longer-term, affordable loan that creates wealth can be a beneficial experience. It can help a consumer to buy a home, obtain transportation to a job or go to college. But a small loan has a smaller benefit. Small loans are more likely to cover ordinary expenses of the type that are likely to recur and do not build wealth. Thus, when a small loan with a high rate is stretched out over an inordinately long term, the dangers of the long term can easily outweigh any benefit from the loan.

Small but long loans have an especially high potential for profitable defaults and weak underwriting. As discussed later in these comments, the proposed rule has the potential to steer lenders into stretching out the loan terms on small loans—either on the original loan, or on a refinancing in order to avoid a presumption of inability to repay. But small high-cost loans with long terms provide extreme disincentive to determine ability to repay and high risk of prolonged collateral harm. These problems

[508] NCLC, Misaligned Incentives at 18.

are illustrated in the Speedy Cash $300, 18-month loan portrayed in the following chart, taken from NCLC's report on Misaligned Incentives.[509]



A rule that focuses on front-end underwriting with only vague references to the impact of long terms may not adequately protect consumers from the dangers of longer loans. Weaknesses in facially plausible ability-to-repay determinations may not become actionable until the CFPB can examine and study portfolios of longer-term loans that have run their course. Instead, the rule must account for the special risks of longer terms and long strings of refinancings. We have made several suggestions throughout these comments to address the dangers of longer terms, particularly with respect to the ability-to-repay determination generally at section 6 and for longer-term loans in particular in the remainder of this section, as well as with respect to refinancings of longer-term loans at section 11.

10.4. Income and Expense Volatility Is Expected and Must Be Adequately Accounted For: § 1041.9(b).

Income and expense volatility is a way of life for many Americans and is a particularly acute challenge for lower-income and credit-impaired individuals. We appreciate the Bureau's general recognition that this reality should impact the ability-to-repay determination for longer-term loans. Among other provisions, we support the proposed additional requirement that a reasonable ability-to-repay determination for longer-term loans include "appropriately account[ing] for the possibility of volatility in a consumer's income and basic living expenses during the term of the loan."[510]

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[509] NCLC, Misaligned Incentives at 22.
[510] Proposed § 1041.9(b)(2)(i)(F).

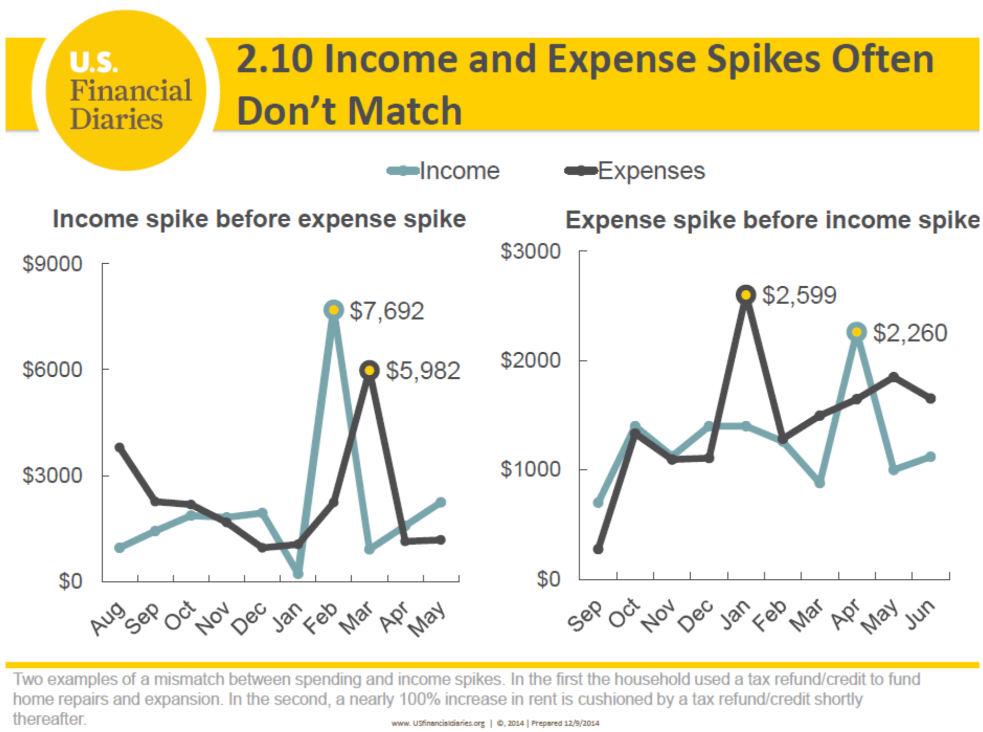
We urge that this proposal be strengthened by ensuring a more meaningful residual income cushion. In addition, lenders should be explicitly required to take a longer look back at the borrower's residual income patterns when making longer-term loans. In addition, as discussed in section 11 below, additional protections on refinancing are necessary in order to strengthen incentives to appropriately account for volatility.

10.4.1. Income/expense volatility is common, and expense spikes are typically outside of the borrower's immediate control.

Income and expense volatility is common. Income is especially volatile for lower-income households, and the impact of any income/expense volatility is most acute for lower-income households.[511]

In addition, as we note in the context of projecting basic living expenses in section 6.2.3, data strongly suggest that expense spikes are typically outside of the consumer's immediate control. The U.S. Financial Diaries research reveals a lack of correlation between income and expense spikes.[512] It found that that 61% of expense spikes occur when there is no income spike, and 33% occur when income is below average.[513] These suggest that residual income as a whole is also highly volatile. They also suggest that borrowers cannot easily reduce expenses at will.

The chart below from U.S. Financial Diaries shows demonstrates the mismatch:



[511] See section 10.4.1.

[512] http://www.usfinancialdiaries.org/blog/2015/2/13/spikes-dips-and-the-perils-of-predicting-income-and-expenses.

[513] Overall correlation between monthly income and expense is .43, ranging from .53 for poor households to .36 for better off households (spending more decoupled from income for better off households). *Id.*

10.4.2. Determining ability-to-repay and the income/expense cushion "during the term of the loan" should include actual and anticipated refinancing: § 1041.9(b)(1)(i) and Comment 9(b)(2)(i)-2.

Proposed § 1041.9(b)(1)(i) requires consideration of ability-to-repay the loan "according to its terms"—that is, without refinancing or reborrowing. Proposed Comment 9(b)(2)(i)-2 requires lenders to account for volatility "during the term of the loan." The longer the time period, the more significant the expected volatility. Employment changes that are not anticipated are more likely over the longer term. Similarly, while large unplanned expense are not anticipated every month, they should be over longer periods.

Lenders should be required to consider not only the actual term of the loan but also the full time that the consumer is expected to be in debt, from origination to final payoff. If lenders can keep consumers in serial refinanced loans without accounting for the volatility expected over the entire time period that the consumer is making payments, the requirement to account for volatility will be inadequate. For example, if the lender makes 6-month loans and refinances the consumer repeatedly so that she is in debt for two years, the lender will never have considered the volatility that is likely over a two-year period.

In assessing the likely volatility over the relevant time period, the lender should initially assume the median number and point of refinances. For example, if the median 6-month loan is refinanced twice after three months, then the lender should assume that the term is 12 months.

If a particular consumer has refinanced more than the median, then the lender should be required to account for the cushion required for the remainder of the loan term. (As discussed in section 11.7, however, a simpler and more protective approach would be to prohibit (or impose a strong presumption before) a second refinancing.)

We recognize that some consumers may repay their loans sooner than the original term, including possibly some consumers who have refinanced.[514] But lenders should never be allowed to consider a period shorter than the original term. The lender has a duty to consider ability-to-repay the loan on its actual terms. Even if some consumers pay off their loans early, every consumer should be determined able to sustain the loan for its full term. A portfolio-level pattern of early payoffs also should not excuse lenders from the need to add additional cushion or to consider the potentially longer term for consumers who refinance. Here again, the refinancing may be due to an inadequate cushion, and it subjects the consumer to a longer period in debt. Loans may also be paid off early for reasons that negate, rather than affirm, ability-to-repay—i.e., the consumer may have gotten help from a family member, charity, or credit union to escape unaffordable debt.

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[514] One industry study found that although the average payday installment borrower takes out 1.36 loans, the average total sequence is only 67% of the original term. Beales/Goel at 43. However, the study does not appear to have separated out the impact of defaults. The study only finds that "at least 75% of borrowers have resolved their debt by payment *or default* on or before the maturity date of the original loan." *Id.* (emphasis added). Clearly, defaulted loans end before their term. Those defaults bring down the average. The averages cited also appear to include loans that were not refinanced, including first payment defaults. We also note that a lender that is able to make a profit on portfolios with an average term well below full term have especially skewed incentives to underwrite appropriately. *See* NCLC, Misaligned Incentives.

10.4.3. The proposed "cushion" is critical, but the rule's approach to it considerably undermines the requirement: Comment 9(b)(2)(i)-2.

Proposed Comment 9(b)(2)(i)-2 elaborates on the required consideration of volatility, stating that a lender complies with this requirement by "reasonably determining an amount (i.e., a cushion) by which the consumer's residual income must exceed the sum of the loan payments under the loan and of the amount needed for basic living expenses."

The Comment then notes that the cushion is reasonably determined if, essentially, it:

- assumes a level of volatility "experienced by similarly situated consumers during a similar period of time"; *or*
- is zero, based on a reasonable determination that a particular consumer is unlikely to experience such volatility "notwithstanding the experience of otherwise similarly situated consumers during a similar period of time, such as if a consumer has stable employment and receives a salary and sick leave."

The first standard is vague and problematic; the second risks sanctioning routine exclusion of any cushion at all. The Bureau does not provide specific lender/borrower scenarios in the Commentary.

While we strongly support a required cushion for longer-term loans, we have serious concerns about the parameters the proposal provides for what constitutes a "reasonably determined" one.

First, we note, as discussed at section 6.2.3 above, that the starting point for this calculation is already a cushion of zero, resulting from the general ability-to-repay determination that provides an overly narrow category of those deemed "basic living expenses." That makes the inclusion of a legitimate cushion for longer-term loans all the more important.

Second, the second standard in the Comment could give the misleading impression that it would ever be appropriate for a lender to assume no income/expense volatility. The scenario provided could be read to suggest that so long as a borrower has stable employment and sick leave, no cushion is required. But is not clear as to how long a period constitutes "stable" and does not address expense volatility at all.

Third, and related, we fear that the Bureau's Commentary conveys an overly narrow view of when and why a borrower may experience income or expense volatility. The only example it provides in the Comment addresses income, and even that example is far too limited. Even stable income does not eliminate the need to deal with medical expenses and many other types of sporadic expenses that everyone experiences, like winter utility bills, auto repairs, back-to-school expenses, holiday gifts or a winter coat. In the discussion of the rule, the Bureau addresses volatile expenses in one scenario, and only in the context of a borrower's having health insurance indicating that the borrower's health expenses may not be expected to rise. Such an assumption would be unfounded; even those with health insurance rarely have 100% of their medical costs covered and still may experience spikes in medical costs. Indeed, many consumers have annual deductibles which result in significant volatility from the end of one year to the beginning or another, or maximum annual coverage limits that have a similar impact at a later point in the year.

Additional discussion indicates that the Bureau in fact expects that most borrowers have volatility that would require a cushion. It notes that "occasional reductions in hours . . . or occasional spikes in expenses (such as an occasional spike in a utility bill) *are very much to be expected* over the course of a longer-term loan."[515] And it references "ordinary volatility" as something that we should expect. But its actual proposed regulation leaves little assurance that volatility will be sufficiently accounted for.

Fourth, lenders cannot take too narrow a view of "similarly situated." The requirement to account for volatility must require an adequate cushion for the *unexpected or unplanned* expenses that hit *everyone*. It cannot be seen as a narrow requirement to identify particular sources of vulnerability for a specific consumer and account only for those. A major cited justification for the high-cost lending market is the routine volatility in people's lives and the difficulty that LMI families have in coping with that volatility. *All* borrowers of covered loans face volatility, and lenders should not be permitted to disregard it simply because there may be no study that focuses on a borrower with the precise characteristics of the borrower at hand.

Fifth, lenders should be required to consider the time of year when they account for volatility. For example, a bigger cushion for utility payments must be built in during winter months, and, in warmer climates, during summer months. Most consumers can be expected to incur extra expenses in December. Indeed, lenders have noted increased loan volume in December, so the expense spike should be anticipated.[516]

Finally, as discussed in section 11 below, high refinancing rates may signal that a lender is not providing an adequate cushion for volatility. Consumers who borrow before the term of a loan ends—especially if before the first loan has been substantially repaid—may have been left without enough resources to manage volatility.

In light of our concerns, we have several recommendations. First, for all longer-term loans, in addition to considering volatility experienced by similarly situated consumers, the lender should be required to consider other clear indicators of volatility for the particular borrower, including a credit report showing delinquencies within the past year. (We address consideration of the credit report in detail at section 6.3.5 above; we emphasize here that it should be a factor in determining the cushion.)

Second, the Comments should be modified to make clear that the cushion should never be zero and that seasonal fluctuations should be considered.

Third, for loans longer than six months, the standards for determining a sufficient cushion should be higher. Six months is the approximate median for both storefront and online installment loans in the large study noted in section 10.3 above, which found that default rates on loans longer than the median were higher than those with terms shorter than median. As the Bureau notes, the NCUA has also expressed concern that loans longer than six months may have unintended negative consequences.

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[515] 81 Fed. Reg. at 48013; Diana Farrell & Fiona Greig, Weathering Volatility: Big Data on the Financial Ups and Downs of U.S. Individuals (2015), https://www.jpmorganchase.com/content/dam/jpmorganchase/en/legacy/corporate/institute/document/54918-jpmc-institute-report-2015-aw5.pdf; Anthony Hannagan & Jonathan Morduch, Income Gains and Month-to-Month Income Volatility: Household Evidence from the US Financial Diaries (2015), http://www.usfinancialdiaries.org/paper-1.

[516] *See*, *e.g.*, Enova Internat'l, Inc., Annual Report (Form 10-K), at 65 (Mar. 7, 2016).

For loans longer than six months, the Bureau should require a cushion determined based on review of a consumer's degree of financial stability looking back the length of the loan term. For open-end lines of credit, the period should be how long it takes the full credit line to be repaid making the minimum payments.

This might involve review of actual transaction activity, which shows both income and expenses. It could also consist of proof of income (via paystubs with year-to-date information, tax returns, or employer statements of income) and review of a credit report for delinquencies dating back the length of the loan term. This recommendation is consistent with proposed Comment 9(b)(2)(i), which notes that accounting for volatility requires considering the length of the loan term because the longer the loan term, the greater the possibility that residual income could decrease or basic living expenses could increase during the term. But it is more concrete and, for particularly long loans, necessary to help ensure meaningful ability-to-repay determinations.

In the alternative, for loans longer than six months, the Bureau could require that lenders discount the borrower's income by 25%. As Pew has noted, 25% is a common measure of income volatility, and studies have shown that more than half of households experience at least this level of volatility over the course of a year.[517] The U.S. Financial Diaries found that low-income households in their study experienced a 25% decline in income an average of 2.5 times per year.[518]

10.4.4. As proposed, there should be no assumption of accumulation of savings: Comment 9(b)-2.ii.B.

For longer-term loans, proposed Comments 9(b)-2.ii.A and B provide two indications that the ability-to-repay determination is unreasonable. One, as for short-term loans, is an assumption that the consumer will obtain additional consumer credit. See section 6.3.6 above for our support of that comment, which also applies here.

The second, unique to the longer-term determination, is an assumption that a consumer will accumulate savings during the longer-term loan that will enable the consumer to make payments. We support this example of an unreasonable determination. Little if any evidence would support a likelihood that high-cost loan borrowers will accumulate savings during the course of a longer-term high-cost loan.

10.4.5. Verification evidence should be required looking back the length of the loan term, for loans longer than six months: §1041.9(c)(3)(ii)(A).

As noted above in the context of the cushion, the Bureau's Commentary provides that income or expense volatility is greater the longer the loan term. At the same time, the Bureau notes in its discussion of verification evidence required for making a reasonable determination that while it "believes that, generally, the term of a loan will affect the period of time for which a lender will need verification evidence in order to [make a reasonable determination of ability to repay,] . . . it does not

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[517] Memo provided by The Pew Small-Dollar Loans Project, on file with authors.
[518] Anthony Hannagan and Jonathan Morduch, "Income Gains and Month-to-Month Income Volatility: Household Evidence from the U.S. Financial Diaries" (2015), 10, 25, http://www.usfinancialdiaries.org/paper-1.

believe it is necessary or appropriate to require verification evidence covering a lookback period of a prescribed length."[519]

The Bureau further notes that the sufficiency of the history may depend on the loan term of the covered longer-term loan and the consistency of the income shown in the verification evidence the lender initially obtains. As an example, in discussion, the Bureau states that the lender's practice for making a six-month loan may be to obtain three recent receipts of net income, but if these show significant variation, then projecting net income based on the highest receipt would not be reasonable.

While we agree with that assessment, we are concerned this example sanctions obtaining six weeks of income as sufficient for projecting net income for a six-month, or potentially significantly longer, loan for a population of consumers who have significant income volatility.

Instead of this approach, we urge a more specific one, consistent with our recommendations related to a cushion requirement above. The Bureau should require verification evidence supporting a period as long as the loan term. For open-end lines of credit, the period should be how long it would take the full credit line to be repaid making only minimum payments. As noted above, lenders can use account transaction data, paychecks with year-to-date information, tax returns, or employer statements verifying income to corroborate past income.

10.5. Longer-Term Balloon Loans Should Be Underwritten for 60 Days Beyond the Loan Term: § 1041.9(b) and (c).

For longer-term loans with a balloon payment, the proposal requires that a reasonable determination conclude sufficient residual income for 30 days following the highest payment.[520] Again, for reasons noted in section 8.3 above, we urge this period be 60 days rather than 30 and that it run from the last payment rather than the highest payment, particularly given how large these balloon payments often are.

10.6. Longer-Term Open-End Loans Warrant Special Considerations for the Ability-to-Repay Determination: 1041.9(b)(1).

In section 6.3.2 above, we describe how short-term open-end lines of credit are typically evasion products and should be treated as such. Longer-term high-cost open-end loans, too, have a history of being used to evade consumer protections, and they pose particular risk of harm to consumers. The provisions applied to these products must be strengthened to ensure they adequately protect borrowers from harm.

10.6.1. High-cost lenders have a history of using longer-term open-end credit to evade consumer protections.

High-cost lenders have a long history of using open-end credit to evade consumer protections. Styling a loan as open-end credit has several advantages for predatory lenders.

[519] 81 Fed. Reg. at 48016.
[520] Proposed § 1041.9(b)(2)(ii).

Open-end credit can exploit gaps in state usury caps or other state laws. Many states have no rate cap, or a looser one, for open-end lending.[521]

Lenders evade other state laws with open-end products as well. For example, as noted earlier, Virginia places restrictions on closed-end payday loans but not on open-end ones. Consequently, payday lenders have moved to open-end loans.[522]

All Credit Lenders offers an open-end line of credit that uses the consumer's debit card as an access device. The lender advertises a 24% APR, but also charges an "account protection fee."[523] The Illinois Attorney General has sued, alleging that most, if not all, borrowers were enrolled in the account protection fee and that the additional fee—at least $11 for every $50 outstanding balance—was used to shroud the true cost of borrowing.[524]

Advance America previously offered the Choice Line of Credit, an open-end line of credit of up to $500 at 6 percent interest along with a monthly participation fee of $149.95. The State of Pennsylvania claimed that the fee structure was designed to evade the state's usury law. In February 2015, Advance America agreed to a settlement of $8 million in restitutions and was required to forgive approximately $12 million in unpaid balances.[525] But other states, like Virginia, have not yet had success stopping open-end evasions.

Misleading APR disclosures for open-end credit make it seem less costly than it really is. Regulation Z has significant gaps in the APR disclosure required for open-end credit. In general, only periodic interest must be included in the open-end advertising APR, not any fees.[526] Thus, the APR disclosed could be dramatically understated. A credit line that does not charge periodic interest does not need to disclose any APR at all or may even be legally allowed to disclose an APR of 0%.

Advance 'Til Payday, for example, discloses a 0.0% APR on its open-end credit line that requires an $80 monthly participation fee on a $100 credit line.[527] The true APR is 960%, which Advance 'Til Payday would be required to disclose if instead it made a one-month closed-end loan of $100 with an $80 finance charge.

Although the CFPB is aware of this gap in Regulation Z and is using a more effective measure of the total cost of credit, that does not change the ability of lenders to slap a price (in the form of an APR)

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[521] NCLC, Misaligned Incentives at 43-51.
[522] *See* "Lenders Find Loopholes Around Virginia Law Limiting Payday Loans," FoxNews.com (Dec. 31, 2008), http://www.foxnews.com/politics/2008/12/31/lenders-loopholes-virginia-law-limiting-payday-loans/.
[523] *See* https://www.allcreditlenders.net/#.
[524] Complaint for Injunctive and Other Relief, Illinois vs. CMK Investments, Inc. DBA All Credit Lenders, Inc., (Cir. Ct. of Cook Co., IL, filed Mar. 18, 2014), http://www.cfpbmonitor.com/files/2014/03/ALL_CREDIT_LENDERS_03-18-2014_16-26-531.pdf.
[525] Boyle, Jim. "Advance America Agrees to $8M Settlement with Pennsylvania." *Legal Newsline Legal Journal*. February 12, 2015. http://legalnewsline.com/news/254880-advance-america-agrees-to-8m-settlement-with-pennsylvania.
[526] Treatment of these fees under Regulation Z is unclear. The fees would be included in the advertising APR only if they are considered *both* a finance charge and a periodic rate. Lenders may argue that a fee is a participation fee, which is not a finance charge. Or they may charge the fee as a flat fee and not as a periodic rate. Although it is possible that even a flat fee could be viewed as a periodic rate if it is tied to a time period.
[527] Periodic statement on file with the authors.

that appears reasonable on a far higher-cost loan. And to the extent that a state usury cap is based on the APR, the weakness of Regulation Z undermines the usury cap.

Indecipherable pricing for open-end credit confuses consumers, legislators, and potentially employers. On its Elastic line of credit, Elevate discloses "easy to understand pricing" of a 5% cash advance fee plus a minimum charge of $1 to $80 on the outstanding balance (after each payment, due every payday).[528] But there is nothing easy about it. In order to figure out the cost of a $300 loan, even an APR expert has to examine the terms and conditions, figure out the payments and charges using an Excel spreadsheet, and plug them into a software program to come up with an estimate that the true APR appears to be over 160% and the loan takes 14 weeks to repay.

As discussed in section 2.5.4 above, payday lenders are active in state legislatures seeking authorization for high-cost open-end lines of credit. The industry may be counting on legislators' difficulty in understanding (or plausible deniability of) the true rate. In Arizona, for example, the industry pushed a "Flex Loan" bill that purported to carry a 36% interest rate but that also had "customary" fees up to one-half of one percent *per day*.[529] With fees included, the true APR would have been 218%. Yet due to loopholes in Regulation Z, it is possible that only a 36% APR would be disclosed, misleading consumers. Other open-end proposals exploiting the APR loophole have pushed in Alabama, Oklahoma, Kentucky, and South Dakota, as well as in Tennessee where the Flex Loan product became law.[530]

We have also seen employer-based loan products with obscure open-end pricing that may make it difficult for employers to realize that they are enabling predatory lending.

Lenders can use open-end credit to avoid rollover rules for short-term loans with longer-term lines of credit. The only minimum payment required on the Advance 'Til Payday $100 line of credit was the $80 monthly participation fee. That is effectively a traditional 30-day payday loan with a monthly rollover fee, with no end in sight to the rollovers unless the consumer makes a balloon payment.

Lenders can use open-end credit to avoid underwriting requirements. Open-end credit plans, by definition, contemplate repeat lending and are harder to mesh with either state or federal rollover limits. Unlike a series of single payment payday loans, a payday line of credit needs only a single authorization from the consumer. This poses particular risk in light of the potentially indefinite length of a line of credit, coupled with high income and expense volatility over time. While the CFPB has proposed some rules to address this problem, they must be strengthened.

Open-end credit can exploit the proposed exemption for "credit cards" in this rule and gaps in the proposed rules addressing hybrid prepaid-credit cards. Many payday lenders sell prepaid cards and are eager to link their loans to the cards.[531] Indeed, the overdraft fees triggered by payday loans often cause consumers to lose their bank accounts and prevent them from getting new ones, driving the consumers to prepaid cards.

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[528] Https://www.elastic.com/.
[529] See Arizona General Assembly HB2611 "Consumer Flex Loans," http://www.azleg.gov/legtext/52leg/1r/bills/HB2611P.pdf.
[530] Details on file with CRL.
[531] See NCLC Payday Lender Prepaid Cards.

The CFPB has issued rules to protect consumers who have prepaid cards linked to lines of credit. The Credit CARD Act rules and some additional new protections will apply to hybrid prepaid-credit cards that can overdraft while making purchases, obtaining cash, or doing person-to-person transfers. While those new protections are welcome, that may also mean that the credit line is also exempt from the payday loan rule through the credit card exemption. The CARD Act ability-to-repay requirements are far weaker than the proposed protections and are not adequate for high-cost credit lines.

On the other hand, the new hybrid prepaid-credit rules and the CARD Act will not apply if a credit line is linked to a prepaid card but is not accessed through overdraft. For example, a deposit advance product linked to a prepaid card that allows consumers to transfer funds from the credit line to the prepaid card, with the credit repaid automatically from the prepaid card, will not be covered by the CARD Act or other proposed protections for hybrid cards (such as a 30-day waiting period before a credit line is added, fee limits in the first year, or payments no more frequently than monthly).[532] That is, payday lenders will apparently be able to sell prepaid cards simultaneously with the credit lines that undermine the safety of the cards, pushing predatory, high-cost credit on the most vulnerable consumers.

10.6.2. Lenders are shifting to high-cost open-end loans, which pose substantial risk of significant harm for consumers.

In light of the advantages that open-end credit poses to predatory lenders, it is no surprise to see them moving in that direction. Prior to its shift to pawn loans, from 2011 to 2014, Cash America's open-end credit line balances grew from $21.6 million to $66.2 million, amounting to 22% of the company's loan balances.[533] Enova and Elevate are also growing their open-end offerings.

In addition, as discussed at section 2.5.4, lenders are pushing legislative proposals to permit high-cost open-end lending in additional states.

Unaffordable high-cost open-end loans cause substantial harm. Several examples of borrower experiences with these loans are identified as such in Appendix A.

10.6.3. The ability-to-repay determination requirements for open-end credit must be stronger.

Like the requirements for short-term open-end loans, proposed § 1041.9(b)(1) requires a reasonable determination of ability-to-repay for longer-term open-end loans (i) before making a new loan or increasing the credit line or (ii) before advancing more credit if more than 180 days have passed since the last determination. In addition, the proposal for longer-term lines requires that, if the terms do not provide for termination of access to the line by a certain date and for repayment of all amounts due by

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[532] However, If there are recurring payments, the credit lines would still be covered by the ban on mandatory repayment by electronic fund transfer, 12 C.F.R. § 1005.10(e)(1), including transfers accomplished through offset, 12 C.F.R. § 1005.3(c)(5); NCLC, Consumer Banking and Payments Law § 5.1.3.7 (5th ed. 2013), updated at nclc.org/library.

[533] Hecht, John. "Alternative Financial Services: Innovating to Meet Customer Needs in an Evolving Regulatory Framework" at 31 (presented at the CFSA Solutions, Little Rock, AR, Feb. 27, 2014), http://cfsaa.com/Portals/0/cfsa2014_conference/Presentations/CFSA2014_THURSDAY_GeneralSession_JohnHecht_Stephens.pdf.

a subsequent certain date, then the determination must assume that any remaining balance be repaid 180 days following the consummation date.[534]

We support requiring a new determination both before opening the credit line and before increasing it. The original underwriting for a smaller credit line is inadequate to support the larger amount of debt, possibly larger minimum payments, and longer time to repay for a larger credit line. We also support requiring a new determination if the prior determination was more than 180 days ago.

In addition to these requirements, we urge more explicit requirements related to determining a volatility cushion and reviewing verification evidence for longer-term open-end loans, as discussed at section 10.4.5 above. And as discussed further at 11 below, we urge that an increase in the credit line also trigger a presumption of inability to repay if there are any indicia that the borrower is struggling to repay the existing credit line, such as a single bounced payment or sustained high credit utilization.

We support the proposal to require lenders to assume, when considering ability to repay, that an indefinite line of credit will be repaid in full within 180 days. This requirement is necessary to prevent high-cost credit lines that create a perpetual debt trap with little progress in repaying the credit. The provision will encourage lenders to have appropriate minimum payments so that an initial advance on the loan can be repaid in six months.

This rule also prevents evasions of the short-term rollover rules. For example, as discussed above, one lender in Virginia has a credit line that requires payment of only the monthly participation fee. That fee is effectively a rollover payment. The consumer is stuck in the same cycle of paying and facing a large balloon to get out of debt. A lender making this type of loan would effectively have to meet the same ability-to-pay standard that a longer-term balloon payment lender must meet, because the lender would have to assume that the entire loan is due at a fixed point in time.

11. PROTECTIONS AGAINST REFINANCES OF LONGER-TERM LOANS MUST BE STRENGTHENED: § 1041.10.

11.1. Overview.

Proposed section 1041.10 sets out a presumption that the consumer does not have the ability to repay a covered longer-term loan made under section 1041.9 if it either is made during or shortly after a loan with a balloon payment or if another loan is outstanding under circumstances that indicate the consumer is having trouble repaying the loan. The section also sets out the standards for rebutting that presumption (except that the presumption may not be rebutted for loans made during or closely following a short-term exemption loan, *i.e.* one made under section 1041.7).

The standards in this section are critical to the success of the rule and to compliance with a meaningful ability-to-repay standard. Even if a loan is required to be underwritten based on the highest payment, weaknesses and uncertainties in the ability-to-repay standard may result in unaffordable balloon payments that would trigger reborrowing. Similarly, even if the loan lacks a balloon payment, the underwriting requirements of section 1041.9, on their own, may not dependably produce loans that consumers can afford to repay while meeting other expenses *without reborrowing*. Refinancing of longer-term loans can mask inability to repay and cause consumer harm just as it can for short-term

[534] Proposed § 1041.9(a)(5)(iii).

loans. Consequently, we support the additional protections set forth in this section but have the following recommendations, which we address in detail in the subsequent subsections.

In general, the presumptions of inability to repay for new loans made following an underwritten balloon-payment loan are appropriate. However:

- A 60-day presumption period, rather than 30, is especially critical when a lender is moving a consumer from a balloon-payment loan to a longer-term loan, where there are fewer limits on bait-and-switch to long-term debt.
- We strongly oppose the proposed exemption for a new loan with substantially smaller payments, unless it also has a lower total dollar amount of new payments. That will encourage weak underwriting of balloon loans and bait-and-switch tactics to move consumers from shorter balloon loans to longer high-cost installment loans.

The presumptions proposed for refinancing loans without balloon-payments need more substantial strengthening. Our key recommendations are:

Lenders should be prohibited from refinancing their own defaulted loans (those 120 or more days delinquent).

Lenders may try to evade the refinancing rules by having borrowers repay their loans early—which then are no longer "outstanding"—and then immediately reborrow (i.e., the next day). To prevent this evasion, a loan should be deemed to be "outstanding," triggering the § 1041.10(c) rules, for 30 days after the consumer makes a lump sum payment to repay a loan early.

A broader range of circumstances should trigger the presumption of inability to repay:

- Loans with indicia of unaffordability in the previous 90 days, not 30.
- A loan that is even one day late in the past 30 days, or more than seven days late in the past 90 days.
- A failed payment transfer (including failed payroll deductions).
- Payments not initiated due to nonsufficient funds.
- Revocation of payment authorizations unless the consumer has since made an on-time payment.
- New delinquencies on a credit report since the prior loan.
- An expression of inability to meet major financial obligations or basic living expenses, not just the loan payment.
- Reborrowing before making substantial progress in repaying the loan (i.e., repaying 75% of principal), not merely receiving a small amount of cash-out.

When indicia of unaffordability are present, there should be no exception to the presumption for:

- Loans with smaller payments.
- Loans with a lower APR, unless the total dollar amount of new payments is lower than those remaining.

The term "improvement in financial capacity" should be defined to mean only an improvement in net income or major financial obligations as defined in the ability-to-repay rules.

Lenders should not be permitted to use *any* type of non-covered loan as a bridge loan. Bridge loans should also completely restart, not just toll, the 30-day period.

Only one refinancing should be permitted.

Open-end credit needs more protection:

- Increases in credit lines should be viewed as a refinancing.
- New advances on an existing credit line should also be viewed as refinancings and be subject to the presumption (and a potential freeze on the credit line), if indicia are present showing that the credit line is proving unaffordable.

The CFPB should review portfolio-wide refinancing rates and track data on the number of loans that meet the indicia of unaffordability but gain an exemption from it or overcome the presumption.

11.2. General standard and review of borrowing history: § 1041.10(a).

Proposed § 1041.10 sets out additional requirements that apply if a consumer seeks a new covered longer-term loan before repaying a previous one. Proposed § 1041.10(a)(1) describes the basic standard that, if a borrower is presumed to be unable to repay a loan pursuant to § 1041.10(b) or (c), then any determination that the consumer can repay the loan is unreasonable unless the presumption has been rebutted as set forth in § 1041.10(d). The section also repeats the rule of proposed § 1041.10(e) that the presumption cannot be rebutted if the new loan closely follows a short-term exemption loan that was not underwritten. We will comment on each of these sections below.

The CFPB has asked whether it would be appropriate to impose similar limits (i.e., a presumption of inability to repay) if there is an increase in the credit available under an existing loan. It is essential to cover increases in credit lines as well; if the consumer shows indications of struggling to repay the first loan without reborrowing, then a presumption of inability to repay is certainly warranted before giving the consumer additional credit. It does not matter whether that additional credit takes the form of a payoff/new loan refinancing with cash out or an increase in credit under a line of credit.[535] Indeed, it is all the more important to ensure ability to repay when the consumer is taking on higher amounts of debt (which, as discussed below, we fear proposed § 1041.10(c)(iv) will encourage).

The CFPB has also asked whether limitations should apply to new advances on existing lines of credit. In general, we believe that the same indicia of inability to pay should require the lender to freeze a credit line. At a minimum, a presumption of unaffordability should apply if there are indicia of unaffordability at the intervals when lenders are required to periodically reevaluate ability-to-repay open-end credit or before a credit line increase. In addition, we discuss below the circumstances under which the indicia of unaffordability should lead to a freezing of new advances under the existing credit line in between reassessments of ability-to-repay.

Proposed § 1041.10(a)(2) requires the lender to review information about the consumer's borrowing history from the records of the lender and its affiliates and from a registered information system, if available. Proposed Comment 10(a)(2)-2 explains that checking the records of the lender and its affiliates alone is sufficient if no information systems have been registered.

[535] "Increasing" the credit available on a closed-end loan would seem to simply be a payoff/new loan transaction already covered under this section.

We recommend that, if no information system has yet been registered, the lender should be required to check any available state databases in the borrower's state. As notes in section 14.4.5 below, many states have databases that will contain some information on borrowing history, at least as far as previous short-term loans. There is no reason not to require the lender to check those databases if applicable until the registered information systems are up and running.

11.3. Presumption of inability to repay following balloon loans: § 1041.10(b)(1).

11.3.1. Extend the presumption period to 60 days; apply to lines of credit.

Proposed § 1041.10(b)(1) sets forth the presumption that a consumer does not have the ability to repay a loan if it is made during or within 30 days of repaying a short-term underwritten loan (made under proposed § 1041.5) or a longer-term loan that has a balloon payment. (Short-term exemption loans are dealt with separately in proposed § 1041.10(e).) Comment 10(b)(1)-1 simply explains the rule.

We support the rule of proposed § 1041.10(b)(1), while urging that the 30 day period be 60 days. As discussed earlier in these comments, the proposed underwriting requirements give lenders significant discretion and potentially permit lenders to ignore substantial evidence that a consumer is struggling with existing expenses. We are not confident that the underwriting requirements will dependably produce loans with affordable payments. For all of the reasons short-term loans lead to a cycle of reborrowing, balloon payment loans are highly likely to strain consumers' budgets and make it difficult for them to meet other expenses. It does not matter whether the balloon payment is from a single payment loan or from a longer-term loan with a balloon at the end. If the underwriting was successful, the consumer should not have to reborrow shortly after the balloon payment. If the consumer does return to reborrow, then it is appropriate to impose a presumption that the reborrowing was triggered by the balloon payment.

A 60-day gap is especially important when a longer-term loan follows a balloon loan because longer-term loans lack even the weak rollover and debt trap limits that the proposed rule requires for short-term loans. For short-term loans under § 1041.5, the rules impose a presumption of unaffordability after every loan and a prohibition after the third in a row. While that is not sufficient, and we urge a stronger 90-day limit on indebtedness each year, there is nothing comparable for longer-term loans. Lenders can move borrowers directly from balloon-payment loans into a long-term debt trap.

Indeed, the new debt-trap longer-term loan can even be an interest-only loan or extremely slow amortization loan that is the equivalent of an extended sequence of short-term payday loan rollovers without any limit. For example, on a $300 loan, Big Picture Loans collects five $105 interest-only payments due every 14 days before adding any principal to the next 11 payments.[536] That is the equivalent of five rollover fees on a 14-day loan. Similarly, the Speedy Cash loan discussed in section 10.3 above, while fully amortizing, has effectively interest-only payments for a year due to the extremely high rate and long term.

As discussed more fully in section 11.8 below, there is too little that protects borrowers if lenders use an unaffordable balloon-payment loan as a gateway loan, and 30 days is not long enough to recover.

[536] *See* https://www.bigpictureloans.com/loan-rates.

Thus, we urge the Bureau to impose a 60-day presumption period between a balloon-payment loan and a longer-term loan.

We also urge that, if the covered longer-term balloon payment loan is a line of credit, then the credit line should be frozen with no new advances during the 60-day period unless the lender can overcome a presumption of inability to repay. A new advance is a new loan, and balloon payments on lines of credit should not be permitted to drive reborrowing.

The CFPB has asked whether there are other circumstances that would also warrant a presumption of unaffordability when a borrower seeks a covered longer-term loan in close proximity to a covered short-term or longer-term loan.

As discussed in section 3.6 above, "non-covered bridge loans," which appropriately toll or restart the waiting period, should be more broadly defined to include any non-covered longer-term loans from the same lender—not just pawn loans. A presumption of inability to repay is especially important if the non-covered loan is a balloon payment loan.

In addition, as discussed in section 8.2 above, after a consumer has been in debt on short-term covered loans (underwritten or exemption loans) for 90 days in the previous year, no additional covered loans should be made that year by the same lender. A hard prohibition on additional loans after 90 days of short-term indebtedness should apply if the same lender attempts to switch the borrower to a longer-term loan. Otherwise, lenders will simply use bait and switch between loan types to keep the consumer in perpetual debt.

11.3.2. Exception to presumption of inability to repay following balloon loan: § 1041.10(b)(2).

Proposed § 1041.10(b)(2) creates an exception to the presumption of inability to repay when a loan is made in close proximity to a loan with a balloon payment. The proposed exception is for loans that have payments that are "substantially smaller" than the largest payment on the prior loan.

We oppose this exception, unless it is revised to require the new loan also to have lower total payments measured in dollars. The fact that a new loan has smaller payments does not change the fact that the first loan was unaffordable or that the unaffordable balloon payment caused the reborrowing. A high-cost lender that is making balloon payment loans and that has made a deficient ability-to-repay analysis should not be permitted to make a new loan without overcoming a presumption of inability to repay.[537] Nor should a new high-cost lender be permitted to exploit a consumer stuck in an unaffordable loan.

The only exception should be a new loan that has lower total dollar costs than the remaining payments on the old loan. We describe the importance of total dollar cost in section 11.5.2 below.

Without a cost limitation, this exception will encourage bait-and-switch tactics and will undermine compliance with and enforcement of the ability-to-repay requirements. Lenders will be encouraged to

[537] As discussed below, we agree with the criteria that the CFPB has proposed for overcoming the presumption, criteria that focus on improved financial capacity. The mere fact that payments on the second loan are smaller would not permit the lender to overcome the presumption.

start borrowers off with shorter loans with balloon payments and then will be able to use the unaffordability of those loans to push the borrower into a longer-term debt trap. Consumers may be more willing to take out an initial loan if the length of the debt trap is not apparent. Indeed, some consumers have said that they take out payday loans because it does not add a "debt."

We appreciate that this exception does not apply following short-term exemption loans without an ability-to-repay determination. Nonetheless, weaknesses in the underwriting requirements could still lead to unaffordable balloon payment loans that can be used for a bait-and-switch or cloud unaffordability. Indeed, there would be no need for proposed § 1041.10(b) at all if unaffordable balloon payments were not a distinct possibility under the rule despite the fact that they carry ability-to-repay requirements.

Permitting a bait-and-switch between large balloon payments and longer-term loans with smaller payments will also cloud default rates on the balloon payment loans. This will make it more difficult to detect and enforce against unreasonable ability-to-repay determinations on the balloon payment loans.

This exception could also further undermine the non-payday states by giving payday lenders an incentive to continue lobbying those states to permit short-term payday loans. Even if the short-term rules succeed in preventing extended rollovers of short-term loans, it will still be worth it for lenders to start consumers off with those loans, setting them up for the long-term debt trap. Lenders may be able to argue to legislators that the limits on short-term loans will protect consumers from the dangers of those loans, while, in reality, the lenders plan to flout those protections if the rule permits this easy shift to longer-term loans.

Even if the second loan has payments that are so much smaller that they plausibly meet the ability-to-repay analysis, it is still appropriate to prohibit the lender that made the first loan from making a second loan. Prohibiting the second loan helps to prevent unfair, deceptive and abusive practices by eliminating an incentive to make unaffordable loans.

Better options than a second high-cost loan are available to help a consumer get out of a loan with an unaffordable balloon payment. The lender could work out a repayment plan for the balloon payment. The lender or another lender could make a lower cost non-covered loan. (As discussed in section 11.10 below, though longer-term exemption loans could also be used here, covered lenders should not be allowed to use exemption or non-covered loans as bridge loans *between* covered loans.) Or consumers could use the range of options that they use in states without payday loans.[538] A second high-cost loan, most likely from the same lender that trapped them with an unaffordable balloon payment, is not an option the CFPB should promote.

To the extent that the CFPB retains this exception as proposed, the "substantially smaller" standard should be stronger and more specific. Proposed Comment 10(b)(2)-2 explains that a $250 payment is not substantially smaller than a $300 balloon payment, but a $75 payment is substantially smaller than a $167 payment.

If the CFPB must retain this exception, the new payment should be no larger than the greater of (1) one-third the size of the balloon payment or (2) for loans with at least three payments, the smallest

[538] See section 19.2.3 below.

payment on the prior loan. The CFPB has proposed to define a balloon payment as one that is at least twice as large as another payment.[539] For example, if a loan had five payments of $50 and one of $100, the new loan could have payments no larger than $50. If a loan requires five payments of $50 and then a $300 balloon payment, the new loan could not have payments larger than $100.

The Bureau solicits comments on whether it should carry over the step-down rule for short-term exemption loans. (The step-down rule creates an exception to the ability-to-repay rules for three loans that step down in amounts.) We oppose using the standard in that provision as a metric for determining whether a payment is "substantially smaller." As discussed in section 8.4 above, we object to that standard in proposed § 1041.6(b)(2)(i) for back-to-back short-term loans as well. The step-down rule focuses on principal size, not payment size, and it also does not prevent another unaffordable balloon payment. Using the step-down approach, a $500 loan with five $50 payments and then it seems a $350 balloon could be followed by another similar loan as long as the balloon is only $250, followed by a third loan with a $150 balloon.

If the CFPB retains the smaller payment exemption, the lender should be required to consider the original loan an unaffordable loan, to adjust underwriting standards to prevent such unaffordable loans, to keep data on these unaffordable loans, and to report them to the CFPB. In evaluating the lender's compliance with the ability-to-repay rule, the CFPB should treat unaffordable balloon payment loans just like defaulted loans, even if the lender is able to avoid a default by making a new loan with a smaller payment.

We also urge the CFPB to prohibit back-to-back balloon payment loans regardless of the size of the balloon on the second loan. Balloon payments invariably push consumers into reborrowing. The lender's interest is in making that balloon so unaffordable that it forces immediate reborrowing. Any balloon that springs on a financially distressed consumer after a series of smaller payments is likely to push the consumer to reborrow. Once a lender has made one balloon payment loan and succeeded in triggering reborrowing, it should not be permitted to do so a second time. Thus, if the CFPB retains the "substantially smaller" exception, it should require the second loan to have equal payments.

11.4. Presumption of inability to repay for certain refinancings: § 1041.10(c)(1).

11.4.1. Limiting refinancing is essential.

11.4.1.1. Overview.

Proposed § 1041.10(c)(1) sets forth four situations in which making a new covered longer-term loan when another loan (covered or non-covered) is outstanding, or refinancing that loan, would trigger a presumption of inability to repay. In sections 11.4.2-11.4.9, we will comment on those four situations as well as others that should trigger the presumption because they evidence a consumer in distress.

But before commenting on the details, we discuss why the CFPB should take a broader view of the types of refinancings that indicate that the borrower is unable to repay the loan while meeting other

[539] As discussed in section 3.2 above, we urge the CFPB to define a balloon payment as any payment that is at least 10% larger than the smallest payment.

expenses without reborrowing. Tighter rules on refinancing longer-term loans are essential to the viability of the ability-to-repay requirements and the protection of consumers.

The CFPB has set limits (albeit insufficient) on refinancing of short-term loans because of the documented harm of reborrowing. High refinancing rates for longer-term loans can indicate inability to repay and cause serious consumer harm for the same reasons that high refinancing rates are problematic for short-term loans. Refinancing of either short- or longer-term high-cost loans can:

- Be triggered by the unaffordability of the prior loan;
- Show that the consumer was unable to repay the prior loan without reborrowing;
- Disguise default rates;
- Inhibit enforcement of the requirement to make a reasonable ability-to-repay determination;
- Change the way loans function from the way they are marketed;
- Encourage longer and more dangerous loans;
- Increase misaligned lender incentives to make unaffordable loans and the likelihood that a lender can make a profit on a borrower who ultimately defaults;
- Lead to a long debt trap;
- Increase costs for consumers;
- Increase the chance that the consumer will incur penalty fees, late fees, or overdraft fees over the course of the loan;
- Cause the greatest injury to those who have especially long loan sequences.

In sections 11.4.2-11.4.7 below, we describe some of the many ways that permitting high rates of refinancing undermines the ability-to-repay rule and results in consumer harm. In subsequent sections, we discuss specific proposals to limit refinancings that reflect unaffordability and encourage evasions.

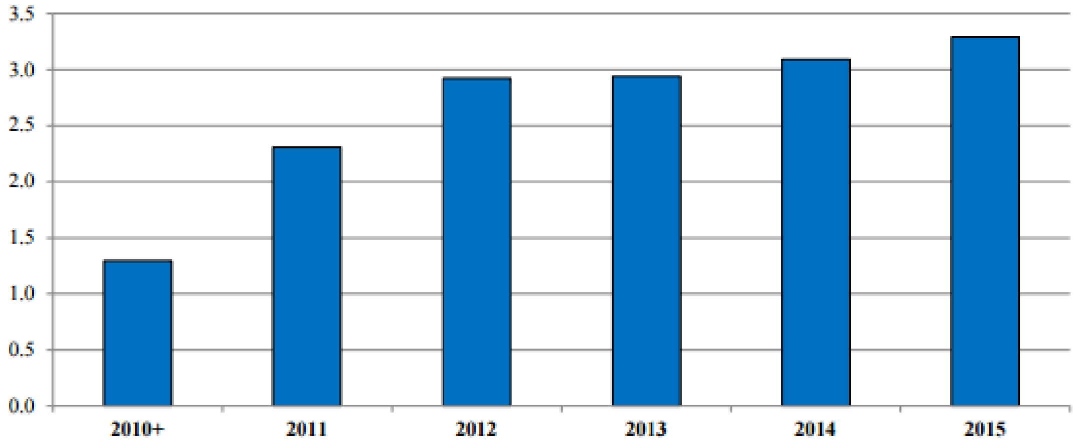
11.4.1.2. Lenders have strong incentives to use unaffordable refinancings of installment loans to ensnare borrowers in a cycle of debt.

Reborrowing is central to the debt trap of short-term payday loans and is one of the central practices the CFPB is attempting to address. As lenders transition to longer-term loans, it is increasingly clear that refinancing creates a debt trap with longer-term high-cost loans as well. Indeed, without careful rules on refinancing, a rule that encourages payday lenders to offer longer-term loans may end up simply driving consumers into a deeper and longer debt trap than the one already posed by short-term loans. In either the short-term and longer-term situation, refinancing provides the consumer a temporary reprieve from the burden of the first loan but prolongs the time in debt and increases the costs to the consumer.

The experience in Colorado is instructive here. Refinancing rates, and total days in debt, have consistently increased each year since reforms pushed lenders into installment loans. In 2010, consumers took out an average of 1.3 loans per year compared to 3.29 loans per year in 2015.[540] This is especially notable since the minimum loan term is six months and the vast majority of the loans are between 181 and 186 days. Yet the average customer is in debt 299 days a year.

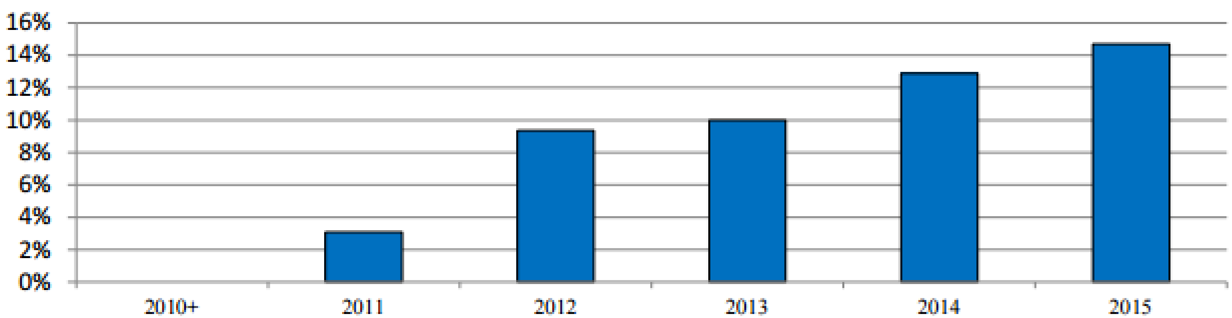
[540] Colorado 2015 Demographic and Statistical Information at 18. The chart is taken directly from the report. The unaudited self-reported data in the summary of annual reports compiled by the State of Colorado reveal fewer loans per consumer. Regardless of which number is more accurate, the trend of increasing number of loans and increasing number of days in debt appears clear.

In 2015, consumers transacted, on average, 3.29 loans from the same lender during the previous 12 months.



Due to Colorado's very unusual rebate structure, lenders do not have a pricing incentive to encourage refinancing.[541] But lenders still have a powerful motivation to push refinancing in order to keep consumers in perpetual debt. The percentage of consumers who are in debt continually for all 365 days per year has risen from about 3% in 2011 to 14.69% in 2015.[542] The consumers in that group had an average of 6.54 loans in 2015. Notably, as discussed in section 7.3 above, default rates are also high and likely increasing in Colorado, showing the unaffordability of these loans. Somewhere between a third and a half of Colorado borrowers are struggling with their loans.

Percentage of Post-HB 10-1351 Loans Written to Consumers Indebted (to the Lender Being Examined) Every Day for the Prior 12 Months or More



In other states, unlike in Colorado, refinancing can increase the loan cost, as shown in the following example from a $500 six-month loan in Louisiana. [543] Even without up-front fees or add-ons, refinancing also extends the time in debt.

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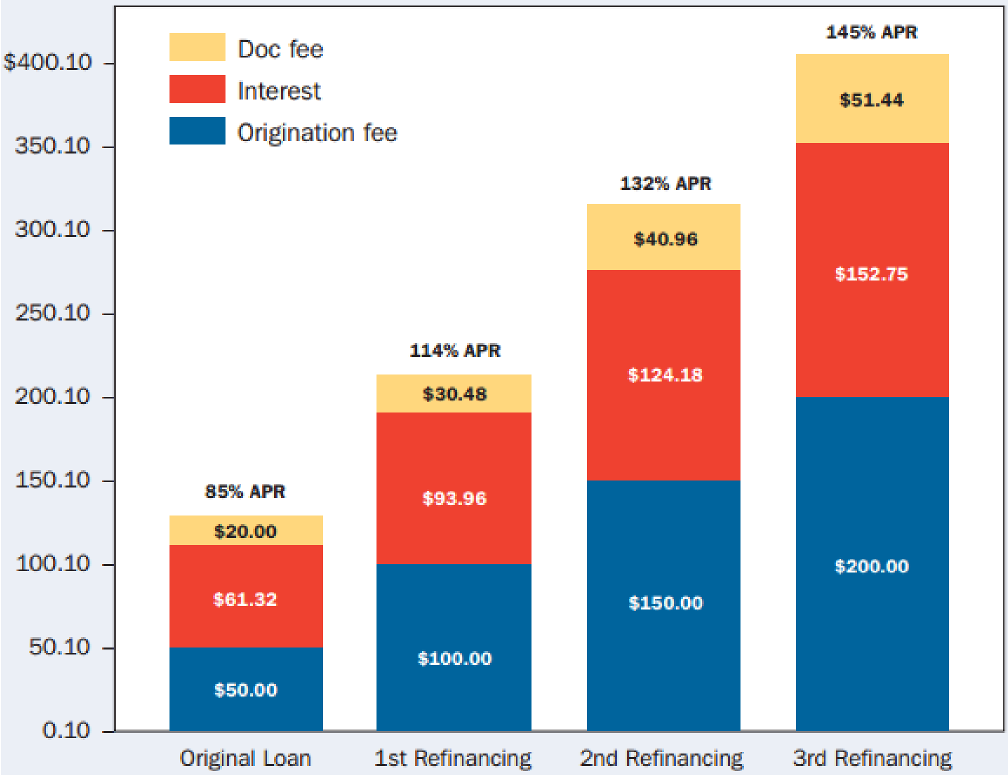
[541] The effective APR paid actually decreases with refinancing. It is harder to say if total costs go down because it depends on whether the consumer repays the last loan early, on the regular schedule, or through perpetual refinancing.

[542] Colorado 2015 Demographic and Statistical Information at 25. The chart is taken directly from the report.

[543] NCLC, Installment Loans at 22.

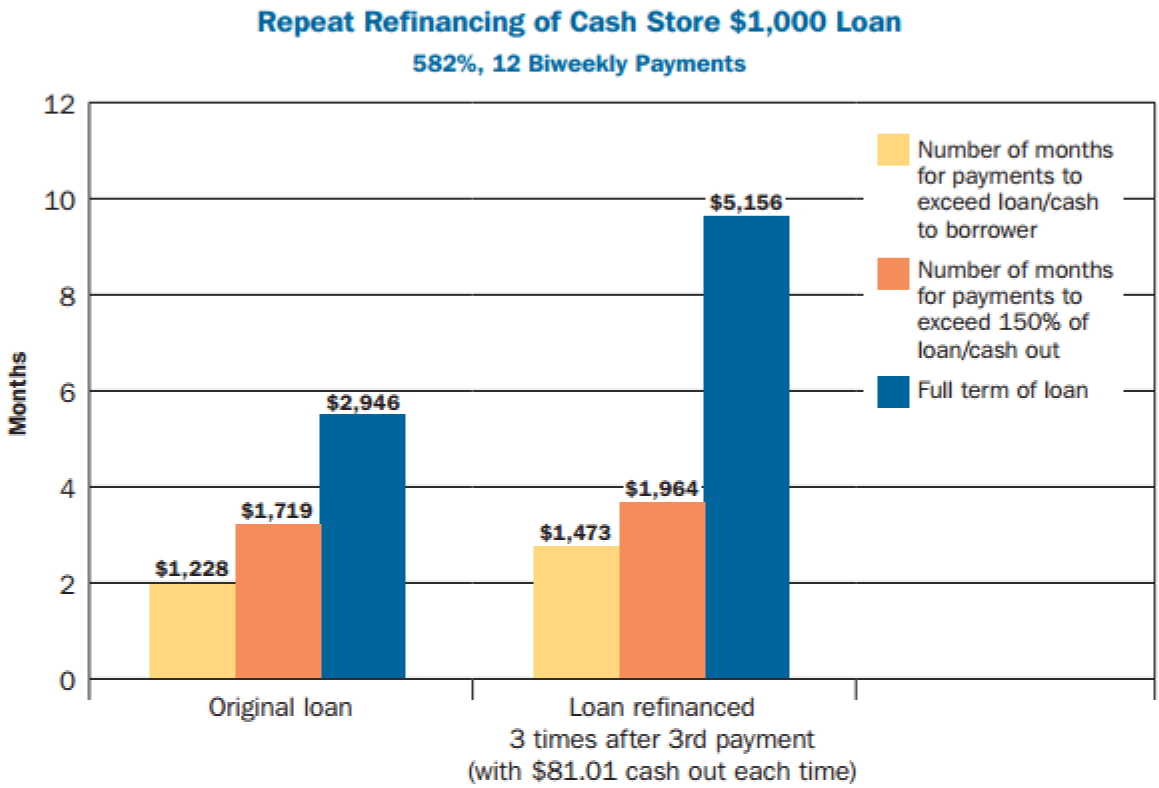
Effect of Refinancing a $500 Six-Month Louisiana Loan Three Times



The example assumes that 1) the borrower refinanced the loan three times, each time after making the second payment; and 2) the borrower did not obtain any new money upon refinancing, but simply refinanced the remaining balance each time so that it would be repayable over six months. The result of the three refinancings is an increase in the repayment period from 6 months to 12 months.

The enhanced profits from refinancing can weaken lenders' motivation to make sure that refinanced loans are affordable. As time in debt and loan costs increase, the gap between lender success (a profitable loan, even if the borrower defaults) and borrower success (a fully repaid loan) increasingly diverge. For example, the following chart shows the potential impact of refinancing a Cash Store loan. Generously assuming that the lender needs to recover 150% of the loan to make a profit, the gap between lender profits and borrower success widens from about two months of payments to about six months after three refinancings.[544]

[544] NCLC, Misaligned Incentives at 26.



11.4.1.3. Refinancing, particularly before the borrower has made substantial progress in repaying the loan, often shows inability to repay <u>without reborrowing</u>.

Proposed §§ 1041.4 and 1041.8 both state that it is an abusive and unfair practice to make a covered loan without reasonably determining that the consumer will have "the ability to repay the loan." In discussing both standards, the CFPB has explained:

> "Ability to repay" in this context means that the consumer has the ability to repay the loan *without reborrowing* and while meeting the consumer's major financial obligations and basic living expenses.[545]

Similarly, the CFPB has stated that consumers must have the ability to repay a loan "according to its terms"[546]—that is, to "make *all payments* under the loan and to meet basic living expenses during the term of the loan."[547] This standard must be met without any "implicit assumption that the consumer will obtain additional consumer credit . . . ."[548]

The "without reborrowing" element of the ability-to-repay rule is critical to its integrity. (Indeed, as discussed in section 5.3 above, we urge the CFPB to make that element explicit in the rule itself.) The

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545 81 Fed. Reg. at 47933 (emphasis added); *id.*at 47993 (same).
546 Proposed § 1041.5(b); proposed § 1041.9(b).
547 Proposed Comment 5(b)-1 (emphasis added); proposed comment 9(b)-1.
548 Proposed Comment 5(b)-2.ii.A; proposed comment 9(b)-2.ii.A.

question is not simply whether a consumer can survive an individual loan, or even a string of loans, without defaulting. The ability-to-repay standard requires lenders to reasonably determine that the borrower will be able to make it *to the end of the loan* without needing to reborrow.

Not every refinancing is a sign of unaffordability. Some consumers may choose to take out additional cash even if they are able to make their payments and cover their debt obligations and basic living expenses without doing so.

But ensuring that reborrowing is not triggered by unaffordability of the loan is critical. Several elements of the rule's underwriting obligations are aimed at supporting a "without reborrowing" standard. The lender must reasonably determine that the consumer has sufficient residual income to cover (1) existing debt obligations, (2) basic living expenses, and (3) a cushion that is sufficient to cover the spikes in expenses (such as utility bills or medical bills) or dips in income (such as uneven hours) that are experienced by similarly situated consumers over the course of the loan's term. As discussed in section 10.4.510.4, a reasonable cushion should also account for the historic volatility in the particular borrower's life. That is, the lender should look for indications in the consumer's credit report or deposit account that the borrower has experienced spikes or dips over a similar time period as the loan that have led to inability to pay expenses.

While the overarching principles here are strong, we are very concerned that these underwriting requirements give high-cost lenders too much latitude to design loans with payments that theoretically fit into a consumer's budget but in reality are unaffordable. The danger is especially great for loans that have smaller payments that stretch out for a very long time—where the cumulative burden of the payments over time is not apparent from looking at a one-month snapshot of identifiable expenses. We have made suggestions earlier in these comments for ways to strengthen the up-front underwriting requirements. But looking at reborrowing patterns and holding lenders to a standard of ability to repay *without reborrowing* is critical. When financially distressed consumers reborrow before making substantial progress toward principal, there is a strong chance that there has been a failure in the underwriting to successfully predict the consumer's income and expenses as required.

Most refinancings (94.3% to 99.9% in the CFPB's study) involve some cash out to the consumer.[549] The consumer's need for additional credit is triggered by some expense, or combination of expenses, that the consumer cannot cover without reborrowing. While, in some cases, consumers are reborrowing in order to cover a discretionary expense, in many cases consumers are reborrowing to cover basic living expenses or debt obligations.[550]

While the lender is not expected to predict extraordinary shocks, it must build in a cushion that is sufficient to cover the reasons that similar consumers—most likely financially distressed consumers—could need additional cash. The CFPB has explained:

> [R]equiring a lender to account for volatility does not mean that a lender must provide a cushion that is so large that it could shield a consumer from *extraordinary shocks* in income or basic living expenses, such as those resulting from job loss or medical bills from catastrophic

[549] Supplemental Findings at 20.

[550] Payday lenders have long used the example of the need to make a car repair as justification for their loans, despite repeat studies showing that most borrowers are covering routine budget shortfalls. We expect that study of the reasons that consumers refinance installment loans would come to the same conclusion.

> illness. But *occasional reductions* in hours (and resulting earnings) or *occasional spikes in expenses* (such as an occasional spike in a utility bill) are *very much to be expected* over the course of a longer-term loan.[551]

In order to preserve and enforce the integrity of the underwriting requirements, including reasonable predictions of income and expense volatility, the rule must do more to prevent reborrowings that are triggered by a failure of underwriting to preserve a sufficient cushion to enable borrowers to make it to the end of the loan term. Allowing lenders to have a business model that leads large numbers of consumers to regularly reborrow in order to cover basic expenses and debt obligations makes a mockery of the "ability to repay without reborrowing" principle. Theoretically, some consumers' reborrowing could be triggered by a desire to make a discretionary or truly unusual purchase that the lender was not required to originally account for. But allowing this type of exception would let an exception swallow the rule.

The CFPB acknowledges the problems of reborrowing when it asks "whether refinancing early in the repayment schedule of the loan would evidence unaffordability of the outstanding loan and, if so, up until what point in the life of the loan."[552] As discussed in section 11.4.8.2 below, refinancing before the consumer has made significant progress in repaying the loan is strong evidence of unaffordability. We recommend that substantial progress be measured by repayment of 75% of the loan principal.

11.4.1.4. The CFPB's data on payments before default does not show that refinancing is unrelated to unaffordability.

The CFPB has declined to take a firmer position on reborrowing because it believes that the data it analyzed is "ambiguous":[553]

> The Bureau believes that this evidence [of high refinancing rates] can be viewed in one of two ways. On the one hand, the fact that in most situations consumers who are refinancing these loans have been able to make the required payments when due could be understood to suggest that they are not refinancing a loan because of difficulty satisfying obligations on the existing loan. On the other hand, the fact that after making a certain number of such payments consumers need to borrow more money could be seen as evidence that these consumers cannot afford the cumulative effect of the repayments and that the repayments are causing the need to reborrow.[554]

The CFPB analyzed data from a limited set of loans and found that consumers who refinanced were not previously any more behind in their payments than consumers who ultimately repaid in full without defaulting.[555] The CFPB concluded that the fact of these payments shows that the consumers were not struggling. We disagree with this conclusion for several reasons.

First, and critically, the CFPB's conclusion ignores the impact of the leveraged payment mechanism. As the CFPB has explained extensively throughout its proposal, lenders' ability to collect payments from

[551] 81 Fed. Reg. at 48013 (emphasis added).
[552] 81 Fed. Reg. at 48026.
[553] 81 Fed. Reg. at 48025.
[554] 81 Fed. Reg. at 48025.
[555] Supplemental Findings at 15-19.

consumers in no way shows that the consumer can afford those payments. In the short-term payday context, the CFPB views rollovers as evidence of inability to repay without reborrowing whether or not the previous payday payments bounced or were short. Many payday loans are paid in full on the day they are due but then reborrowing happens the same day. A key rationale for the entire proposed rule is precisely that lenders are able to extract payments from consumers who *cannot* afford to repay their loans without reborrowing.

Second, the monthly payment loans that the CFPB analyzed are different from the more typical loan with biweekly or semi-monthly payments.[556] High-rate loans have payments tied to payday. Monthly payments are most often seen with Social Security and disability recipients and other types of public benefits or other income paid monthly.[557] Government payments are highly dependable, so it is not surprising that lenders are able to consistently collect payments on time even if a borrower is struggling financially. Indeed, the Bureau notes elsewhere that monthly borrowers are particularly likely to be stuck in long cycles of reborrowing on short-term loans—suggesting both (1) income that lenders can easily take for repayment, and (2) unaffordability of the loan.[558] Further, one study found lower default rates for loans paid monthly than at other intervals,[559] even though these loans are typically offered to borrowers who have especially low incomes.[560] While it is noteworthy that borrowers who defaulted were in such distress that, on average, they were paying late or only partially from the beginning, this does not prove a lack of distress among the borrowers who refinanced. We note that even if data on loans with bi-weekly payments were to show similar results, they still would not take into account the power of the leveraged payment mechanism to mask distress.

Third, the cash out provided by the refinancing may be the very reason that payments stayed on schedule when the consumer was having difficulties. If an ordinary income drop or expense spike—or even just the cumulative weight of making payments—is what triggered the reborrowing, the consumer's track record of payments before then does not refute the fact that the consumer was unable to get through the full term of the loan without reborrowing. Indeed, we do not know what percentage of the refinancers went on to default. But here again, defaults are not the only measure of consumer harm or unaffordability. The leveraged payment mechanism can result in harm not reflected in defaults—such as overdraft fees, bounced payments before a payment is collected, or difficulty paying other expenses.

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[556] The borrowers on the refinanced loans also made 10 of 12 monthly payments before refinancing. A refinance deep into the loan term is less likely to be due to difficulty repaying than one done earlier. But even then, a pattern of difficulty paying might not be apparent for the reasons discussed above.

[557] In addition, most installment loans on the market appear to be shorter than 12 months. It is not clear what might be different about these 12-month loans and whether differences in loan size or borrow characteristics could impact the payment analysis.

[558] Indeed, the Bureau notes elsewhere that monthly borrowers are particularly likely to be stuck in long cycles of reborrowing on short-term loans—suggesting both (1) income that lenders can easily take for repayment, and (2) unaffordability of the loan. 81 Fed Reg. 47981.

[559] Loans with monthly payments had a 28.73% charge-off rate compared to 33.99% for biweekly, 39.59% for semimonthly, and 97.37% for weekly. Beales & Goel, Small-Dollar Installment Loans: An Empirical Analysis at 25 (Mar. 20, 2015).

[560] The CFPB found that 18% of payday borrowers receive public benefits and that these payments typically occur monthly. CFPB, Payday Loans and Deposit Advance Products at 19. It also found that borrowers that receive public benefits as their income source are highly concentrated towards the lower end of the income range of payday borrowers. *Id*. at 19-20.

Thus, the CFPB's study draws conclusions from the fact of repayment that are inconsistent with its knowledge of the impact of leveraged payment mechanisms, may be skewed by the unusual loan and borrower characteristics studied, and ignores the fact that a spike or dip that should have been covered by a basic expenses cushion may be what triggered a refinance by a borrower who had been making payments. We do not believe that this study in any way disproves that many refinances are triggered by the unaffordability of the first loan.

11.4.1.5. Permitting widespread refinancing will make it more difficult to prevent or enforce against unreasonable ability-to-repay determinations and will disguise default rates.

We support the CFPB's general approach to assessing ability to repay: looking at *both* the lender's up-front procedural underwriting requirements *and* how loans perform in practice on the back end. But refinancing will undermine attempts to assess a lender's practices from either the front or the back end.

The following example illustrates how high reborrowing rates can provide evidence of an unreasonable ability-to-repay determination. Security Finance purported to conduct a residual income evaluation of a consumer's monthly income and expenses to determine affordability of the loan. The company indicated that the loan repayment, plus the borrower's other expenses, could not exceed 90% of monthly income, meaning a borrower purportedly had 10% of income left over after paying the loan and meeting expenses.[561] But the Colorado Attorney General found that the company was injuring consumers by "trapping them in a cycle of debt," continually flipping loans in order to maximize acquisition charges and prevent consumers from paying off their loans as scheduled.[562] The lender accomplished this, Colorado found, by "engaging in underwriting practices that continually place consumers into loans and refinances they have no reasonable probability of repaying."[563] In one examination cited by the Colorado AG, 85 percent of loans examined were refinances.[564]

The CFPB has been clear that a lender's front-end underwriting must consider not only specific expenses that must be documented (such as housing and debt obligations) but also a cushion for basic living expenses. In considering both the consumer's income and basic expenses, lenders are required to account for possible income and expense volatility "over the term of the loan," with a greater cushion for longer-terms "because the longer the term of the loan, the greater the possibility that residual income could decrease or basic living expenses could increase."[565]

Yet refinancing changes the term of the loan. If a lender makes a six-month loan, it must consider potential volatility over that time period. If it refinances the loan after three months with a new six-month loan, it will again consider that six-month horizon. If this pattern of refinancing stretches out for

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[561] Though Security Finance's installment loans generally would not be covered by this rule unless the rule covered unsecured loans (or unless Security Finance moved more to an auto-pay model), this lawsuit nonetheless illustrates the importance of meaningful underwriting for loans under the scope of the rule. (Security Finance does make vehicle title loans that would be covered.) This lawsuit resulted in a settlement whereby the company agreed to refund certain acquisition charges on refinances and decided to leave the state.
[562] *Id.*
[563] *Id.* at 4.
[564] *Id.* at 7.
[565] Proposed Comment 9(b)(2)(i)-2.

two years, the lender will have never considered the volatility that is likely in the life of a financially distressed consumer over a two-year time period.

Similarly, the flexibility that the CFPB is proposing to give lenders to design underwriting criteria requires the CFPB to have a strong commitment to loan performance standards that reveal the reasonableness of the lender's ability-to-repay assessments. The CFPB has indicated that rates of delinquency and default are indicators that the agency will use to assess the lender's underwriting practices.[566]

Yet those back-end measures will also be obscured if a lender has high refinancing rates. If refinancing a loan permits a consumer to avoid delinquency or default, then the first loan will appear as one that was paid in full without defaulting. Refinancing may also give consumers just enough respite from time to time to keep them in the "sweat box"— with the lender collecting payments without showing a troubled loan on its books.

The CFPB is well aware that, when refinancing is common, loan-level statistics need to be adjusted into per-consumer statistics in order to obtain a true picture of how consumers are performing. For example, the CFPB found that, at the sequence level, per-consumer default rates on short-term payday loans are about 20%, while the loan-level default rate is only 3%.[567] Similarly, the CFPB has found that default rates on installment loans are higher when a consumer's sequence of loans is considered a single string of borrowing:[568]

	% defaulted (loan level)	% defaulted (sequence level)
Vehicle title installment loans	22%	31%
Payday installment loans (all)	24%	38%
Storefront payday installment	17%	34%
Online payday installment	41%	55%

But calculating per-consumer delinquency or default rates is not a simple matter. The CFPB has been forced to conduct a complicated analysis of loan sequences in order to obtain a true picture of how loans perform.[569] Determining per-consumer performance data on longer-term loans is even more complicated than it is for short-term loans. A lender may have a variety of loans of different sizes and lengths. Loans or loan sequences may stretch out over several years. How all of these factors fit together to get a picture of what percentage of consumers, not loans, default or have periods of delinquency will not be easy if loans are strung together in strings of refinancing.

The CFPB has also indicated that reborrowing rates may be used to assess the reasonableness of ability-to-repay determinations.[570] It is not clear if that only applies to reborrowing following balloon payment loans and despite a presumption of inability to pay, or if the CFPB intends to scrutinize refinancing of installment loans more broadly. If the CFPB views refinancings of longer-term non-balloon loans as unrelated to unaffordable lending unless the refinancings meet narrow, documented

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[566] *See* Proposed Comment 9(b)-2.iii.
[567] 81 Fed. Reg. at 47930.
[568] See Supplemental Findings at 22.
[569] As the CFPB analyzes refinancing patterns, it should use the same loan sequence definition that it did in its study (i.e., any loan that is repaid before it is due with a new loan taken out within 30 days).
[570] *See* Proposed Comment 9(b)-2.iii.

indicia showing a struggling consumer, then it is hard to see how it would use reborrowing rates. Most refinancings would be condoned (because there are no documented indicia), and likely few would be prohibited (because the presumption of inability to repay was not rebutted). Without the changes we suggest below, it would be difficult for the CFPB to use high portfolio-wide refinancing rates as evidence that the lender's underwriting criteria are unreasonable.

Permitting strings of refinanced loans could also force the CFPB to wait years before being able to determine how a consumer performs in the end. While many payday installment loans are in the six- to 12-month range, assessing a consumer's ultimate performance will take much longer if the consumer refinances several times, pays thousands of dollars, makes little progress in paying down the original loan, and ultimately defaults. Assessing performance of larger and longer loans could be even more difficult.

At the end of the day, the CFPB will have the best chance of enforcing reasonable ability-to-repay determinations if each loan is forced to sink or swim on its own and can be evaluated by how it performs. The use of leveraged payment mechanisms already makes it difficult to access affordability by looking at payment history. Obscuring loan performance by allowing regular refinancing will make it all the more difficult.

Finally, as discussed in section 7 above, all of these problems are compounded if the CFPB merely compares covered lenders to other similar lenders with the same debt-trap business model. If all covered lenders have high rates of reborrowing and the CFPB only targets the outliers, then the standard of ability to repay without reborrowing will be virtually meaningless.

11.4.1.6. Refinancing changes the way loans function from the way they are marketed, leading to a debt trap and high costs for consumers

It is important to remember that unaffordable loans that are refinanced can cause harm even if the loan does not end in default. Short-term payday loan defaults are concentrated among borrowers who only take out a few loans.[571] Yet the CFPB correctly found that refinancing short-term payday loans causes significant consumer harm to "repayers" even if most refinanced loans do not end in default.[572] The same is true for refinancing of unaffordable installment loans.

Among the reasons that the CFPB cites for regulating short-term payday loans are:

- The loans do not function as marketed.[573]
- Consumers experience lengthy loan sequences that they do not expect.[574]
- Lenders encourage long sequences and incentivize employees to push reborrowing.[575]
- Long loan sequences impose high costs on consumers.[576]
- Lenders that repeatedly use leveraged payment mechanisms expose consumers to bank fees and difficulty paying other expenses.[577]

[571] CFPB Data Point at 7-15.
[572] 81 Fed. Reg. at 47940-41.
[573] 81 Fed. Reg. at 47920.
[574] 81 Fed. Reg. at 47920.
[575] 81 Fed. Reg. at 47924.
[576] 81 Fed. Reg. at 47925.
[577] 81 Fed. Reg. at 47939.

All of these reasons apply equally to longer-term loans that are refinanced. Indeed, the CFPB found that the harms that repayers of installment loans suffer from collateral injuries and from having to refinance as a result of unaffordable payments "dwarf" the benefits they receive.[578]

When a loan is refinanced part-way through its term, the time need to repay the loan typically starts over again. The CFPB found that payday and vehicle title installment loans that are refinanced are usually replaced with a second one in the same or somewhat greater amount as the original loan.[579] Assuming that the term of the new loan is the same as well, the new loan will extend the time that the consumer is in debt by a period equivalent to the time between the original loan and the refinancing.

Thus, if a consumer refinances a six-month loan at the three-month mark, even if the loan is refinanced only once, it will take the consumer nine months from the original loan before the credit is paid off unless the consumer pays off the loan early. If the loan is refinanced twice more, the total time in debt could be 15 months. Similarly, if a 12-month loan is refinanced three times at the six-month mark with the last loan repaid on schedule, the total time in debt will be 30 months.

Consumers who enter into installment loans are unlikely to understand that they may be in debt far longer than the term of the loan. A consumer who takes out a six-month loan or even a 12-month loan does not expect to be in debt for years. Even if some consumers understand the impact of refinancing, it is highly likely that—just as the CFPB observed about short-term loans[580]—the consumers that experience the longest loan sequences will suffer the greatest injury and will be the least likely to anticipate the extended debt trap when they first take out a loan.

Installment loans may even have a greater propensity than short-term payday loans to mislead consumers about the extended debt trap they are entering. The refinancing mechanism is more complicated, especially with the cash-out. Consumers may not understand that they are refinancing and extending the time to repay existing debt rather than simply taking out a new loan with new cash. It will be harder for consumers to look back and realize how long they were in debt on the original amount. Even standard loan amortization is far from intuitive, and many borrowers likely will be unaware of how great a portion of their early payments has been applied only toward interest, leaving a counterintuitively large portion of principal. And refinancing strings can go on for years rather than months.

It is also less obvious to consumers how a refinancing of an installment loan increases the cost of that loan. When a payday loan is rolled over, the price of each rollover is relatively clear and is paid up front (although the cumulative price of multiple rollovers is far less clear). When an installment loan is refinanced, the consumer typically gets cash back instead of making a payment, and the incremental price of that cash is not likely understood. This is especially true if there are upfront fees, credit insurance or other add-on products.

Lenders take advantage of borrower's lack of understanding of the disparity between the small amount of cash out that a refinancing may yield and the additional payments and time in debt that will be required. Cash that is the equivalent of skipping one or two payments can require three, four or six times that many additional payments.

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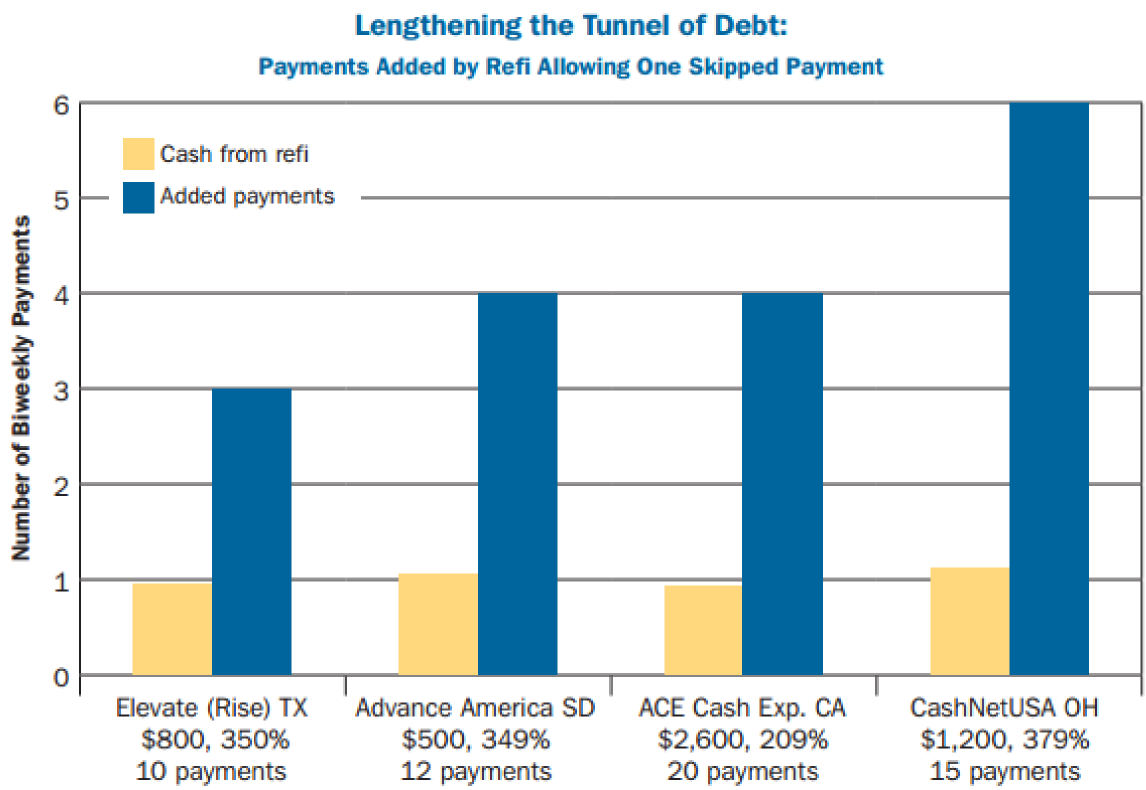
[578] 81 Fed. Reg. at 47939.
[579] Supplemental Findings at 20.
[580] 81 Fed. Reg. at 47936.

The chart below illustrates the additional payments required after a refinancing that yields cash out that is the equivalent of about one payment. With a Rise $800, 350% loan with 10 biweekly payments, a refinance after the third payment yields $145.34 in cash out. That refinance doesn't even quite cover one $150.15 payment, but it adds three additional payments – 6 more weeks in debt and $450.45 in payments.



Note: Each loan is refinanced at the point where the principal reduction (and thus the cash out from a refinance) is about one payment.

The disparity between, on the one hand, cash that covers a single payment, and on the other hand, the added number and cost of payment, is even greater with other loans:

- $92.69 cash-out adds 8 more weeks and $344.44 in additional payments on an Advance America $500, 349%, 12 biweekly payment loan in South Dakota.
- $252.93 cash-out adds 8 more weeks and $1,069.24 on an ACE Cash Express $2,600, 209%, 20 biweekly payment loan in California.
- $226.74 cash-out adds 12 more weeks and $1,203.42 on a CashNetUSA $1,200, 379%, 15 biweekly payment loan in Ohio.

Because the examples above involve cash that only covers one biweekly payment, these scenarios would not be possible under the proposed rule unless a lender can rebut the presumption of inability to repay. But under the proposed rule, the lender can avoid that presumption simply by lowering the size of the payment and stretching out the loan.

Lenders can also increase the cash out and avoid the presumption by increasing the loan or waiting to push refinancing until the consumer can get more cash than a month's worth of payments. Indeed, the bigger the new loan and the greater the amount of cash-out provided, the more payments and cost the refinancing will add.

While consumers will not anticipate the long debt trap of a string of refinanced loans, lenders surely do understand it. They will work to maximize it, taking advantage of consumers' lack of understanding of the disparity between the loan as marketed and the loan in practice. The CFPB has already found very high refinancing rates in the high-cost installment loan market. We have every reason to believe that the same incentives that lead to the first refinancing will lead to successive refinancings. Lenders have an incentive to push refinancing for several reasons, including:

- To mask or cope with a consumer's difficulty repaying, as discussed in section 11.4.1.3 and 11.4.1.5 above;
- To keep the consumer trapped in debt;
- To multiply up-front fees, add-ons, or interest-only periods, serving to increase the cost and often deepen the debt trap.

The CFPB has found that lenders push refinancing of short-term payday loans, even for consumers who are struggling. For example, ACE Cash Express trained and instructed its in-house debt collectors to create a "sense of urgency" and collectors leveraged the sense of urgency to encourage delinquent borrowers with a demonstrated inability to repay their existing loans to take out new loans.[581] The employee manual illustrated the "loan process" with an actual cycle of unaffordable debt.[582]

Undoubtedly, as payday lenders are transitioning to installment loans, they will train their employees to push refinancing of longer-term high-cost loans as well. Indeed, longer-term lenders are already doing this. Consumers who are struggling to manage repayment of their loan, even if their struggles are not documented in the loan file, will be ideal targets for lenders pushing refinancings. Expecting lenders to honestly document the loan file when a consumer has indicated trouble repaying will not work any better than have state laws that require lenders to offer repayment plans (see section 2.6.3 above).

An employee training manual from The Cash Store makes clear how one lender (and likely many others) manipulates consumers who are stuck in high-cost loans to keep them in long term debt. Employees are encouraged to offer to refinance loans in the reminder calls that are made before every payment:

> *"By the way, Tracy, with your scheduled payment, you could qualify for a cash amount of $___[amount]."* [583]

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[581] Consent Order at 7, In the Matter of ACE Cash Express, Inc., CFPB Administrative Proceeding, File No. 2014-CFPB-0008 (filed July 10, 2014), http://files.consumerfinance.gov/f/201407_cfpb_consent-order_ace-cash-express.pdf.
[582] *See* http://files.consumerfinance.gov/f/201407_cfpb_graphic_ace-cash-express-loan-process.pdf.
[583] Cottonwood Financial, LTD, New Hire Instructor Guide-Tex, Handling Customers, Part 1 at 7 (2013) ("Cottonwood New Hire Guide").

Refinance and cash back are the first payment options listed in courtesy calls, ahead of making a payment.[584] Another courtesy script describes "Selling Refinance with Cash Pay Out" for a consumer who responded that he would have trouble paying and had been in the hospital:[585]

> *"I'm sorry to hear you have been ill. I hope you are feeling better. Well, how would you like some extra cash to help you out?"*[586]

Even when a payment is late or has bounced, Cash Store employees must offer refinancing "as the first choice" because it "keeps the customer in an active loan, thus increasing profitability for the store."[587] Sample scripts for dealing with delinquent loans explain "Selling Extension/Refinance." Employees are trained to offer only the choice of refinancing or payment in full and to discourage partial payments: [588]

> "*If the customer wants to pay part of the debt balance, strongly encourage him or her to take advantage of the Refinance option*."[589]

For all of the same reasons that the CFPB gave for addressing the debt trap caused by payday loan rollovers, the rules must also prevent lenders from taking advantage of the unaffordability of their loans to extend the debt trap through regular refinancing of installment loans.

11.4.1.7. Loose refinancing rules will encourage more loans with especially long terms, which pose heightened risk of inability to repay.

There is significant focus in the proposed rule, and appropriately so, on loans with a term that is too short to give the consumer a chance to repay it. But loans can also be too long, as the CFPB has indicated both in its discussion of this rule and in its Request for Information.

As discussed at greater length in section 10.2 and 10.3 above, loans with long terms can be especially dangerous for financially struggling consumers for a number of reasons:

- The longer the term of the loan, *the greater the likelihood that the consumer will be unable to make all of the payments without defaulting, becoming delinquent, or struggling to pay other expenses*. These difficulties arise both from the sustained burden of making payments and from the likelihood of income dips and expense spikes over a longer-term.[590]
- Lenders are *more callous about defaults and inability to repay with longer-term high-cost loans*, because the lender can make a profit early in the loan as long as it collects enough payments.[591]
- Longer loans have ugly amortization schedules that *conflict with consumer expectations* that their payments are making progress reducing their debt. Consumers can make thousands of dollars in payments while making *little progress in repaying the loan*.

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[584] *Id.* at 2.
[585] Cottonwood New Hire Guide, Handling Customers at 17.
[586] *Id.* at 17.
[587] Cottonwood New Hire Guide, Collection Transactions at 6.
[588] Cottonwood New Hire Guide, Collections at 12.
[589] Cottonwood New Hire Guide, Collections at 11.
[590] *See* section 10.4 above.
[591] *See* NCLC, Misaligned Incentives.

- It is *harder to escape* from a longer high-cost loan. It not only takes longer to pay the loan off by paying to full term, but it is also harder to use a tax refund or help from a family member to pay the loan off early because the loan balance likely will not have gone down much.
- The longer the loan, *the more the consumer pays in interest and fees*, and also potentially in late fees, overdraft fees and insufficient funds fees.
- Long loans can *trap consumers in long-term debt for a small loan*. It's one thing to take on a 30-year mortgage to obtain a home or a 5-year auto loan to obtain a car. It's another thing to be in debt for two years over a $500 loan that just helped pay one month's rent and did not improve the consumer's financial stability.

Loose rules on refinancings can lead in three ways to longer-term loans with high risk of inability to repay.

First, as described in the previous section, refinancing can turn a shorter loan into a longer loan. A six-month or nine-month loan can stretch out for years if it is refinanced regularly. A string of these relatively shorter loans that stretches out for a long time has all of the dangers highlighted above.

Second, as discussed in section 11.5.1 below, even if a lender has made an unaffordable loan, the proposal allows the lender to avoid the presumption that a refinancing would be unaffordable by offering a refinanced new loan that lowers the payment and stretches out the loan length. These stretched out loans are likely to be especially ugly—and by extension, difficult for borrowers to have the ability to repay over their extended loan terms. Thus, loose refinancing rules can permit a bait and switch from one unaffordable loan to another one with a high likelihood of proving unaffordable.

Third, the ability to refinance can disguise default rates and delinquencies, alleviating some of the risk that lenders would otherwise face when making unaffordable loans with especially long terms. Even with a leveraged payment mechanism, the longer the loan term, the greater the risk that the consumer will become delinquent at some point or even ultimately default. While lenders may still be able to make profits on loans that default if they collect enough payments,[592] the lender could be found to be in violation of the ability-to-repay rule if defaults get too high. But refinancing can help the lender to avoid defaults and delinquencies by giving consumers a respite when they are having difficulties, thus making the lender less wary of stretching out the loan term.

While proposed § 1041.10(c)(1) may impose a presumption of inability to repay for some of these refinances, many struggles will not be captured by the objective indicia listed in § 1041.10(c)(1). As discussed in 11.4.1.6 above, lenders often call consumers before payments are due, and lenders will be required to send notices of upcoming debits under proposed § 1041.15. Thus, lenders will likely aim to identify a struggling borrower and refinance a loan before the consumer is late, giving the consumer some cash out to cover a couple of months' worth of payments and avoiding a default on the first loan.

In addition, if the lender has lost the payment authorization under proposed § 1041.14, offering a refinance with cash back will be the easiest way for the lender to persuade the consumer to reauthorize automatic payments. For that reason, as discussed in section 11.4.3 below, it is essential for bounced payments to trigger a presumption of inability to repay.

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[592] *See* NCLC, Misaligned Incentives.

11.4.2. Presumption of inability to repay when an unaffordable loan is outstanding: § 1041.10(c)(1).

11.4.2.1. In General.

Proposed § 1041.10(c)(1) presumes that a consumer does not have the ability to repay a covered longer-term under § 1041.9 if the consumer currently has a covered or non-covered loan outstanding from the same lender or affiliate and one of four indicia of unaffordability are present. This presumption can be rebutted following the rules in proposed § 1041.10(d). Neither the presumption nor the ability to rebut the presumption applies to loans with balloon payments or short-term exemption loans, which have more firm limits on refinancing. We support firmer limits for those loans, as discussed in sections 8 and 11.3 above.

We support imposing a presumption of inability to repay during the time the borrower owes an unaffordable loan. Even if the lender has "checked the boxes" and arguably performed the procedural underwriting requirements of § 1041.9, there remains a significant chance that the loan will be unaffordable. This may be because the lender's underwriting was deficient, because there were other issues not captured in the underwriting analysis, or because the borrower's circumstances have changed.[593] Whatever the reason, if the loan has proven to be unaffordable, clearly the starting assumption must be that the borrower does not have the ability to repay a loan. (We discuss the situations in which that presumption can be rebutted in section 11.6 below.)

We support the proposal to apply the presumption of inability to repay whether the prior unaffordable loan was a covered loan or a non-covered loan. Either way, the lender has made an unaffordable loan and the consumer has demonstrated inability to repay. Indeed, if the prior loan was a non-covered loan, the presumption may be even more important. If the prior loan was exempt because the rate was under 36%, then it is especially unlikely that the consumer will be able to repay a higher-rate loan. If the prior loan was a high-rate loan that was exempt because it did not have a leveraged payment mechanism or vehicle title, then the consumer was unprotected by the ability-to-repay rules and the lender was likely engaging in reckless and evasive lending practices. The consumer could be subject to even greater harm from a covered loan.

As discussed at 3.4.2 above, we urge that the definition of "lender" be modified to ensure that loans by the same or affiliated service providers are also subject to this provision.

11.4.2.2. A loan should be "outstanding" for 30 days after an early repayment.

Proposed § 1041.10(c) applies only when the consumer "*currently* has a covered or non-covered loan *outstanding* …." (emphasis added). But lenders will be able to easily evade this rule by asking the consumer first to repay the original loan, which is then no longer "outstanding," and then take out a new loan—either the same day or within a few days. The CFPB is well aware of how lenders have evaded state prohibitions on rollover, and the same will happen here if the refinancing provision only applies to "outstanding" loans.

[593] Lenders will be quick to cite changed circumstances. But most "changes" are likely due to the income and expense volatility that is typical in the life of borrowers of covered loans.

These early payoffs will function much like the balloon loans addressed in proposed § 1041.10(b) – the consumer will have made a balloon payment, and will be reborrowing shortly thereafter. Thus, there should be a 30-day waiting period after an early repayment. The presumption should apply not only when a covered loan is "outstanding" but also for 30 days afterwards if a consumer makes a lump sum payment to repay a loan early.

For example, assume a loan has a 9-month term and that the consumer is delinquent on the sixth monthly payment. If the consumer then pays off the loan, she should be subject to a presumption of inability to repay if she seeks to reborrow within 30 days of that payoff.

Similarly, assume that a consumer takes out a 46-day loan with three biweekly payments, makes the first payment at day 14, and comes in at day 20, saying that she is having trouble making the next payment because her utility bill is due. The lender tells her she can pay off the entire loan and then take out another loan with some cash out a day or two later. She should be subject to the presumption of inability to repay for 30 days following the payoff of the first loan.

11.4.2.3. Other lenders should also be bound by evidence of unaffordability.

Proposed § 1041.10(c) only applies to lenders that are considering making a new loan to a consumer who has a prior loan from the same lender or an affiliate. We urge the CFPB to expand this provision to include any lender that makes a longer-term ATR loan under § 1041.9 following an unaffordable prior loan if the unaffordability of the first loan is apparent. (If this provision stays as is, it must also reflect loans offered by the same service provider such as a CSO, as discussed at 3.4.2 above.)

The new lender will have an obligation to check the registered information system for other covered loans and will know that one was taken out and whether it is still outstanding. If there is a prior covered longer-term loan outstanding, then the new lender should be required to obtain documentation that shows the loan is current before a new loan can be made.[594] Certainly, if the consumer expresses inability to repay the prior loan, the lender cannot ignore that statement. Thus, the new lender has the ability to obtain most of the information that the original lender must account for, and the new lender should be bound by that information as well.

These requirements would not apply to a new lender that is making a loan with lower total dollar costs in order to help the borrower get out of the previous loan. But as discussed below, we oppose an exemption for loans that merely have smaller payments or lower APRs but not lower actual costs.

11.4.2.4. Longer-term exemption lenders should be subject to the presumptions of unaffordability when refinancing their own unaffordable loans under § 1041.12.

While we believe that all lenders making loans under proposed § 1041.9 should be subject to a presumption of inability to repay if indicia of unaffordability are visible, we agree that lenders that make longer-term exemption loans under proposed § 1041.11 or § 1041.12 should not be restricted due to the unaffordability of another lender's loans. (See section 12 below for our concerns and recommendations related to longer-term exemption loans.)

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[594] The new lender may also have information on outstanding non-covered loans from a traditional credit report and should take that information into account, as discussed in section 6.3.5 above.

However, a lender that makes loans under § 1041.12 should be covered by § 1041.10 if it is seeking to refinance its own § 1041.12 loan and the indicia of unaffordability of § 1041.10(c)(1) are present.[595] Section 1041.12 loans may have higher amounts, longer terms and higher fees than the loans under § 1041.11. Even at 36%, a $5,000 or $10,000 2-year loan is a very expensive loan. In addition, the limits on default rates for § 1041.12 loans may give lenders an incentive to mask default rates through refinancing. Thus, applying the presumptions of § 1041.10(c)(1) to the § 1041.12 loans is important when the lender is refinancing its own loan.

In addition, at a minimum, as discussed in 12.2, any fees charged on loans under § 1041.12 should be rebated pro rata if a loan is refinanced.

11.4.2.5. Lenders should not be permitted to refinance their own defaulted loans (those 120 or more days delinquent).

The presumption of proposed § 1041.10(c)(1) only applies if there is a prior covered or non-covered loan "outstanding." Proposed § 1041.2(15) excludes from the definition of "outstanding loan" a loan on which the consumer has not made any payments within the previous 180 days. However, the CFPB has asked whether it should generally prohibit lenders from making a new covered longer-term to a consumer for the purposes of satisfying a delinquent obligation on an existing loan with the same lender or its affiliate. The CFPB has also asked whether it should include a specific presumption of unaffordability in the event that the lender or its affiliate has recently contacted the consumer for collection purposes.

Any lender that has made an unaffordable loan should not be able to use the collection process on that loan to trap the borrower into additional high-cost debt. This rule should apply no matter how long the loan has been delinquent if the lender is still attempting to collect it or to use it as a hook to induce new borrowing.

Indeed, a prohibition on refinancing defaulted loans should apply even if the loan is no longer "outstanding" because it has been fewer than 180 days since the last payment. Once the loan is in default (which the CFPB should define uniformly as 120 days delinquent), refinancing should not be permitted by the same lender. This rule should not be a presumption that can be rebutted. The lender can work out a payment plan on the original loan, but it should not be able to make a new loan while it has an unaffordable loan on the books.

To permit otherwise would:

- encourage aggressive collection tactics of the type the CFPB has criticized;
- allow lenders to re-age their debts—defeating statutes of limitations; and
- enable lenders to renew repayment devices that have been revoked (either by the consumer or by the proposed rule).

A strict rule on refinancing the lender's own delinquent debt will also help to enforce robust ability-to-repay assessments at the outset.

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[595] The balloon loans covered by § 1041.10(b) should be inapplicable, as the loans under §§ 1041.11 and 1041.12 may not have balloon payments.

If the delinquent loan has been sold or is no longer being collected by the lender or its affiliates, then there should be a presumption of inability to repay for 365 days following the lender's or affiliate's last collection attempt. This presumption would only apply to the original lender and its affiliates, not new lenders. (This is an increase from the 180 days currently proposed, by function of the proposed definition of "outstanding loan" that we urge the Bureau to modify.) The presumption could be rebutted by evidence of a change in the consumer's financial capacity. If a lender made an unaffordable loan, and the consumer has not been able to respond to a collection attempt within the past year, it is appropriate for the lender to have to show that the situation has changed. A longer period is appropriate in this situation than the 180 days required for a loan to be considered "outstanding" in proposed § 1041.2(15). The lender bears some responsibility and has more information than an outside lender, and six months is not enough time to expect that the consumer's situation has changed.

Our complete recommendations related to delinquent debt and review of the credit report more broadly are discussed at 3.7, 6.2.2, and 6.3.5 above.

11.4.3. Any late or bounced payment should trigger the presumption: § 1041.10(c)(1)(i).

Proposed § 1041.10(c)(1)(i) imposes a presumption of inability to repay if the consumer is or has been delinquent by more than seven days within the past 30 days on a scheduled payment.

We support a presumption of inability to repay if the consumer is delinquent on a prior loan. The delinquency is strong evidence of the consumer's inability to repay and appropriately creates a presumption that the lender should have a burden to overcome. However, we believe that the proposed standard is too weak.

First, any late payment, not merely one that is eight or more days late, should trigger the presumption. Setting the rule at eight days merely creates a glaring loophole, giving lenders the opportunity to contact the borrower and get them to refinance before the eighth day. If the consumer is even one day late, that is evidence that the consumer is struggling and that the unaffordability of the prior loan may be the very reason that the consumer is refinancing. Even a one-day late standard will miss many loans, as lenders often contact borrowers before the payment is due. Lenders will urge borrowers to refinance before a loan is actually delinquent.[596]

While there may be reasons other than unaffordability for being only one or two days late, the confluence of *both* a late payment *and* a request to refinance are a very strong indication of inability to repay. (And if the refinancing results from an offer from the lender to a borrower who is late, it shows how lenders will use refinancing to disguise unaffordability and avoid presumptions.) If the consumer does have the ability to repay, then the lender can wait to refinance until the consumer has a track record of being current or can rebut the presumption of inability to repay. Moreover, if the lender holds a leveraged payment mechanism, then being even one day late is most likely to be due to nonsufficient funds, not other benign reasons.

We also note that the Bureau's study of payment presentments, discussed in section 13.2 below, supports viewing payments that are only a few days late as a sign of unaffordability. That study

[596] Nonetheless, we do support the payment notice.

showed that 60% of payment requests made after an initial failed payment occur between one and seven days after the initial failed request, and a large majority of these failed.[597]

Nonetheless, if the Bureau accepts our recommendation in the next section to extend the lookback period for indicia of unaffordability to 90 days rather than 30, then the standard should be one day late in the past 30 days or more than seven days late in the past 90 days. It is important to have a one-day-late standard for the last 30 days to prevent evasions, but that is less of a concern if slight tardiness was a couple of months ago and payments are now current. However, as discussed in the next section, a more significant delinquency is still strong evidence of struggles, especially in light of the power of the leveraged payment mechanism.

Second, as discussed in section 11.4.2.5 above, lenders should be completely prohibited from refinancing their own defaulted loans (i.e., a loan that is 120 or more days delinquent), even if the loan is no longer "outstanding" because it is more than 180 days delinquent).

Third, the presumption of inability to repay should be triggered if any payment attempt during the review period was unsuccessful. An unsuccessful payment attempt should include not only a failed payment attempt as defined in proposed § 1014.14(a)(1) but also an unsuccessful attempt to make a payroll deduction.

Certainly, the fact that a payment has been rejected and funds are likely unavailable—even on payday— is powerful evidence that the consumer is unable to make the payment while meeting other obligations. A rejected payment is even stronger evidence of unaffordability than a late payment. Even if a payment is returned due to a stop payment order rather than for insufficient funds, that should also trigger the presumption of inability to repay. The consumer likely stopped payment due to the unaffordability of the loan.

Including unsuccessful payment attempts is especially critical in order to prevent lenders from evading the protections of proposed § 1041.14, which require the lender to obtain a new payment authorization after two consecutive failed payment attempts (as discussed at 13.2, we urge that the trigger requiring reauthorization be one failed payment attempt rather than two consecutive). The easiest way for a lender to obtain a new payment authorization will be to offer to refinance the loan with some cash-out. It is critical that these refinancings be subject to a presumption of inability to repay. While some may be caught if the borrower is more than seven days late or gets little to no cash-out, it is possible that the consumer will make a timely or nearly timely payment or will get enough cash-out to avoid the presumption. But even in those circumstances, the fact of two consecutive failed payments is powerful evidence of a struggling consumer.[598]

Fourth, for the same reasons, the presumption should be triggered if the lender learns that the account has insufficient funds—if, for example, the lender has obtained bank account login information—or if the lender otherwise refrains from making a payment attempt because it learns that the attempt will be unsuccessful.

[597] CFPB Online Payday Loan Payments at 13, 16.
[598] As discussed in section 13.2 below, we urge the CFPB to require payment reauthorization after any failed payment attempt.

Fifth, the consumer's revocation of authorization for an automatic payment should trigger the presumption until the consumer has successfully made at least one payment since the revocation. A revoked authorization does not (or at least should not) lead to a payment attempt, and thus there will be no unsuccessful payment attempt. But a consumer is likely to revoke authorization because a loan is unaffordable. If the consumer does not voluntarily pay after revoking the payment authorization, then the payment will be late and the presumption of inability to repay should be triggered. If the consumer does pay, then this circumstance would no longer apply.

Without a presumption in this situation, when a consumer contacts the lender to revoke authorization, lenders will have an incentive to push the consumer into a refinance that reauthorizes automatic payments by offering cash out. While there will be a presumption of inability to repay if the cash out is not substantial, lenders may offer enough cash out to avoid that presumption.

Finally, if the outstanding loan is a line of credit, a single past delinquency that has been cured should not prevent a new advance, but the credit line should be frozen with no new advances if a payment is late, until the payments are current. A new advance is a new loan, and the lender should not be making new loans if the loan is not current. If the lender is redetermining ability to repay at the 180 day point, a delinquency of more than seven days within the previous 90 days should trigger a presumption of unaffordability.

11.4.4. The lookback period for indicia of unaffordability should be 90 days, not 30.

Proposed § 1041.14(c)(1)(i) and (ii) impose a presumption of inability to repay if the consumer has been delinquent or has expressed inability to repay in the previous 30 days. However, the lookback period for these indicia of difficulties, and the others we have recommended, should be **90 days**, not 30. That is, there should be a presumption of inability to repay if, at any time in the prior 90 days:

- A payment was more than seven days late, or even one day late in the previous 30 days;
- A payment was unsuccessful;
- The lender refrained from initiating a payment because of a ping or other indication that the payment would not be successful; or
- The consumer revoked authorization for an automatic payment and did not subsequently make a payment voluntarily.

A 30-day period is insufficient because the leveraged payment mechanism gives the lender the ability to collect payments on time in many months despite the unaffordability of those payments. Payments that trigger overdraft fees will not fail and will not be visible to the lender. With a mere 30-day lookback, if a consumer is struggling, the lender will simply wait until a month when the payments went through and then push refinancing at that time. In addition, as discussed in section 8.3 above, a typical expense cycle for financially distressed consumers is likely substantially longer than 30 days.

Unaffordability will often not be evidenced by late or bounced payments, but if it is visible, events in the past 90 days are recent enough that they should trigger a presumption of inability to repay until the consumer has successfully paid on time for three month. We also note that the CFPB found that, when a payment attempt fails, bank account closures typically occur within 90 days of the first observed failed transaction.[599] So 90 days is a reasonable place to draw the line. The fact that the presumption can be rebutted should alleviate concerns about using a longer look-back period. If, for example, a

[599] CFPB Online Payday Payments at 24.

payment bounced 60 days ago, the presumption would apply but could be rebutted. The consumer could show, for example, that her hours were cut temporarily but have since rebounded, as discussed in section 11.6.1 below.

We recommend a corresponding change to proposed Comment 10(c)(1)(i)-1, which currently states that the presumption of inability to repay does not apply if a consumer was 10 days delinquent three months prior. The Comment should say that the presumption does not apply if the delinquency was *more* than 90 days earlier.

11.4.5. New delinquencies on a credit report should trigger a presumption of inability to repay.

In addition to delinquencies on an outstanding covered loan, any new delinquency that shows up on the consumer's credit report since the outstanding loan was taken out should result in a presumption of inability to repay. The lender was required to make a reasonable determination that the consumer had the ability to meet debt obligations and basic expenses. If, since the loan was taken out, the consumer has become so delinquent on another expense that it shows up in the credit report, the consumer clearly is not meeting those expenses.

Lenders do not report to credit bureaus unless a loan is at least 30 days late. Some companies, like utilities, may not report to the big three credit bureaus at all until the bill is 90 days late and/or is in collections. Thus, if these items have shown up on the credit report pulled by the lender since the last loan, it is a sign that the consumer is having significant trouble with the current covered loan.

At a minimum, any accounts that are over 60 days late since the origination of the outstanding loan should result in a presumption of inability to repay. This is the threshold under the Credit CARD Act when a lender can retroactively raise the APR on an existing credit card balance because of the presumed increased risk to the lender.[600]

11.4.6. Presumption if the consumer expresses inability to repay: § 1041.10(c)(1)(ii).

Proposed § 1041.10(c)(1)(ii) imposes a presumption of inability to repay if the consumer has, in the previous 30 days, expressed an inability to make one or more payments on the outstanding loan. We support the presumption in this situation for the obvious reason that the lender must take the consumer's statement at face value.

We also support the indication in proposed Comment 10(c)(1)(ii)-1 that a consumer can express inability to pay in "a number of ways." In particular, we agree that a consumer "may request ***or accept*** an offer of additional time to make a payment" (emphasis added). That is, even if the lender's file does not document that the consumer requested additional time, the fact that a payment date was extended should be treated the same way. The same is true when a payment is accepted late without a late fee that would normally be imposed. One study noted that "lenders often adjust installment dates to accommodate borrower requests," [601] but lenders are also likely to make offers to borrowers without waiting for a request when the lender contacts a borrower when a payment is late. Lenders also cannot be counted on to document that the adjustment was made in response to a request.

[600] 12 C.F.R. §1026.55(b)(4).
[601] Beales/Goel at 11.

We do have some suggested improvements for this provision and the related Comments.

First, for reasons discussed in the previous section, this presumption should apply if the consumer makes such a statement at any time in the previous 90 days. Consumers will not normally make these statements to lenders—or at least lenders will not document that they have—even when the loans are unaffordable. Thus, any such statement in the loan file should trigger a requirement that the lender examine whether the situation has changed. If it has not, then a new loan should not be made.

Second, we urge the CFPB to phrase this presumption slightly more broadly. The presumption should apply if the consumer expresses inability to make a payment on the loan or to cover any other expense that the lender was required to consider or account for when underwriting the loan. Money is fungible, and it is no different if the consumer says "I can't make my loan payment this month" or says "Here is my payment but I'm short on funds for rent, can I get a new loan?" Thus, if the consumer expresses an inability to pay rent, food, utilities, or child care expenses, the presumption would apply.

Third, the presumption should also apply if the consumer expresses inability to cover more sporadic, non-extraordinary medical expenses, car repairs, holiday expenses, and other expenses of the type that must be included in the cushion for basic expenses and volatility over the term of the loan. Any expression of inability to pay that puts into doubt the lender's compliance with or the consumer's fulfillment of the *full* ability-to-repay standard appropriately triggers a presumption of inability to pay. If inability to pay these expenses is immaterial, then the CFPB's rules on leaving a cushion to account for volatility are rendered worthless.

As discussed in section 10.4.2 above, the lender should be required to consider potential volatility over the entire term of the consumer's indebtedness from the date of the original loan, not just the period of the latest refinancing, in determining whether the new expense is one that should have been accounted for originally (and thus indicated inability to repay).

Thus, we recommend that proposed § 1041.10(c)(1)(ii) be re-phrased to read:

> (ii) The consumer expresses or has expressed within the past ~~30~~ <u>90</u> days an inability to make one or more payments on the outstanding loan <u>or to meet major financial obligations or basic living expenses</u>.

A new Comment should then cross-reference proposed Comment 9(b)(2)(i)-2 to make clear that the phrase "basic living expenses" includes sporadic and less predictable expenses of the type experienced by similar consumers over the period of time encompassed by the loan—and, in addition, by the entire loan sequence.

Finally, if the outstanding loan is a line of credit, the credit line should be frozen with no new advances if the consumer expresses inability to make loan payments or payments on other expenses that must be considered in the ability-to-pay determination.

11.4.7. Presumption if a refinancing results in a skipped or delayed payment: § 1041.10(c)(1)(iii).

Proposed § 1041.10(c)(1)(iii) imposes a presumption of inability to pay if the first payment on the new loan would be later than the next payment due on the refinanced loan. In other words, this provision covers refinancings that allow the consumer to skip or delay a payment that would otherwise be due. Proposed Comment 10(c)(1)(iii)-1 simply explains the provision.

We support this provision. If a consumer cannot afford to make a payment or needs more time to make a payment, that is a clear sign of difficulty repaying the loan. The fact that the new payment is due later is enough to impose this presumption. Lenders cannot be counted on to accurately document the reason for a refinancing that leads to a skipped or delayed payment. Refinancings can be used to mask unaffordability without this presumption. If delaying payment is not the reason for the refinance, then the lender can easily make the first payment due at the same time the next one would otherwise be due, or require the next payment on the old loan and start the new payments after that.

The same presumption should apply under an open-end line of credit if the transaction permits a consumer to skip or delay a payment. The credit line should be frozen with no new advances.

11.4.8. Presumption if cash out does not substantially exceed 30 days of payments: § 1041.10(c)(1)(iv).

11.4.8.1. Introduction.

Proposed § 1041.10(c)(1)(iv) applies a presumption of unaffordability if the new covered longer-term loan does not result in the consumer receiving cash out that substantially exceeds the payments that would be due within 30 days. This provision covers refinancings that are the equivalent of a skipped or delayed payment or payments even though the payment schedule is not directly changed.

We agree that a presumption of unaffordability is necessary in this situation, for the same reasons discussed earlier in connection with refinancings that skip or delay a payment. But the circumstances must be considerably broadened, and the CFPB should focus on the amount by which the prior loan has been paid down, not the amount of cash out; otherwise, the rule will encourage lenders to put borrowers in larger loans.

The CFPB has appropriately observed that a refinancing may mask inability to make payments on the prior loan even if there is no documented indication of unaffordability in the loan records. Just as a refinancing that permits a skipped payment is a sign of unaffordability, the same result can be achieved through one that yields cash out to cover that payment. The consumer can simply apply the cash to cover the payment.

The CFPB is imposing a presumption of unaffordability if the cash out does not “substantially exceed” 30 days’ worth of payments. The CFPB notes:

> A transaction that would result in a consumer receiving only enough cash to satisfy the forthcoming payment or payments due to the lender or its affiliate within 30 days, the length

> of a typical income and expense cycle, may indicate that the consumer is having difficulty making payment on the outstanding loan and is seeking the new covered longer-term loan in order to obtain cash to make those payments.[602]

We agree that a refinancing that is the equivalent of simply skipping one month's payments (skipping either one monthly payment, two semi-monthly payments, or two to three biweekly payments, depending on the calendar) most likely shows that the prior loan was unaffordable. All the refinancing has done is given the consumer a temporary reprieve from the loan with no extra cash for any other purpose.

However, we disagree with two fundamental aspects of this provision. First, the focus should be on how much of the prior loan the consumer has repaid, not how much cash out the consumer has received. Second, to avoid the presumption of inability to repay without reborrowing, the consumer must have made more progress on the first loan than the proposal requires.

11.4.8.2. The focus should be on lack of progress repaying the prior loan, not the amount of cash-out.

The CFPB's analysis of refinancings shows that consumers who refinance typically receive from $350 to $450 in cash out.[603] The CFPB has also found that, in general, consumers who refinance only slightly increase the size of their loans.[604] Thus, the CFPB concludes that the median borrower has paid down a substantial amount of the old loan before the refinancing.[605] In other words, the CFPB is essentially saying that the cash-out is largely generated by what some lenders call "equity" in the loan—the amount by which the prior loan has been repaid. While left unstated by the CFPB, it appears that the CFPB concludes that the fact of a "substantial" reduction in the prior loan balance prior to refinancing shows that the consumer has not been struggling to repay the loan.

Setting aside the question of how much is a "substantial" cash out, the CFPB does not explain why proposed § 1041.10(c)(1)(iv) focuses on cash out rather than loan reduction. The CFPB may view the two as essentially the same thing in light of its finding that cash-out largely comes from principal reduction.

However, it is critically important to focus on progress in repaying the prior loan rather than the amount of cash out for several reasons.

First, only a standard that requires real, substantial progress in repaying the first loan before a refinancing is consistent with and supportive of the requirement that lenders ensure ability to repay without reborrowing. The amount of cash-out that a consumer is given says nothing whatsoever about their ability to repay the prior loan. The fact that a consumer has in fact paid down the prior loan does. Ironically, in its discussion of refinancing and cash-out, the CFPB's final conclusion is that substantial cash-out, together with loan sizes that generally do not increase, "implies that the borrower paid down a substantial amount of her loan before the refinancing occurred." That is, the CFPB seems to

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[602] 81 Fed. Reg. at 48027.
[603] Supplemental Findings at 19.
[604] Supplemental Findings at 20.
[605] *Id.*

acknowledge that *repayment* is the relevant criteria.[606] We agree—and repayment progress should be measured directly, not indirectly.

If a consumer has not made substantial progress in repaying the loan, the refinancing is highly likely to reflect a failure of original underwriting. While we are not pushing for a complete ban on refinancing before 100% of the prior loan has been repaid, if the fact of mid-term and early-term reborrowing is to be ignored, it must be in circumstances where the consumer has truly demonstrated the ability to *substantially* repay the loan in *practice*. A focus on cash-out does not do that. The proposed rule would permit refinancings for consumers who may have made little progress in repaying their prior loans—without even a presumption of unaffordability that can be rebutted.

Second, a focus on cash out requires lenders to push consumers to agree to larger loans. If the consumer's principal reduction on the first loan is not enough to generate sufficient cash out, the lender will have to push the consumer to increase the loan size to avoid the presumption of unaffordability. Even if the consumer has substantially paid down the prior loan, she may be required to reborrow more than she otherwise would in order to generate sufficient cash out.

For example, the CFPB found that the median consumer who refinanced a storefront payday installment loan received $402 in cash-out. This cash was not entirely generated by principal pay-down: the median new loan was more than 12% larger than the original loan.[607] Of the $402 in cash-out, nearly a third, $123 came from the larger loan,[608] and only $279 came from the principal pay-down. With a $994 median previous loan size[609] and assuming 12 biweekly payments[610] and a 248% APR,[611] the biweekly payment would be $142.42. Without the extra $123 from the increase in loan size, the $279 cash-out would thus not even cover 4 weeks of payments (*i.e.* two payments of $142.42, totaling $284.84). That means that the median storefront payday installment lender in the CFPB's data *must* push the consumer to increase the loan size in order to avoid the presumption of inability to repay—just as they are already doing.[612]

[606] Supplemental Findings at 20.
[607] Supplemental Findings at 20. The CFPB found that the ratio of the previous loan to the new loan was .89. Reversed, 1.0 divided by .89 shows the new loan was 112.4% as large as the previous loan.
[608] For storefront installment loans, the ratio of the median cash-out to the median new loan principal was .36. Supplemental Findings at 20. So if the cash-out was $402, the median new loan was $1117. The ratio of the median previous loan to the median new loan was .89, so the previous loan was $994.
[609] *See id.*
[610] The CFPB has stated that this is the most common loan product. Supplemental Findings at 29.
[611] That is the median APR that the CFPB found with storefront payday installment loans. Supplemental Findings at 13.
[612] As discussed below, even using a cash-out standard, $402 in cash-out should not be viewed as "substantially" exceeding the $284.84 in payments due over 4 weeks.

Median Refinanced Storefront Payday Installment Loan (assuming 248% APR, 12 biweekly payments of $142.42)	
Original loan	$944
Balance at refinancing	-$715
Amount repaid	=$279
New loan	$1117
Increase over prior loan	$123
Total cash-out	$402

If loans are refinanced more than once, as is likely, loan sizes will continue to creep up. For example, an industry report also shows refinancing leading to larger loans. The report found that consumers who refinance take out an average of 2.6 loans and that, for the median consumer, the last loan is 20% higher than the first one. [613] This is similar to the pattern that has been found in short-term payday loans—where consumers get deeper in debt over time, rather than digging themselves out.[614] This pattern is exactly opposite to the one the CFPB should be encouraging.

While larger loans will have to pass an ability-to-repay determination, this may not be hard under the rule as proposed, especially if the loans creep up gradually or the loan term is stretched out. Indeed, the lender's need to increase loan size without increasing the payment too much will encourage a trend towards longer loans. As discussed above, longer loans are more dangerous for financially distressed consumers, requiring them to sustain payments for a longer period of time.

The way a cash-out focus can lead to ugly, longer loans that are unlikely to be affordable on a sustained basis can be seen in the following example. Assume that a lender makes a $500, 398% APR loan with 13 biweekly payments of $90.78. After four payments, the consumer is struggling and seeks cash to help with necessary expenses. In order to avoid a presumption of inability to pay under proposed § 1041.10(c)(1)(iv), the lender wants to offer enough cash-out to cover eight weeks of payments.[615] However, the consumer has only reduced the loan principal by $71.56, so simply renewing the same size loan would not generate enough cash-out.

Instead, the lender offers to increase the loan amount to $750 with the same $90.78 payments, but with a lower 296% APR and a term twice as long: 26 biweekly payments. Although the lender might have to build in an additional cushion for income and expense volatility for the longer loan term,

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[613] Beales/Goel, supra , at 38-39. The report found that the average last loan was 48% larger, indicating that a small fraction of loan sequences resulted in a more substantial increase. A dramatic jump in loan size might indicate a lender that offered a "tester" loan to a new customer and then a much larger loan once the consumer repaid the first loan. Smaller loan increases would appear to be indicative of loan creep and a deepening debt trap.

[614] A study by CRL based on Oklahoma borrowers found that initial loans averaged under $279 but the average borrower owes $466. Uriah Kina & Leslie Parrish, CRL, Payday Loans, Inc.: Short on Credit, Long on Debt at 3-4 (Mar. 31, 2011), http://www.responsiblelending.org/payday-lending/research-analysis/payday-loans-inc-exec-summary.pdf.

[615] It is not clear if 8 weeks of payments would "substantially exceed" the payments due in 30 days under the CFPB's interpretation of that provision. If the CFPB retains a metric measured by the payments due, we urge the CFPB to require the cash-out or principal reduction to equal or exceed 90 days of payments. See section 11.4.8.4.

without changes in the current proposal, it seems unlikely that this requirement has enough specificity to prevent a dangerous longer-term loan.[616]

Refinancing Into Larger Loan with Longer Term		
	Original Loan	Refinanced Loan
Loan	$500	$750
APR	398%	296%
Term	26 weeks (13 biweekly payments)	52 weeks (26 biweekly payments)
Payment	$90.78	$90.78
Total finance charge	$679.85	$1,610.28
Total payments	$1,180.14	$2,360.28

This pattern also has resulted in a bait-and-switch from a smaller, shorter loan to a larger, longer, and more expensive one. While the APR has gone down from 398% to 296%, that should not be seen as a positive development. Lenders almost always charge lower APRs on larger and longer loans. The APR is still extraordinarily high and the finance charges on the new loan are much higher. The total cost has doubled from $1,180.14 to $2,360.28. The total finance charges have increased nearly two and a half times—from $679.85 to $1,610.28—even though the new loan is only half again bigger. An extra six months and nearly $1000 in interest have been added for just $250 in additional credit. The lender has taken advantage of the borrower's need for addition cash to put the borrower in a far different, more expensive, and riskier loan than the borrower originally signed up for.

Even if refinancing does not result in larger loans for many borrowers at the median, avoiding rules that encourage larger loans is important to protect the more vulnerable borrowers. We don't know the numbers at the 25th percentile, but those consumers likely are reborrowing even earlier in the loan term, and must take out even larger loans to generate the same amount of cash-out.

If, instead, the CFPB focuses on the amount by which the prior loan has repaid, there is no reason to push larger loans. The consumer either is or is not eligible to refinance without a presumption of inability to repay, regardless of the size of the new loan. In the example above, assuming that $402 is enough pay-down to qualify as "substantial" (we do not believe it is), and absent the other indicia of unaffordability, the consumer could refinance with no presumption after seven of 12 biweekly payments. The consumer could take out a new loan of the same size and get the full amount of cash out, or she could get a smaller loan if she preferred.

Third, permitting lenders to avoid a presumption of inability to repay when they offer cash-out, regardless of the amount of the prior loan paid down, encourages refinancing of especially unaffordable loans with interest-only periods, up-front fees, add-on products, astronomical APRs, and especially long terms. When any of these factors are present, the consumer's initial payments will make very little progress in repaying the loan. In addition, a significant portion of the cash from a refinance with be eaten up by new fees and charges on the new loan.[617] Thus, in order to generate cash-out to avoid the presumption, these lenders making the worst of the worst loans will have an especially strong incentive to push borrowers into larger loans. Refinancing of these loans is even more

[616] See sections 10.4 and 11.4.1.5.
[617] *See* NCLC, Installment Loans at 19-25.

abusive, because it extends the already very long period when the consumer is making substantial payments with little to no progress in repaying the loan.

Conversely, a focus on pay-down rather than cash-out creates an incentive for loans with shorter terms, lower rates, no up-front fees, regular amortization schedules, and payments that make significant progress in repaying the loan. These are exactly the kinds of loans the CFPB should be encouraging, because consumers are more likely to be able to afford them and the loans are more likely to perform as consumers expect. Shorter loans are more likely to amortize more quickly than longer ones. The faster that the payments reduce principal, the faster the lender will be able to refinance the loan without having to rebut a presumption of unaffordability. Discouraging longer loans and encouraging shorter loans (i.e., those with 3- to 6-month terms) is especially important for financially distressed borrowers, for the reasons discussed in section 10.2 and 10.3 above.

We can imagine a few reasons that could be motivating the CFPB's focus on cash-out rather than pay-down. But these reasons can be accommodated with a pay-down approach.

First, proposed § 1041.10(c)(1)(iv) is designed to impose a presumption of inability to repay when the refinancing is the equivalent of skipping a payment or two. Measuring the amount of cash-out is a way of determining whether the refinancing simply yields a small respite from making loan payments (sought due to difficulty repaying) or instead is an effort to obtain significantly more credit for some other purpose. (Although, as discussed above, the need to reborrow for another ordinary expense is a strong signal of inability to repay without reborrowing.)

But skipped-payment refinances can be evaluated by measuring the amount of the prior loan paid down--and thus available for reborrowing—rather than measuring the actual amount of cash-back provided. The cash-out provided will most likely equal or exceed the paydown, as the CFPB's analysis shows. But measuring paydown rather than cash-back avoids the problems of pushing people into larger loans and of permitting refinances of loans where the consumer has made little to no meaningful progress in repaying.

Second, the CFPB may be attempting to accommodate lenders that start new borrowers out with small tester loans, planning to offer a larger loan after the consumer proves able and willing to make payments. The jump in loan size in that situation is not due to trouble repaying, but rather to the fact that the first loan is smaller than the consumer wanted or the lender was willing to give to an unknown customer.

But if a small tester loan has a reasonably short repayment period, then the borrowers should be able to show that they can substantially repay that small loan before getting a larger loan. If the lender had some question about the borrower's financial capacity, meaningful progress on the first loan answers that question better than simply the lender's ability to collect a few payments. While the payments may also help the lender screen for fraud, the lender can accomplish the same purpose by making a small loan and waiting for it to be paid off, without risking refinancing abuses or bait-and-switch from small loans to large ones.

Third, the CFPB may expect that some consumers take out an initial loan smaller than their ability to pay can justify. They then decide later that they would like to take out additional credit for a discretionary expense—or truly unusual expense—of the type that does not question the validity of the original ability-to-pay assessment.

But this “overqualified borrower” who takes out a high-rate loan with a leveraged payment mechanism is far less likely than one who is refinancing because of an inability to repay without reborrowing. The “unusual expense” scenario is an exception that would swallow the rule, as discussed in section 11.6.2 below. Moreover, if the first loan is a small loan with a reasonable repayment period, then a pay-down test will not prevent new credit for very long. If the first loan is a bigger and longer loan, then it is less likely that a consumer who does not have lower cost, non-covered credit options has significant additional borrowing capacity. It is more important to prevent the more likely early refinancings that reflect unaffordable loans, and to stop a cycle of debt for struggling consumers, than it is to accommodate this rare and unlikely scenario of the subprime consumer with excess ability to repay.

11.4.8.3. Substantial progress repaying the prior loan—i.e., repayment of 75%—should be required to avoid a presumption of inability to repay without reborrowing.

Proposed § 1041.10(c)(1)(iv) imposes a presumption of inability to repay if the cash-out from the refinancing does not “substantially exceed” the payments due on the original loan within 30 days. The rationale is that a refinancing that simply enables the consumer to skip a month’s worth of payments likely reflects difficulty managing the loan payment.

We agree that refinancings done for the purpose of skipping a payment or payments should trigger a presumption of inability to repay. However, we believe that the standard should be even stronger, imposing a presumption unless the consumer has made substantial progress in repaying the loan, such as paying off 75% of the prior loan.

A 75% standard bolsters the integrity of the ability-to-repay rule. Setting aside the significant caveat that the leveraged payment mechanism often masks financial difficulties, a consumer who has successfully repaid well more than half the loan, with the end in sight, has at least demonstrated sufficient funds on payday to *actually, in practice, repay* the bulk of the loan. Conversely, a consumer who seeks to reborrow before substantially repaying the prior loan has not even demonstrated that much.[618]

When refinancing happens with many weeks or months of payments remaining, the power of an offer of extra cash to address immediate needs for a borrower financially stressed by an unaffordable loan will likely overpower concerns about extending a loan term that already feels far off. The CFPB’s own observations about the difficulty that consumers have in balancing problems they face today with costs and risks down the road confirms the danger of letting lenders push early refinancing.[619] A 75% standard mitigates that risk.

We recommend that a 75% standard be measured by the amount of principal repaid. That will serve as a check on loans structured with interest-only or very slow amortization schedules, which can make it more difficult for consumers to pay off their loans, take advantage of consumers’ lack of understanding, and lead to more substantial debt traps when loans are refinanced. A second-best approach would require 75% of the payments to be made.

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[618] We note again here that the reasonable ability-to-repay determination cannot assume the consumer will get new credit.
[619] See section 5.4 above.

If the CFPB is unwilling to adopt the 75% standard, we urge it to impose a presumption of inability to repay unless the consumer has "made substantial progress" in repaying the loan.

11.4.8.4. If the CFPB measures cash-out against the monthly payments, cash exceeding three months' payments should be required to avoid a presumption.

If the CFPB retains the proposed exception to the presumption of unaffordability for new loans that provide cash-out greater than an amount measured by monthly payments, it should strengthen this standard considerably. In order to avoid a presumption of inability to repay, proposed § 1041.10(c)(1)(iv) requires the cash-out to "substantially exceed" the payments due in 30 days on the original loan. Proposed comment 10(c)(1)(iv)-1 explains that, if a loan requires $100 biweekly payments, then $200 in cash-out is not substantially more than the payments due in 30 days. The comment further states that $1000 in cash-out *is* substantially more than the $200 in payments due in 30 days.

With respect to the first example, while $200 is clearly not "substantially more" than $200 (the amount due in 30 days), the example is unhelpful because it is so obvious. The CFPB should include a better example—i.e., that $300 or $400 is not substantially more than $200.

More importantly, if the CFPB declines to adopt a refinancing standard based on substantially repaying the original loan, and instead continues with an approach tied to the amount of the payments due, we urge the CFPB to strengthen the standard and require the cash-out to equal or exceed three months' worth of payments.

We agree with the example in the proposed comment stating that $1000 in cash-out is substantially more than $200. We further agree that a consumer who has obtained new credit that is the equivalent of five months' worth of payments—or better yet, who has reduced her original principal by that much—is less likely to have refinanced due to difficulty covering her payments than one who has simply gotten a one- or two-month reprieve.

However, there is a lot of space between this *five-month* example and the rule's requirement of substantially more than *one* month. It is not clear how much more than one month is required to avoid the presumption. The rule could be read to imply that two months of payments—or even 45 days' worth—is enough.

Indeed, while the example in the proposed comment is encouraging, the CFPB's discussion of the impact of the cash-out provision is more troubling. The CFPB notes that its "analysis of confidential data gathered in the course of its statutory functions indicates that the circumstance in proposed § 1041.10(c)(1)(iv) would likely occur rarely because most consumers in the loan sample analyzed by the Bureau took out substantial cash when refinancing a longer-term installment loan."[620] This statement is troubling for two reasons.

First, if the cash-out rule of § 1041.10(c)(1)(iv) would "rarely" result in a presumption of inability to repay, then the proposed rule simply endorses the payday lenders' current business-as-usual approach

[620] 81 Fed. Reg. at 48027.

of keeping consumers trapped in debt with unaffordable loans and high levels of reborrowing before the loan is repaid. Even the CFPB observes that there is already a "very high level of refinancing" of longer-term loans.[621]

Second, the CFPB's data seems to indicate that the "substantial" cash-out that the CFPB has observed is only a bit more than the cash needed to cover 30 days' worth of payments. That is hardly enough to allay concerns that the reborrowing just gives the borrower a short respite from unaffordable payments.

We assume that the confidential cash-out data that the CFPB describes is the same data that is analyzed in the Supplemental Findings. The Bureau found that the median cash-out ranges from $345 to $450 depending on the type of loan, and the CFPB characterized those amounts as "substantial."[622] We do not know the payment size for the loans in the CFPB study or how the median cash-out amounts compare to the payments due in 30 days. But assuming that a storefront payday installment loan has a 248% APR and 12 biweekly payments,[623] the biweekly payments would be $142.42 and the payments due in 28 days would be $284.82. The CFPB found that median cash-out for a storefront installment loan was $402.[624] That is only 141% of the payments due in 28 days—or just over 39 days of payments on a pro rata basis. In other words, "substantially exceed" 30 days' of payments could really mean "just a bit over 30 days."

A weak cash-out standard is all the more troubling if the CFPB continues to measure it by actual cash-out regardless of the amount of pay-down on the first loan. As illustrated in section 11.4.8.2 above, only $279 of the $402 in cash-out on the median storefront installment loan came from principal reduction; the remaining $123 came from increasing the size of the next loan. The median $279 in principal reduction is less than the $284.42 in payments we estimate are due in 28 days. Thus, if our assumptions about the data and interpretations of the CFPB's meaning are correct, the proposed rule allows a refinance without any presumption of inability to repay even if the prior loan has not even been paid down enough to generate 30 days' worth of payments.

We hope that we are misinterpreting both the data and the CFPB's understanding of the proposal. In order to avoid evasions, protect borrowers, and provide clarity for lenders, we urge the CFPB to adopt a rule with more specificity as to the amount of cash-out (or, we hope, principal reduction) needed to avoid a presumption of inability to repay. If the CFPB decides to focus on the relationship between the amount of cash and the monthly payments, we urge the CFPB to draw a clear line at three months' worth of payments. That is, there would be a presumption of inability to repay unless the cash-out (or, better, principal reduction) equals or exceeds the payments that would be due in three months. To provide some wiggle room for loans that will never meet that standard, the CFPB could permit refinancing at the time of the next-to-last payment even if the pay-down or cash-out does not equal three months of payments.

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[621] 81 Fed. Reg. at 48025.

[622] The median cash-out with a refinancing was $345 for online payday loans, $402 for storefront payday installment loans, and $450 for vehicle title installment loans. Supplemental Findings at 20.

[623] As described in section 11.4.8.2, the Supplemental Findings found that 248% is the median APR for a storefront payday installment loan and that a loan with 12 biweekly payments was the most common loan.

[624] Supplemental Findings at 20.

For all of the reasons discussed earlier, reborrowing before the consumer has substantially repaid the loan is likely to indicate inability to repay while meeting other expenses without reborrowing. A refinancing that simply gives the consumer a two-month break in payments would seem to be driven by the burden of those payments. A two-month break may be a particularly insignificant benefit to the consumer when it comes along with a substantially longer loan term, which payday lenders are likely to adopt in order to lower the payments and preserve enough residual income.

A stricter standard for permissible refinancings will help prevent lenders from disguising difficulties paying and default rates. The longer that a lender has to wait before a loan can be refinanced, the more certain the lender needs to be that the consumer truly can afford to pay that long. Conversely, a lender that does not adequately underwrite or that makes dangerously long loans risks accumulating evidence of delinquencies, bounced payments, and defaults that casts doubt on the reasonableness of the lender's ability-to-repay determination.

Finally, again, whatever yardstick the CFPB ultimately chooses, we urge the CFPB to measure it by pay-down and not cash-out, as discussed in section 11.4.8.2. For example, even if the standard were two months of payments, the CFPB could require the loan to be paid down by that amount rather than just evaluating the cash-out. This approach focuses on a more telling indicator of ability to repay—actual repayment progress—while avoiding the risks of a rule encourages lenders to push struggling consumers into larger loans. A focus on repayment also imposes tougher refinancing limits on loans with payments that make little progress in repaying the loan and are especially likely to take advantage of desperate consumers.

11.4.9. Presumptions for open-end credit when refinancing before substantial repayment or with little cash-out.

The presumption of inability to repay in proposed § 1041.10(c)(1)(iv) should also apply in certain situations involving open-end credit where there is reborrowing by a consumer who has not been making significant progress in repaying the loan.

First, a presumption of inability to repay should apply when a lender *increases the credit line* for a consumer who has had sustained high usage of the credit line without making substantial progress in repaying the credit. This is similar to the closed-end situation where the consumer refinances before making substantial progress in repaying the loan or without receiving significant cash-out.

Thus, if the CFPB adopts our proposal to adopt a presumption of inability to repay before a closed-end loan has been 75% paid off, a similar presumption should apply for open-end loans. The presumption would apply whenever a credit line increase is being considered for a consumer who has not made payments that reduced the balance due below 25% of the available credit at some point over the previous 90 days. For example, if the consumer's credit line is $1000, then the presumption would apply to any credit line increase for a consumer who had not reduced the balance below $250 at any point in the previous 90 days.

The rule would apply similarly to an increase in a credit line if the CFPB instead retains the current approach of assessing the amount of cash-out from a refinancing. For example, if a borrower of a closed-end loan has $200 in payments due within 30 days and refinances the loan with $200 in cash-out, there is a presumption of inability to repay. The same presumption should apply if a consumer with a credit line has $200 in payments due within 30 days, has little or no available credit, and seeks an increase in the credit line that increases the available credit by only $200. In other words, the presumption would apply if the new available credit from a credit line increase, together with the current available credit, does not meet whatever standard the CFPB adopts for principal pay-down or cash-out to avoid a presumption of inability to repay a closed-end loan.

We note that it is natural for a responsible lender to start a consumer with a smaller credit line and then to increase it if the consumer proves creditworthy. But if the consumer is making only minimum payments on a smaller credit line that do not significantly pay down the line, that casts doubt on his ability to handle a larger credit line.

Second, a presumption of inability to repay should result in the *freezing of the credit line*, preventing new advances, if a consumer has had sustained high usage (90%) of the credit line for 90 days without making progress paying it down. A consumer who has not reduced the credit line below 90% utilization in the previous 90 days should be subject to a presumption of inability to pay that prevents new advances. The same presumption would apply if the credit line was reduced below 90% only due to a required minimum payment and the consumer took out a new advance within 30 days after the payment, bringing the utilization above 90%. As discussed in section 10.6.3 above, we support the proposed requirement that lenders of open-end credit be required to reassess ability-to-repay every 180 days. As part of that reassessment, sustained high utilization would be grounds for freezing the credit line.

11.5. The Exceptions to the Presumptions of Unaffordability Must Be Narrowed To Prevent Harm.

11.5.1. The exception for substantially smaller payments should be eliminated unless the total cost is the same or lower: § 1041.10(c)(2)(i).

The CFPB proposes two exceptions to the presumption of unaffordability for loans with the indicia described in proposed § 1021.10(c)(1). The first exception is when every payment on the new loan is "substantially smaller" than every payment on the outstanding loan. Proposed comment 10(c)(2)(i)-1 explains that $100 is substantially smaller than $300 but $250 is not.

The CFPB should eliminate this exception. The CFPB should permit an exception for loans with smaller payments only if the total dollar cost of the new loan payments are the same or lower than the amounts still owed on the original loan, which it can achieve by modifying the second exception.

The Bureau rightly notes that the smaller-payment exception "could prompt some lenders to extend loans with substantially smaller payments but a substantially longer duration, which could impose higher costs on the consumer over repayment of the loan . . . ."[625] Yet the Bureau concludes, without explanation, that the benefits of this exception outweigh this potential source of consumer harm.

We disagree. It is highly likely that lenders will exploit this exception and harm consumers.

For example, a lender could start a consumer on a $500 loan at 398% APR with 13 biweekly payments of $90.78. After six payments, the consumer is struggling, is eight days late, and the lender encourages renewal of the same loan and gives the consumer $126 in cash-out. There would be a presumption of

[625] 81 Fed. Reg. at 48027.

inability to pay both because the consumer is delinquent and because the cash-out is less than 30 days of payments. Assuming that a $45 payment would be viewed as “substantially smaller” than a $90.78 one, the lender could avoid the presumption of unaffordability and refinance the consumer into a loan three times as long with 39 biweekly payments of $45 and a 225% APR. While the payments and the APR are lower than the original loan, the new one is more expensive: the total finance charge for the same loan amount has doubled, from $680.14 to $1,255.00, and the total cost has gone from $1,180.14 to $1,755.

Example of Loan Refinanced into Smaller Payments		
	Original loan	Refinanced loan
Loan amount	$500	$500
APR	398%	225%
Biweekly payment	$90.78	$45.00
Number of payments	13	39
Total finance charge	$680.14	$1,255.00
Total payments	$1,180.14	$1,755.00

The CFPB may see a benefit for consumers with this type of refinancing because it reduces their payments and might avoid a default on the first loan. But there are several reasons why the potential benefit of the exception is not significant and is vastly outweighed by the potential harm.

First, this exception will give lenders an incentive to push the ability-to-repay envelope on the first loan and offer loans with high, likely unaffordable payments. If the loan proves unaffordable, the lender then simply renews the loan with smaller payments but a higher total cost. This exception will be especially useful for lenders that seek to renew a leveraged payment mechanism that was lost under proposed § 1041.14 due to failed payments on an unaffordable loan. Even if the consumer ultimately defaults on the new loan, the lender may still come out ahead, because when a small loan has a long term, the lender recovers far more than the loan principal early in the term.[626]

Second, the new loan harms the consumer in several ways even if the consumer ultimately pays it in full. The consumer likely incurs higher finance charges: $575 higher in the example given above. The consumer is in debt longer: in the same example, 18 months, compared to the 3 months remaining on the original loan. Over that longer period of time, the consumer risks overdraft fees, nonsufficient funds fees, late fees, and other consequences stemming from problems meeting other expenses.

Third, the consumer has been taken advantage of by the bait-and-switch and ends up with a new loan that is substantially different than the one she originally agreed to.

Fourth, the new loan may still end up in default, but later and at a higher cost to the consumer. If the consumer is going to default in any event, it is better to default sooner than later. The sooner the consumer defaults, the sooner the clock starts running on the statute of limitations on the loan and on the period that the default can damage her credit report. Postponing default also adds to the costs that a struggling consumer incurs before defaulting, including additional payments as well as the other consequences of unaffordable loans.

[626] *See* NCLC, Misaligned Incentives at 20-22.

The CFPB notes that the lender would still need to satisfy the ability-to-repay requirements for the new loan. But that is cold comfort when the lender has already been wrong with its first assessment. The lender is highly likely to simply plug the new loan into its old formula and determine that any loan with smaller payments is now affordable. While the lender will have to account for income and expense volatility over any longer term, that vague requirement may not deter the lender unless the CFPB tightens it up, as discussed in section 10.4 above.

A smaller-payment exception should be available only if the new loan does not increase the total actual dollar cost of the payments. This condition will ensure that the exception cannot be used to push consumers into longer, more expensive loans.

11.5.2. The exception for substantial reduction in "total cost of credit" should require reduction in the total actual dollar cost of payments, not the merely the rate: § 1041.10(c)(2)(ii).

Proposed § 1041.10(c)(2)(ii) creates a second exception to the presumption of unaffordability if the new loan results in "a substantial reduction in the total cost of credit" compared to the first loan. Proposed comment 10(c)(2)(ii)-1 explains that if the total cost of credit for the original loan was 100%, then a 45% total cost of credit is a substantial reduction but 90% is not.

The phrase "total cost of credit" is defined in proposed § 1041.2(a)(18). The cost is "the total amount of charges associated with a loan expressed as per annum rate" as detailed in § 1041.2(a)(18)(i), (ii) and (iii). As this definition and the proposed comment make clear, the "total cost of credit" is an *annual rate*, not the actual total cost of credit. It is basically an APR (though with appropriately broader fees included than in the TILA APR formula).

It is entirely possible—indeed, likely—that a loan with a lower "total cost of credit" will in fact have a higher *actual total cost*. Our biggest fear is that refinancing will push consumers into bigger, unaffordable longer-term loans that cost more and are a bigger debt trap. As detailed in other sections, both the underwriting requirements and the limitations on refinancing loans without substantial cash out give lenders an incentive to make payments smaller and loans bigger and longer.

Bigger and longer loans almost always have lower interest rates. But that does not mean that they are better or safer loans that should be exempt from a presumption of unaffordability. To the contrary —if there are already indications that the consumer is struggling with the first loan, the last thing we should incentivize is bigger or longer loans, even if the rate is lower.

Here are a few examples of how lenders charge lower rates on bigger and longer loans, taken from the loans analyzed in a recent report by the National Consumer Law Center.[627] We realize that there is a substantial jump in loan size (and variation in the state where the loans are made) in some of these examples, and they may not reflect a logical progression from one loan to another as a result of refinancing. But they do illustrate the larger point that lenders reduce rates as loans get bigger and longer.

[627] NCLC, Misaligned Incentives.

Lender	State	Loan*	Interest Rate**	# biweekly payments
ACE Cash Express	NM	$500	398%	13
ACE Cash Express	CA	$2,600	209%	20
Advance America	SD	$500	349%	12
Advance America	CA	$2,550	196%	26
CashNetUSA (Enova)	OH	$800	459%	12
CashNetUSA (Enova)	OH	$1,200	379%	15
Elevate (Rise)	TX	$800	350%	10
Elevate (Rise)	AL	$2,250	274%	26
Speedy Cash	MO	$500	430%	39
Speedy Cash	MO	$1,500	199%	39
**Rates are rounded. Rates are generally as stated by lenders and may not be accurate APRs.				
*Fees may reduce the amount the consumer receives or may be added to the amount financed.				

Below are some examples of how a consumer who has a $500 loan at 398%, payable in 13 biweekly payments of $90.61, may be refinanced into a loan with a lower rate but a much longer-term and a higher cost. We do not know if the rate reductions shown would count as a substantial reduction. But all of these loans increase the total dollars that the consumer is obligated to pay. They also all substantially increase the remaining time the consumer is in debt, from doubling it to increasing it more than five-fold. As we have previously discussed, longer loans are especially dangerous, even if the payment is relatively small.

Refinancing Into Loan at Lower APR But Higher Cost						
	Original Loan	**Remaining Balance after 6 payments**	**Refinanced Loan 1 (same original loan, smaller payment)**	**Refinanced Loan 2 (bigger loan, same payment)**	**Refinanced Loan 3 (larger loan, same finance charge as original loan, higher total payments)**	**Refinanced Loan 4 (same original loan, same finance charge remaining, more total payments)**
Loan	$500	$374.03	$500	$750	$750	$500
APR	398%	398%	225%	296%	145%	172%
# biweekly payments	13	7	39	26	26	13
Payment	$90.61	$90.61	$45.00	$90.61	$55.16	$58.48
Finance charge	$684.21	$260.24	$1,255.00	$1,605.86	$684.16	$260.24
Total payments	$1,184.21	$634.27	$1,755.00	$2,355.86	$1,434.16	$760.24

For example, the lender could provide a new $500 loan (which would give the borrower some cash back), reduce the rate from 398% to 225%, lower the payment from $90.61 to $45, but increase the term to 39 biweekly payments. Not only has the cost increased by nearly $1,000, but the consumer is put at considerable risk with the need to make payments for 18 months and the dangers of the leveraged payment mechanism. The lender could even put the consumer in a bigger loan as long as the APR goes down substantially.

Instead of focusing on a reduction in *rate*, we strongly urge the CFPB to limit this exception to refinanced loans that have lower *total payments* than the payments *remaining* on the original loan. It is important to remember that this exception is only triggered after circumstances that indicate inability to repay. The consumer is reborrowing within 30 days of a balloon payment, is delinquent, or has said she cannot afford to pay the loan, or there are other indications that the refinancing is driven by unaffordability. The total cost going forward is more relevant to the loan's unaffordability at that point than the interest rate alone.

If the total payments must be lower, and not just the rate, then the lender is less likely to stretch out the loan term; a shorter loan term is more likely to be sustainable for a struggling consumer. If the remaining term stays the same, then reducing the "total cost of credit" rate will also reduce the total dollar cost. For example, assume the original $500, 398% loan above, with the consumer refinancing after six payments. If the lender refinances the $374.03 balance by reducing the rate to 145% but with the same seven payments still remaining, the payment will drop from $90.61 to $65.91. Not only has the interest rate gone down, but the total dollar cost to repay the loan has dropped from $634.27 to $461.72.

The lender may also extend the term on the new loan, but only if the total dollar cost is lower. That rule will put some brakes on the tendency to lengthen the loan, and will force a more substantial reduction in payment size. For example, using the same original loan and same refinanced $374.03

(with no cash-out), the lender could reduce the payment to $45 but require 13 more payments instead of seven. The APR would be 185% and the total dollar payments would be $585, below the $634.27 currently due.

Refinancing into Loan with Lower Actual Total Cost			
	Remaining Balance after 6 payments	**Refinance 1: Same remaining term**	**Refinance 2: Longer term**
Loan	$374.03	$374.03	$374.03
APR	398%	145%	185%
# biweekly payments	7	7	13
Payment	$90.61	$65.96	$45.00
Finance charge	$260.24	$87.69	$210.97
Total payments	$634.27	$461.72	$585.00

Requiring total payments to be lower than the remaining payments on the first loan discourages high rates, big loans and long terms. It encourages lower rates, reducing debt, and shorter time in debt. It creates exactly the right incentives without being prescriptive about what the new loan looks like.

This approach also provides a simple, bright-line rule. Even $1 lower is sufficient; lenders do not have to guess whether the charges are "substantially" lower. Lenders have flexibility about how to design a refinanced loan, as long as they reduce the consumer's total costs and meet the general ability-to-repay requirements. These are the only circumstances under which there should be an exception from the presumption of inability to repay when consumers are struggling with an unaffordable loan.

11.6. Overcoming the Presumption of Unaffordability: § 1041.10(d)

11.6.1. In general.

Proposed § 1041.10(d) describes how a lender can overcome the presumption of unaffordability either under § 1041.10(b) for certain loans following balloon payment loans or under § 1041.10(d) when there is a longer-term loan outstanding with certain indicia of unaffordability. The provision requires the lender to have reliable evidence that the consumer will have sufficient improvement in financial capacity to support a reasonable determination that the consumer can afford to repay the new loan despite the unaffordability of the prior loan.

As an initial matter, we note that overcoming the presumption that the *new* loan is unaffordable does not change the fact that the *old* loan was unaffordable. The requirements of proposed § 1041.10(d) allow lenders to make a new loan "despite the unaffordability of the prior loan."

Consequently, it is critical that the original loans be flagged as unaffordable and reported to the CFPB or otherwise captured in data that the CFPB will review. Refinanced unaffordable loans will not show up in the default rates; they will be considered paid in full. Lenders with more than minimal rates of unaffordable loans should be held in violation of the ability-to-repay rules even if the new loans are permissible. Lenders should not be allowed to routinely make and refinance unaffordable loans even if the lender can overcome the presumption that the new loan is unaffordable. The borrower is being forced into the subsequent loan due to the unaffordability of the first loan, which is likely due to a failure of underwriting.

We appreciate the admonition in proposed comment 10(d)-1 that the presumption may be overcome only in "limited circumstances."[628] After a first unaffordable loan, it should truly be a rare exception that another high-cost loan with a leveraged payment mechanism or vehicle title security is permitted. To permit otherwise would allow an exception to swallow the rule and would encourage deficient ability-to-pay determinations at the outset.

As discussed below in section 11.7, we urge the CFPB to prohibit a second refinancing, and we oppose the Bureau's statement that the proposal permits multiple successive refinancings.[629] However, we appreciate the Bureau's statement that "certain patterns of reborrowing may indicate that the repeated determinations that the presumption of unaffordability was overcome were not consistent with proposed § 1041.10(d) and that the ability-to-repay determination for such loans were not reasonable under proposed § 1041.9."[630] We urge the CFPB to scrutinize any pattern of reborrowing strictly.

We support the CFPB's focus in § 1041.10(d) on "improvement in financial capacity." As explained in proposed comments 10(d)-1, -2 and -3, the focus is on a fundamental change in the consumer's overall capacity to repay a loan. That is, essentially the consumer has had an increase in residual income—either an increase in income or a decrease in major financial obligations.

However, the CFPB should define the phrase "improvement in financial capacity" and make clear that it means only an improvement in "net income" or "major financial obligations." The proposed comments and discussion consistently lead to that conclusion, but the rule should be clearer.

The first situation identified in the proposed Comments as representing an improvement in financial capacity is a temporary, unusual decline in income that is not reasonably expected to recur for the period of the new loan. Proposed Comment 10(d)-2 discusses a consumer who made the first six payments on a loan but then missed two payments because she was unable to work for two weeks. The lender could overcome the presumption of inability to repay because it reasonably determined that her residual income had returned to normal levels. The Comment notes that the income decline "is not reasonably expected to recur" for the term of the loan.

It is critical that the loss of income in this situation be an unusual event that is truly not expected to recur. Many consumers have erratic work schedules without regular hours, juggle multiple, irregular part-time jobs, and do not have a steady paycheck. For these consumers, a dip in income from time to time is to be expected, and this volatility should be accounted for in the original ability-to-pay assessment. The fact that the consumer is working full hours at the time of the new loan does not represent an overall improvement in financial capacity if volatility is reasonably foreseeable during the term of the new loan.

The second type of improved financial capacity identified in the proposed Comments is an "increase in net income." (Comment 10(d)-3.) The Comment does not give a specific example of this situation. But as with a dip in income, an increase in income must be a fundamental improvement in the consumer's

[628] "Section 1041.10(d) permits the lender to overcome the presumption in limited circumstances evidencing a projected improvement in the consumer's financial capacity …." Proposed Comment 10(d)-1.
[629] 81 Fed. Reg. at 48028
[630] *Id*.

income, not a temporary spike that make not be sustained. For example, if the consumer got a new job with more regular hours or a higher wage, that is an improvement in financial capacity. The fact that the consumer was able to work more hours for the past two weeks but does not have any assurance that the increase in hours will be permanent should not be sufficient to rebut the presumption.

The third type of improved financial capacity in the proposed Comments is a "decrease in major financial obligations." Proposed Comment 10(d)-3 gives the example of a consumer who moved to a new apartment and reduced her rent by more than $100. We support this example because it is a fundamental change in financial capacity leading to an increase in residual income. The fact that the consumer needed to buy back-to-school clothes last month, or has vowed to spend less on take-out food next month, would not be a decrease in major financial obligations.

We support the examples in the Comments, and we urge the CFPB to be more specific as to what the Bureau means by an "improvement in financial capacity." The CFPB nowhere explains that phrase. The three categories identified above—an unanticipated dip in income that has ended and will not recur; an increase in income; a decrease in rent—all involve an improvement in net income or in major financial obligations, but this can be discerned only by parsing the examples.

Thus, the CFPB should define "improvement in financial capacity" as only an improvement in "net income" as defined by § 1041.9(a)(4) or in "major financial obligations" as defined by § 1041.9(a)(2). This definition is consistent with the examples in the Comments and with the CFPB's discussion.[631] It is also consistent with proposed Comment 10(d)-4, which explains that the lender must have reliable evidence "regarding the consumer's net income and major financial obligations sufficient to make the comparison required."

As discussed in the next section, the CFPB appropriately chose to propose § 1041.10(d) "without permitting an unusual, non-recurring expense to satisfy the conditions of the test."[632] However, the distinction between unusual expenses and major debt obligation is not in either the rule or the Comments. Specifying that only net improvements in income and major financial obligations qualify would enhance compliance and prevent evasions.

[631] "The presumption can be overcome …. The Bureau recognizes, for example, that there may be situations in which the prior loan would have been affordable but for some *unforeseen disruption in income or unforeseen increase in major financial obligations* that occurred during the prior expense cycle and is not reasonably expected to recur during the underwriting period under § 1041.9 for the new loan. The Bureau also recognizes that there may be circumstances, albeit less common, in which even though the prior loan proved to be unaffordable, a new loan would be affordable because of *a reasonably projected increase in net income or decrease in major financial obligations*." 81 Fed. Reg. at 47958 (emphasis added). *See also id.* at 47966 (the presumption of unaffordability may be overcome "only in a *narrow* set of circumstances that are reflected in *certain aspects* of a consumer's financial capacity and can be verified through reliable evidence") (emphasis added).

[632] 81 Fed. Reg. at 48029.

11.6.2. Unusual expenses should not be a third way to overcome the presumption of unaffordability.

The Bureau asks whether unusual expenses should qualify as a third circumstance in which lenders could overcome the presumptions of unaffordability.[633] We agree with the CFPB's decision not to permit "unusual" expenses to be used to rebut the presumption of unaffordability.[634]

This exception would completely swallow the rule. The life of every consumer is filled with erratic expenses that do not recur month to month. Car repairs, appliance break-downs, energy bill spikes and many other unpredictable or unplanned expenses happen all the time. Moreover, as the CFPB observes, "the fact that a consumer may cite a particular expense shock when seeking to reborrow does not necessarily mean that a recent prior loan was affordable."[635] An exception for unusual expenses would eviscerate the obligation to account for expense volatility.

The CFPB has asked how to address unexpected and non-recurring increases in expenses, such as major vehicle repairs or emergency appliance replacements.

First, these "unexpected" expenses are the excuse given for permitting high-cost loans in the first place. As the Bureau finds, consumers who borrow to meet basic living expenses appear more likely to end up in long sequences of reborrowing. So if a consumer is borrowing for that purpose, it would be unreasonable to find that she has ability to repay. Permitting lenders to refinance a borrower before the first loan is paid off due to a second "unexpected" expense just blesses a cycle of debt and reborrowing.

Second, the rules should encourage shorter (3- to 6-month) loans that are not refinanced and do not trap consumers in a cycle of debt. If loans are shorter and consumers are able to successfully repay them without borrowing or being in perpetual debt, then consumers are more likely to be debt-free and able to take out a new loan when a new expense arises.

Finally, if an unexpected expense is the reason the consumer is delinquent on the first loan, nothing prevents the first lender from working with the borrower to get back on track. A work-out does not have to involve a second loan.

11.6.3. Time period for assessing improved financial capacity.

The CFPB asks what is the appropriate time period for comparison of the consumer's financial capacity between the prior and prospective loans. The proposed rule would require the lender to compare the consumer's financial capacity "since obtaining the prior loan" to her capacity during the time period that the lender is required to assess for the new loan. We support this requirement together with our recommendation in section 10.4.2 above that, for any longer-term loan, the lender be required to do a "lookback" at the consumer's income and expense volatility for a period at least as long as the loan term.

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[633] 81 Fed. Reg. at 48029.

[634] Per the proposal, only an "unforeseen increase in major financial obligations" would qualify. We note that this would seem to be a rare occurrence. For example, if the consumer's rent was suddenly increased by $200, but the consumer then moved to another apartment to bring the rent back to the original level, that would qualify.

[635] 81 Fed. Reg. at 47980.

Of course, to rebut the presumption, the rule appropriately requires that the lender have verification that *income* or *major financial obligations* have sufficiently improved since obtaining the prior loan, regardless of what has occurred with basic living expenses. If expenses beyond what was projected for the term of the unaffordable loan have contributed to its unaffordability, the lender's new projection of basic living expenses must take that into account. And any improvement in income and major financial obligations must be sufficient to offset any necessary increase in the projection of basic living expenses.

11.6.4. Reliable evidence.

Proposed § 1041.10(d) allows a lender to overcome the presumption of unaffordability only if it "reasonably determines, based on reliable evidence" that there has been a substantial improvement in the consumer's financial capacity. Proposed Comment 10(d)-4 explains that reliable evidence "consists of verification evidence regarding the consumer's net income and major financial obligations sufficient to make the comparison required." The Comment gives bank statements reflecting direct deposits as an example of reliable evidence that permit the lender to determine the change in the borrower's income. The Comment also states that the borrower's self-certification is not reliable evidence.

We support the requirements that the determination of improved financial capacity be both reasonable and based on verification evidence. There is a track record of evasions in this market and concrete evidence should be required to support claims of improved financial capacity. Insisting on clear evidence is especially important when a lender has already made one unaffordable loan. The verification evidence must be independent, third-party documentation that cannot be manipulated and clearly shows the improvement in financial capacity.

The verification evidence generally should be of the same type and quality that is required to document the consumer's ability to repay in the first place. However, proxies should not be permitted, even in areas where they are in the original determination. For example, if the changed component of the consumer's situation is rent that was originally "verified" using a proxy, then that proxy should not be permitted to be used as reliable evidence in a new ability-to-pay determination. Actual documentation of the rent before and after should be required as documentation of a reduction in the borrower's rent; the lender should not be allowed to compare the previous "proxy" rent to the current actual rent. (See section 6.4.4.3.2 for related discussion.)

11.7. Repeat Refinancings and Refinancings That Significantly Extend the Initial Term of the Loan.

The CFPB has requested comment on whether a pattern of refinancing that significantly extends the initial term of the loan warrants application of a presumption of unaffordability and, if so, at what point that presumption would be warranted.[636] For the reasons discussed in sections 11.4.1.3 and 11.4.1.5 above, extending loan terms—either by moving consumers into loans with longer terms, or by strings of refinancings—is strong evidence that the borrower lacks ability to repay and should thus carry presumptions of unaffordability.

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[636] 81 Fed. Reg. at 48026.

First, the CFPB should prohibit a second refinancing or impose a very high presumption that a second refinancing shows inability to repay without reborrowing. As discussed in section 11.7 above, it is especially critical to prohibit a second refinancing after a second loan has triggered the presumption of inability to repay. But this ban or presumption should apply any time a loan is refinanced for a second time, regardless whether there was a presumption for the first refinancing or not.

In the absence of a presumption that applies whenever there is early refinancing, strict limits on repeat refinancing are essential to prevent consumers from being trapped in a long-term cycle of debt with repayment coerced through a leveraged payment mechanism. Even the first refinancing raises serious concerns, for all of the reasons discussed previously. With a second refinancing, there is even a greater likelihood that the lender has been able to game the system—either avoiding a presumption in the first place or rebutting it under the rules. Loans are likely refinanced either to deal with difficulty making the original payments or to deal with a new expense that the consumer cannot afford without reborrowing. If the CFPB wants its ability-to-pay requirements to have meat, especially the rules about income and expense volatility over the term of the loan, it simply cannot let lenders continue to claim that repeated refinancing is not a strong sign of inability to repay.

Second, beyond prohibiting a second refinancing, several of our proposals above will prevent or lessen the chance of refinancings that significantly extend the initial term of the loan. These proposals include:

- Make clear that the ability-to-repay standard means ability to repay without reborrowing. (See section 5.3.)
- Require a more meaningful income and expense volatility cushion, particularly for loans longer than six months (see section 10.4).
- Require lenders that have significant refinancing rates to consider income and expense volatility over the entire anticipated loan sequence, not just a single loan. (See section 10.4.2.)
- View high portfolio-wide refinancing rates as evidence of unreasonable ability-to-repay determinations (see section 11.11).
- Eliminate the exceptions for new loans with smaller payments and lower "total cost of credit" (i.e., the enhanced APR) unless the total dollar payments on the new loan are less than those remaining on the prior loan (See sections 11.3.2 and 11.5.)
- Require a consumer to have made substantial progress repaying the loan (i.e., 75% of principal), rather than to have taken more than a certain amount of cash-out, in order to avoid a presumption of inability to repay. (See section 11.4.8.)
- Do not add a third method of overcoming the presumption of unaffordability based on unusual expenses. (See section 11.6.2.)

Third, if the CFPB does not prohibit second refinancings, it should impose a presumption of unaffordability on any string of refinancings that increases the time in debt from the outset of the original loan by more than 50%. When borrowers take out covered loans, they have an expectation of how long they will be in debt. Once the consumer is stuck in an unaffordable loan, the lender will exploit their desperation for a cash-out refinancing, even if it significantly extends their time in debt. Imposing an outer limit will help prevent refinancing abuses. The only exception should be for a refinance that happens after 75% of the loan has been repaid or after the second to last payment, whichever is later. In that case, the end is in sight, and a refinance is closer to simply taking out a second loan after the first one has been paid off.

11.8. Prohibit a § 1041.9 Loan within 60 days of a Short-Term Exemption Loan: § 1041.10(e)

Proposed § 1041.10(e) prohibits a covered longer-term loan under § 1041.9 for 30 days following a short-term exemption loan made by the same lender or affiliate under § 1041.7. In other words, there are no exceptions or circumstances that allow a lender to rebut the presumption of inability to repay during and for 30 days following a short-term loan that was not underwritten in accordance with the ability-to-repay requirements.

We strongly support a prohibition in this situation. As discussed earlier in these comments, we oppose § 1041.7 in its entirety; no loans should be made without determining ability to repay. We also oppose allowing three non-underwritten short-term loans in succession. But if the CFPB is going to allow those loans, lenders certainly should not be allowed to entrap a consumer without assessing ability-to-repay and then switch the consumer to a longer installment loan. We agree that there should be absolutely no exceptions for covered long-term loans made in close proximity to short-term exemption loans.

However, we strongly urge the CFPB to extend the cooling-off period to 60 days. As discussed in section 8.3.1, 60 days is a more appropriate period to ensure that the borrowing is not driven by the unaffordability of the balloon payment. As discussed in section 11.6.3, a longer period is especially important when the balloon is followed by a longer-term loan, because there are fewer limits on extended debt traps for longer-term loans and more potential for bait-and-switch. And those reasons are even more compelling when a longer-term loan follows a short-term exemption loan under § 1041.7 that has no affordability requirement.

Indeed, the idea that the impact of a balloon payment—the affordability of which was never assessed—on a distressed borrower's finances has disappeared after 30 days is not tenable. There is little or nothing in the Bureau's proposed ability-to-repay requirements that would capture the unaffordability of the prior loan or prevent these bait-and-switch tactics. The ability-to-repay rules for a longer-term loan focus on the affordability of the new loan payment in light of income, future debt obligations, and future basic expenses. Even if the consumer is driven to seek a new loan to cover the unaffordability of the prior loan, nothing in the required analysis captures that fact:

- The lender need not analyze what happened in the previous 30 days (though we have urged that it should).
- While the lender must obtain a credit report—and we have urged the Bureau to make clear that delinquencies on the credit report must be considered (see section 6.3.5)—difficulty in the last 30 days will not show up in a credit report.
- Even the indicia of unaffordability in § 1041.10(c) will not matter because there will be no prior loan outstanding 31 days later and none of those indicia (i.e., recent delinquent payments) are incorporated into the basic ability-to-repay requirements.

Thus, even if the new borrowing is clearly driven by the unaffordability of a short-term balloon loan 31 days ago, the lender has no burden to show an improvement in the borrower's financial circumstances sufficient to afford the new loan.

It is highly likely that payday lenders will use unaffordable short-term exemption loans as a gateway to longer-term debt traps. Indeed, a very large market share of payday loans comes from states where both high-cost short-term and high-cost longer-term loans are currently permitted—including California, Mississippi, Missouri, Ohio, and Texas. If the 30-day cooling off period proves insufficient to allow the consumer's refinances to recover, which data suggest we should expect (see 8.3.1 above), then a bait-and-switch will be far too easy. Preserving this role for short-term exemption loans will also undermine the efforts of non-payday states to keep those loans out of their states, as discussed in section 9.6 above. For these reasons, we strongly urge the Bureau to impose a 60-day cooling off period between a § 1041.7 loan and a longer-term loan.

11.9. Prohibit § 1041.11 and § 1041.12 loans within 60 days of a § 1041.7 loan by the same lender: § 1041.10(e) and Comment 10(e)-1.

Proposed Comment 10(e)-1 explains that the requirement of a cooling-off period after a short-term exemption loan does not apply when the new loan is a lower cost longer-term exemption loan made under proposed § 1041.11 or § 1041.12. We agree that lenders making loans under § 1041.11 or § 1041.12 should be allowed to refinance unaffordable short-term payday loans made by *other* lenders.

However, we urge the CFPB to apply the cooling-off period to longer-term exemption loans under § 1041.11 or § 1041.12 from the same lender/service provider or affiliate. The lender that made the unaffordable balloon payment loan without an ability-to-repay determination should not be allowed to make another covered loan within the cooling-off period, even if it is a lower-cost longer-term exemption loan. Those loans are also exempt from ability-to-repay requirements and may be unaffordable. The fees could also be substantial, resulting in high APRs. For example, a 60-day, $300 loan with a $50 fee, 36% interest and two monthly payments of $182.91 has an APR of 171.7%. That is likely unaffordable for many borrowers.

If a lender that made a short-term payday loan without underwriting wants to help the consumer refinance into a more affordable loan, it can make a non-covered loan under 36% (or even, unfortunately, a high-rate loan without a repayment device). But the lender that made the unaffordable loan should not have *any* exceptions to a 60-day waiting period for covered loans.

Thus, proposed § 1041.10(e) should be revised to read "a lender must not make a covered longer-term loan under §§ 1041.9, <u>1041.11 or 1041.12</u> during the time period . . . ." The proposed Comment should be revised to clarify that only a new lender that did not get the consumer stuck in the unaffordable loan can make the longer-term exemption loans.

We also note this recommendation at 12.3 and 12.4 in our discussion of longer-term exemption loans.

11.10. Prohibit any non-covered loan from being used as a bridge loan: § 1041.10(f).

Proposed § 1041.10(f) prevents a lender from using a "non-covered bridge loan" to avoid the 30-day cooling off period after a short-term loan or a longer-term balloon-payment loan. A "non-covered bridge loan" is defined in proposed § 1041.2(a)(13) as a non-recourse pawn loan made during the 30-day period if the loan is substantially repayable within 90 days. Section 1041.10(f) essentially prohibits these loans from being used as bridge loans between two covered loans that could otherwise not be made back to back without a 30-day gap. As proposed, the time during which the bridge loan is outstanding does not count towards the 30 days.

Thus, if a consumer takes out a pawn loan 5 days after a short-term loan and redeems the pawned item after 14 days, those 14 days do not count towards the 30-day cooling off period. There must be an additional 25 days before the next covered loan in order to avoid the limitations during the 30-day period.

We support rules to prevent pawn loans from being used as bridge loans. However, we urge the CFPB:

- To prohibit use of any non-covered loan as a bridge loan; and
- To require a full 30 (or 60, as we propose) *consecutive* days without borrowing, unless 90 days have elapsed between covered loans and 30 consecutive days have elapsed since the last balloon payment loan (covered or not).

The purpose of the presumption period is to make sure that the new loan is not provoked by the unaffordability of a short-term loan or longer-term balloon-payment loan. That purpose would be defeated if lenders could use pawn loans during that period. Some payday lenders are also pawnbrokers, and it would be quite easy for them to make a pawn loan. Moreover, as discussed in section 4.7.2, we already have fears that lenders will claim that loans are a pawn to avoid coverage. While there may be reasons to exempt pawn loans from this rulemaking, that exemption should not be exploited during the period when lending would otherwise be prohibited or restricted to evade the protections of the rule.

For the same reasons, however, we believe that a covered lender should not be allowed to use any type of non-covered loan as a bridge loan. Even without a leveraged payment mechanism, lenders can use aggressive debt collection tactics, security interests in cell phones or other household goods, or other methods to coerce repayment of unaffordable loans. If these loans only need to last the waiting period in between other covered loans, a wide variety of non-covered loans could be used to evade the purpose of a presumption period.

Even if the interest rate on the bridge loan is 36% or less, covered lenders should not be allowed to use non-covered loans as a bridge to defeat the protections for balloon payment loans. Especially if the bridge loan is a short-term balloon-payment loan or otherwise has large payments, repayment of the principal alone can be a challenge, and a low interest rate does not necessarily make it affordable. And lenders may be very willing to forgo any significant interest for a short period of time so that they can keep the borrower trapped in a cycle of debt and linked up with a new covered loan. Thus, new covered longer-term loans should be covered by the presumption of § 1041.10(b) or the prohibition of § 1041.10(e) until the consumer has survived 30 days without *any borrowing from that lender* since the prior covered short-term loan or longer-term balloon-payment loan.

In addition, we urge the CFPB to require the 30 days to be consecutive. That is, a bridge loan should not simply toll the counting of the 30 days; it should reset the clock so that another 30 days without borrowing is required in order to avoid the rules of §§ 1041.10(b or (e).

A tolling rule does not sufficiently protect borrowers from the impact of unaffordable balloon payment loans. For example, assume that the lender makes the borrower another loan 15 days after the third consecutive short-term exemption loan. The lender offers a 30-day balloon payment loan at 300% APR but with no post-dated check requirement. After aggressive debt collection calls, the consumer repays that loan. A tolling rule would permit a new covered loan 15 days later without any presumption or ban, notwithstanding the fact only 15 days have elapsed since the last balloon payment. Instead, another 30 days should be required.

In addition, a tolling rule is confusing. It requires the lender to keep track of how many days elapsed before the non-covered loan and calculate how many days after the non-covered loan before a new covered loan may be made without consequences. It is simpler and will enhance compliance and enforcement to have a clear rule that 30 consecutive days without borrowing must elapse before a second covered loan (unless any of the exceptions apply).

The only exception to a 30 consecutive day rule should be when the period between the two covered loans becomes so long that it is reasonable to view the new loan not as a bridge loan but as an independent loan not covered by this rule. In addition, the bridge loan must not be designed to compel reborrowing. Thus, 30 consecutive days without reborrowing should be required between covered loans to avoid §§ 1041.10(b) and (e) unless:

- a full 90 days have elapsed between covered loans, AND
- the bridge loan is not a balloon payment loan.

These limitations are necessary to ensure that a covered lender is not using gaps in the rule to evade the protections of the rule and to use unaffordable loans to keep the consumer in a cycle of debt.

11.11. Limit Portfolios With High Rates of Reborrowing Even if Individual Refinances Are Permitted.

All the rules in proposed § 1041.10 are aimed at individual loans and individual consumers. They set out limitations, procedures and prohibitions that govern whether and how lenders may refinance a particular consumer from one covered loan into another one.

But just because the rules do not impose absolute prohibitions on refinancing in certain situations, that does not mean that those refinancings are not problematic. The CFPB is trying to walk a delicate line between giving consumers and lenders the flexibility to refinance in situations where there are fewer concerns about inability to repay without opening up loopholes that permit unaffordable lending. The rules cannot draw that line perfectly for all situations. Even if the CFPB adopts all of our suggestions—and especially if it does not—there will refinancings that are permitted under the rules but that nonetheless mask a consumer who was unable to repay a loan without reborrowing.

In fact, proposed § 1041.10 is not even designed to prohibit new loans that are driven by a need to reborrow following an unaffordable loan. Several of the provisions permit reborrowing “despite” the unaffordability of the first loan. The rule is designed primarily to ensure that the second loan is affordable, not to prohibit refinancing of unaffordable loans. Thus, the refinancing still may reflect poorly on the first loan.

For these reasons, it is critical for the CFPB to watch portfolio-wide reborrowing rates carefully and to take steps if those rates are high even if each individual case is arguably permitted under the rule. As discussed above, refinancing before the first loan is repaid in full—or shortly after a balloon-payment loan—is a strong sign of inability to repay without reborrowing. The exceptions and presumption rebuttal rules should be occasional exceptions, not routine excuses for lenders to make unaffordable loans and then refinance them. Refinancing is also problematic even if none of the indicia in § 1041.10 are present and the exceptions and rebuttals are not triggered at all. Overdraft fees and other struggles paying other expenses will not be captured in § 1041.10.

The goal of this rule is to stop lenders from getting consumers stuck in a cycle of debt. The best proof of success will be consumers who take out loans, repay them successfully, and then feel no immediate need to reborrow. Consequently, it is critical to scrutinize refinancing rates carefully as part of considering whether lenders are making reasonable ability-to-repay determinations, as discussed more fully in sections 11.4.1 above.

12. EXEMPTION FROM ABILITY-TO-REPAY FOR LONGER-TERM LOANS IS VULNERABLE TO EXPLOITATION: § 1041.11 and § 1041.12.

Sections 1041.11 and 1041.12 provide exemptions from the ability-to-repay determination requirements for longer-term loans. Section 1041.11 provides an exemption tracking the National Credit Union Administration's Payday Alternative Loans (PAL) program for loans not exceeding annual interest of 28% and a $20 application fee, up to six times annually (the PAL exemption). Section 1041.12 exempts loans with an APR of 36% or less, fee-inclusive with the exception of an origination fee that can be $50 or a reasonable portion of the lender's origination costs, made up to four times annually per lender, so long as the portfolio-wide default rate does not exceed 5% (the Section 12 exemption).

As proposed, the longer-term exemption loans pose risk of inflicting substantial harm for three primary reasons.

First, any exemption from an ability-to-repay requirement is inconsistent with and undermines the central principle underlying the rule. That principle matters not only for this rule, but for the significance of the ability-to-repay principle in every credit-related context, in every regulatory sphere, going forward. Importantly, these exemptions were designed with the intent of excluding products currently issued by credit unions and community banks that have not been a cause for great concern of consumer harm. But they will be available to all lenders and vulnerable to exploitation. The Bureau should apply the ability-to-repay principle to every covered loan.

Second, any exemption must not sanction unreasonably high origination fees, lest the risk of substantial harm is too great. The $50 fee sanctioned on each loan in the default-based exemption, permitted four times annually, regardless how small the loan is or how short the term. The fee is too high and is not adequately supported by the data the Bureau presents. Moreover, this fee has no clear upper bound, which could result in very costly loans, particularly small ones. The precedent of the CFPB endorsing such a high fee origination fee on a small dollar loan will undermine states' efforts to maintain the integrity of their interest rate caps. In addition, a high upfront fee encourages lenders to flip borrowers from one early refinance to another, adding to the risk of the substantial harm. If this exemption is retained, the rule should limit the fee to 10% of the credit extended up to a maximum of $30, charged once per year. To discourage loan flipping, it should also require a pro rata refund of origination fees for early refinancings.

Third, the rule must be carefully designed to ensure that lenders do not use longer-term exemption loans as bridge loans to evade the provisions aimed at preventing flipping for both short- and longer-term loans. As designed, the rule does not prevent lenders from putting borrowers directly into exemption loans following an unaffordable balloon loan or any longer-term loan repaid early. This has the effect of (1) masking the unaffordability of the prior loan by tiding the borrower over until the lender can put the borrower back into a non-exempted covered loan; (2) assisting lenders to continue making unaffordable balloon loans without the restrictions of this rule, and (3) ultimately permitting the lender to keep the borrower in unaffordable debt indefinitely, without ever triggering a presumption of inability to repay. Thus, the rule should prohibit lenders from using longer-term exemption loans as bridge loans.

We discuss these three issues in more detail below. At sections 12.5-12.7, we comment on additional details of the proposed exemptions. Among other recommendations in those sections, we urge that vehicle title loans not be eligible for these exemptions.

Finally, we support the Bureau's decision not to include the exemption based solely on a 5% payment-to-income ratio included in the preliminary SBREFA outline. There is little reason to presume that a $100 monthly loan payment will be affordable for a typical, already financially distressed borrower earning $24,000 per year. Indeed, the Bureau's more recent data found that default rates on high-cost installment loans, even at payment-to-income ratios not exceeding 5%, reached 28-40%. However, as discussed above, we do believe that payment size matters, and we urge the Bureau to scrutinize loans with large payment-to-income ratios.

12.1. The Ability-to-Repay Principle Should Apply to Every Loan.

The ability-to-repay principle is the cornerstone of this rule and one of responsible lending, generally. See 5.1 above. Any exemptions risk undermining that principle—one that is particularly important in a market aimed at lower-income, financially distressed borrowers.

12.2. Any Exemption Should Not Sanction High Origination Fees.

The Section 12 exemption sanctions far too high an origination fee, four times per year (per lender), and encourages loan flipping.

The Bureau explains the origination cost framework as intended to accommodate existing practices at community banks while providing lenders with certainty about permissible costs to facilitate lending. But in designing an exemption for one particular market that is available to all lenders, the Bureau sanctions too high a fee on every loan in light of existing practices. The approach leaves considerable uncertainty about how high the origination fee can reasonably be. The Bureau does solicit more feedback on origination fees on accommodation loans and the costs reflected in those fees, "including, among others, labor costs, document preparation costs, and any costs of using the applicable underwriting methodology."[637]

The safe harbor amount of $50 is very high, particularly if charged four times annually (per lender) as permitted. In explaining its determination of $50, the Bureau notes that in a community bank survey, $50 was the median fee for loans under $1,000 when the fee was set as a fixed dollar amount. Several factors strongly suggest this amount is far too high for a safe harbor available to all lenders:

- Though the survey did not report average loan terms, it seem unlikely that these accommodation loans typically have terms as short as 90 days. Yet the exemption would permit the fee four times annually, per lender.

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[637] 81 Fed. Reg. at 48044.

- Even based on the fees reported in the survey alone, $50 is a high fee:
    - When set as a percentage rather than a dollar amount, the average fee was 3%, which translates to $30 on a $1,000 loan, the highest loan in the range. On a $500 loan, that fee would be $15.
    - One-third of the banks charged no loan fee on loans less than $1,000 in addition to the rate.

- The average "typical interest rate" was only 12.1% for loans less than $1,000—one-third the amount permitted under the exemption—and the "average maximum rate" was only 16.7%. Thus, it seems unlikely that many banks charged both 36% interest and a full $50 fee. But certainly other lenders will charge the maximum.

- The loans in the survey were significantly underwritten—78% verified income and 93% verified major financial obligations. We cannot count on other lenders to do the same.

- This survey was for accommodation loans, made relatively infrequently, for which lenders may not have highly automated origination systems. Yet this fee would become the safe harbor even for lenders who want to bring this loan product to scale and fully automate it, thus, presumably, being able to originate the loan at a much lower cost.

The practices of community banks and other banks making accommodation loans may not be particularly concerning. But other lenders may exploit the exemption to charge four $50 fees on small loans annually, including quickly flipping borrowers from loan to the next to generate the next fee.[638] State legislatures also may be persuaded by this precedent to permit fee-snowballing that results in high-cost loans. Sanctioning a *minimum* origination fee of $50 on loans with no minimum loan size will make it harder to oppose industry proposals to layer fees on top of deceptively low interest rate caps.[639]

The lack of a maximum fee poses even greater risk of harm. While proposed § 1041.12(b)(5)(i) requires the fee to be a "reasonable proportion of the lender's cost of underwriting loans," that provides little limitation. Proposed Comment 12(b)(5)(i)-1 does not provide additional clarity.

The CFPB's discussion of this provision implies that the standard would be similar to the Regulation Z requirements for an application fee to be excluded from the APR.[640] But that is little comfort. Kinecta Federal Credit Union, for example, has used the Regulation Z loophole to evade its federal usury cap and charge a $37.50 application fee on top of 15% interest to make two-week payday loans that have a

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[638] For example: $100, 2-month loan with a $50 origination fee would have an APR including the fee of $432%; a $300, 3-month loan an APR of 137%. Of course if the fee increases to $75 or $100, the effective APR does as well. Yet no ability-to-repay determination would be required.

[639] *See, e.g.,* Tenn. Code Ann. § 45-12-111 (2016) (allowing 24% interest per annum plus a "customary fee" limited to 0.7% of the average daily principal balance"); H.B. 520, 2016 Reg. Sess. (Ky. 2016) (allowing 24% interest per annum plus an unlimited "customary fee").

[640] The Bureau mentions these fees—among others, labor costs, document preparation costs, and any costs of using the applicable underwriting methodology—which would be application fees under Regulation Z if charged to every applicant.

true annual rate in the triple digits.[641] In addition, the standard will be remarkably difficult to enforce. It is difficult for the outside observer to know whether a high fee is related to underwriting costs or not. And the rule is not clear as to what a "reasonable portion" of those costs is.

Instead, if the CPFB retains this exemption, we urge it to:

- Limit the fee to 10% of the credit extended up to a maximum of $30.[642] Thus, a $200 loan could have a fee of only $20, while larger loans could have a higher fee; and
- permit only one fee per year.[643]

If the Bureau continues to permit multiple fees per year, require that the fee be refunded on a pro rata basis if a loan is refinanced; otherwise, the incentive to flip borrowers is too great. The Bureau has clear authority to provide for pro rata fee refundability using its broad exemption authority.

12.3. Lenders Must Be Prohibited from Using Longer-Term Exemption Loans as Bridge Loans.

As designed, the rule does not prevent lenders from putting borrowers directly into longer-term exemption loans during or soon following an unaffordable balloon loan from the same lender, or any longer-term loan repaid early from the same lender. This has the effect of (1) masking the unaffordability of the prior loan by tiding the borrower over until the lender can put the borrower back into a non-exempted covered loan; and (2) ultimately permitting the lender to keep the borrower in unaffordable debt indefinitely, without even triggering a presumption of inability to repay.

We note that the SBREFA outline would have prohibited lenders from making longer-term exemption loans if the borrower had another covered loan outstanding from any lender. We do not oppose permitting an exemption loan from a different lender with a covered loan outstanding or shortly thereafter. We agree that lenders making loans under § 1041.11 or § 1041.12 should be allowed to refinance unaffordable short-term payday loans made by *other* lenders. But we do urge the following, all of which are discussed in more detail in section 11 of our comments addressing refinancings of longer-term loans:

- A presumption of unaffordability on a longer-term exemption loan:
  - when a *non-exempt covered short-term* loan *from the same lender* is outstanding and for 60 days thereafter.
  - When a lender refinances *its own non-exempt longer-term covered loan* and indicia of unaffordability are present.
  - when a lender refinances *its own Section 12* loan into another longer-term exemption loan and indicia of unaffordability are present.

  A prohibition on a longer-term exemption loan within 60 days of a *short-term exemption loan* from the same lender.

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[641] http://nixlending.com/en/personal-loans/detail/payday-cash-advance; Here is example for long-term loan as well: http://nixlending.com/en/personal-loans/detail/payday-payoff-loan, 18% APR + $49.95 Application fee

[642] The Durbin/Cartwright bills would limit the cost of closed-end credit to a fee-inclusive 36% APR with the exclusion of a $30 application fee charged one time per year. Oregon's fee limit is $10 per $100 up to a maximum of $30; that fee cannot be charged on the two subsequent renewals. 54 Or. Rev. Stat. § 725A.064.

[643] MLA regulations exempt only one PAL fee a year from the MAPR.

12.4. The Combined Use of Exemptions, as Permitted by the Proposal, Poses Undue Risk of Substantial Harm.

Because the short- and longer-term exemptions as proposed would operate in three distinct silos, the proposal would permit a lender to keep a borrower in substantial debt the entire year, paying substantial fees, without ever determining their ability to repay.

Consider the following relatively conservative scenario that could occur over a twelve-month period:

Short-term exemption loans:	six *14-day loans of $500 each, at $15 per $100*
NCUA exemption loans:	*six 60-day loans of $500 each, 28% APR plus a $20 fee*
Default-based exemption loans:	*four 90-day loans of $1,000 each, 36% APR plus a $50 fee.*

In this scenario—with the lowest likely fees on the short-term and default-based exemption and with the borrower receiving longer-term exemption loans from only one lender—a borrower would pay a total of *$1,118 in fees and interest over a 12-month period, with no ability-to-repay determination*.

This example underscores the risk of harm that exemption loans pose to consumers, particularly in the short-term space; when high origination fees are permitted in the longer-term space; and when there are no restrictions on making exemption loans when other types of exemption loans shortly following or during other exemption loans from the same lender.

12.5. Additional Comments on the PAL Exemption: §1041.11.

(For discussion of additional issues common to both proposed exemptions, see section 12.7 below.)

The Bureau proposes this exemption for loans that share certain features of the NCUA's existing payday loan alternative (PAL) program. It notes its objective is to facilitate access. The Bureau notes the purpose of the exemption is to allow those credit unions making PAL loans to continue to do so, as well permitting other lenders, including banks and non-depositories, to make similar loans as well.

As the Bureau reports, nearly 20% of federal credit unions made PAL loans during 2015.[644] The average loan size is about $678 with an annualized net charge-off rate as a percentage of balances outstanding of 7.5%.[645] The Bureau notes that it believes PALs average 100-day loan terms with an all-in APR of about 43%.[646]

We support the Bureau's decision not to make the exemption more permissive than it has despite being urged to so by non-depository SERs. We also appreciate the Bureau's emphasizing that these loans may only be made where they are otherwise permitted by State law.

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[644] 81 Fed. Reg. at 47982.
[645] *Id* (citing 2014 data).
[646] 81 Fed. Reg. at 47892.

12.5.1. Availability for vehicle title loans.

The proposed exemption, unlike the short-term exemption, would be available for vehicle title loans; we oppose this approach. The Bureau does not note, and we are not aware of, federal credit unions currently making PAL program loans—at the higher cost permitted by the PAL program—secured by vehicle titles. Thus, it is not at all clear that a significant justification the Bureau offers for the NCUA-based exemption—to permit PAL programs to continue as usual—applies with respect to vehicle title loans. In addition, we note a concern the Bureau raises in the context of excluding vehicle title loans from the short-term exemption: that because vehicle values typically far surpass loan amounts, lenders may have incentive to make unaffordable loans and profit from repossession of the vehicle.

12.5.2. Loan term conditions: § 1041.11(b).

The exemption would limit the loan term to six months, the principal amount to $200-$1,000, and total cost of credit to not more than the cost permissible for Federal credit unions to charge under the NCUA PAL regulations. We see no reason to loosen these restrictions as laid out by NCUA. With respect to the six-month loan term, we reinforce NCUA's concern, as the Bureau does, that loans longer than six months may have unintended negative consequences. On loan size, we agree that larger loans when accompanied a leveraged payment mechanism may present more risks to consumers.

We emphasize, as the Bureau does, that Regulation Z limits application fees to the recovery of costs associated with processing applications for credit that are charged to all consumers who apply. **This suggests that the fee should not always be the maximum of $20, and that this fee should decrease over the course of making the loans to the same customer.**

12.5.3. Borrowing history condition: § 1041.11(c).

The exemption would limit loans on a per lender/affiliate basis to no more than three per lender/affiliate within 180 days. We support these limits but emphasize, as discussed in 3.4.2 above, that **they should include loans made by the same service provider or their affiliates as well.**

We urge further restrictions based on borrowing history related to other covered loans made by the same lender/service provider; see 12.3 above.

12.5.4. Income documentation condition: § 1041.11(d).

The exemption would require that lenders maintain and comply with policies and procedures for documenting proof of recurring income. It would permit any procedure that satisfies the lender's own underwriting obligations. The Bureau notes that this requirement has been relaxed since the SBREFA outline, which would have required "verifying" income, mirroring the PAL program guidelines. **We recommend underwriting requirements that track the PAL regulations.**[647]

[647] 12 CFR 701.12(2).

12.6. Additional Comments on Section 12 Exemption: §1041.12.

(For discussion of additional issues common to both proposed exemptions, see section 12.7 below.)

Proposed § 1041.12 would exempt from the ability-to-repay and disclosure requirements (but not from the failed payments rules) loans that meet the following conditions:

- Not structured as open-end credit;
- Term of no more than 24 months;
- Repayable in two or more substantially equal payments due at equal intervals no more frequently than monthly;
- Smoothly amortizing with payments allocated by applying a periodic interest rate;
- The total cost of credit is no more than a 36% annual rate except for a single origination fee;
- The origination fee may be the higher of $50 or a reasonable proportion of the lender's costs of underwriting the loans; and
- The 12-month portfolio default rate must not exceed 5%.

The Bureau proposes this exemption for loans that it describes as sharing certain features of loans made through community bank and other depository accommodation lending programs. Again, the Bureau notes the objective of facilitating access. As noted in sections 12.2 and 12.3 above, our key concerns relate to the high origination fee, the related incentive to flip loans, and the use of the exemption as a bridge loan. We address additional issues below.

12.6.1. Availability for vehicle title loans.

The proposed exemption, unlike the short-term exemption, would be available for vehicle title loans. We understand that some banks and credit unions make auto refinance loans and that this exemption may accommodate some of them. But in our conversation with banks and credit unions, it appears that many of these loans are well below the cost that would trigger coverage under the rule at all. It is especially likely that a refinance loan would be low cost and not a covered loan if the borrower has been current on the existing auto loan and the loan is for less than the value of the car. If the borrower is not current, then the ability-to-repay requirements are all the more important. Again, depositories are in a position to be able to make a relatively inexpensive reasonable determination of ability to repay, and they should be required to do so particularly on any loans that put a borrower's car at risk.

More concerning is the possibility that this exemption will be exploited by non-depository lenders. In particular, the refund of the $50 origination fee is a wholly inadequate remedy for an individual borrower whose car has been repossessed because of an unaffordable loan. Any benefit or "access" facilitated by this exemption for vehicle title loans is dwarfed by the risk of harm it poses. Thus, we oppose making this exemption available for vehicle title loans.

12.6.2. Loan term conditions unique to the default-based exemption: § 1041.12(b).

The exemption would limit the loan term to a maximum of 24 months and the modified total cost of credit to a maximum annual rate of 36%, where the modified cost excludes a single origination fee. That fee may either represent a reasonable proportion of the lender's cost of underwriting loans under this section or may be up to $50 even if the lender's costs are lower. See section 12.2 above for our discussion of the origination fee.

The Bureau also solicits feedback on the inclusion in the modified total cost of credit the cost of insurance products related to a lender's vehicle security interest. The Bureau notes that some community banks, credit unions, and other installment lenders may require these products on such loans, and notes that it believes the risks of the loan being unaffordable increase in those circumstances. We agree and urge the Bureau to include, as proposed, not only the cost of "required" credit insurance products but also the cost of those the lender may describe as "voluntary."[648] We note that often products that lenders claim are voluntary have high attachment rates strongly suggestive of coercion. See section 3.9 above on the "total cost of credit" definition above for further discussion.

12.6.3. Borrowing history condition: § 1041.12(c).

The exemption would limit loans on a per lender/affiliate basis to no more than two per lender/affiliate within 180 days. The Bureau asks whether a different limit, like one every six months, would better achieve the objectives of the exemption (including, the Bureau notes, consumer protection and access).

First, we again emphasize the importance of applying any same lender/affiliate limit to same the service provider/affiliate as well; see section 3.4.2 above.

In addition, four loans per year with a high and/or unlimited origination fee is too many. This is particularly concerning given that the limit does not apply across lenders, as the SBREFA outline proposed it would.

We urge further restrictions based on borrowing history related to other covered loans made by the same lender/service provider; see 12.3 above.

12.6.4. Default rate limit of 5% and remedy for exceeding it: § 1041.12(d).

The exemption would require lenders to maintain and comply with policies and procedures for effectuating an underwriting method designed to result in a portfolio rate that will not exceed 5% per year. The lender would be required, at least once every 12 months, to calculate the portfolio default rate for loans outstanding at any time during the preceding year. If the rate exceeds 5%, the lender must refund the origination fee within 30 days to every customer who received a loan included in that calculation.

The Bureau notes that lenders with accommodation loan programs report to the Bureau that they have portfolio default rates well below 5%, noting banks typically had charge-off rates of 1-3%.[649] Nonetheless, we are not confident that a 5% default rate alone guarantees that borrowers are not struggling. These loans will all have leveraged payment mechanisms, which helps to ensure repayment despite unaffordability. Moreover, it is possible that lenders will engage in aggressive debt collection

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[648] See n.173 and accompanying text above; Adam Rust and Amelia O'Rourke-Owens, Reinvestment Partners, Understanding Credit Insurance (2016), http://www.reinvestmentpartners.org/wp-content/uploads/2016/03/An_Introduction_to_Credit_Insurance.pdf.

[649] 81 Fed. Reg. at 38045 n.756 (citing ICBA Letter Oct. 6, 2015)

practices in order to make sure that their default rates stay below 5%. That would be a very harmful side effect.

The proposed remedy, though predictable as the Bureau notes, is not sufficient. For that portion of borrowers who defaulted, the refund does very little to mitigate harm, which could include failure to meet other obligations and expenses, late fees, overdraft fees, loss of bank account, debt collection, and if vehicle title is permitted, repossession of their car.

For these reasons and others, we urge the Bureau to require all Section 12 exemption lenders, at a minimum, to comply with the general underwriting requirement of § 1041.9(b)(1)(i), even if they are exempted from the specifics of § 1041.9(b)(2) and .9(c). That will give the Bureau greater flexibility to take into account indicators like high delinquencies and aggressive debt collection practices on these loans. Indeed, as the Bureau notes, low default rates alone do not prove ability to repay.[650]

In the alternative, the Bureau should add a comment in the anti-evasion section that explains that aggressive debt collection measures would be an evasion of the 5% default rate condition.

We also urge that the lender be required to engage in loss mitigation on the troubled loans.

And we strongly urge that any lender whose default rate exceeds 5% be required to take meaningful corrective actions to bring down the default rate. If the default rate substantially exceeds 5%, or if it exceeds that rate two 12-month periods in a row, the lender should be prohibited from continuing to make loans under the exemption until they submit revised policies and procedures to the Bureau and receive the Bureau's approval.

12.6.5. Calculation of the default rate: § 1041.12(e).

The exemption would require that the default rate be calculated as the percentage of average outstanding balances, using simple month-end balances for each month in the 12-month period, that were either charged off or that were delinquent for a period of 120 consecutive days or more during the period.[651] It must be calculated as a gross sum using all loans outstanding at any point during the 12 months.[652] It must be calculated within 90 days following the last day of the 12-month period.

We agree that a standardized default rate calculation would be important to this exemption. However, we believe that a per-borrower cohort default rate, as described in section 7.5.1 above, would be more appropriate. The Bureau solicits comment on whether the default rate should include loans that are

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[650] 81 Fed. Reg. at 47948 ("factors such as a lender's use of a leveraged payment mechanism, taking of vehicle security, and collection tactics, as well as the consumer's ability to access informal credit from friends or relatives, might result in repayment of the loan without indicia of harm that are visible through observations of loan performance and reborrowing").

[651] The Bureau notes that that the FFIEC's charge-off policy requires charging-off closed-end credit after 120 days delinquent. A loan is considered 120 days delinquent even if it is re-aged by the lender prior to the 120th day, unless the consumer has made at least one full payment and the re-aging is for a period equivalent to the period for which the consumer has made a payment. Proposed § 1041.12(e)(3).

[652] The rule provides that only the unpaid amount is included in charged-off/delinquent amount. The standard would appropriately include both on- and off-balance sheet loans. The rule also requires including loan even if re-aged by the lender unless the consumer has made at least one full payment and the re-aging is for a period equivalent to the period for which the consumer made the payment.

refinanced and if so, how. As we note above, the significant upfront origination fee provides greater incentive for lenders to refinance loans, so monitoring of refinance rates here is very important. A cohort default rate would track individual borrowers and provide a more accurate view of the percentage who are defaulting. It would be a per-borrower rate, not a per-dollar rate like the Bureau has proposed. Per-dollar rates can be deceptively low because they do not account for the fact that many borrowers make several payments before defaulting.

12.7. Additional Comments on Provisions Applicable to Both Longer-Term Loan Exemptions: §1041.11 and § 1041.12.

There are several additional provisions applicable to both longer-term loan exemptions we have not addressed above, which we address here.

Both exemptions provide that, if a lender holds the consumer's funds on deposit, it may not, in response to an actual or expected delinquency or default, sweep the account to a negative balance, exercise a right of set-off to collect on the loan, including placing a hold on funds in the consumer's account, or close the account.[653] We generally support these limitations as important protections when a lender also holds the borrower's funds on deposit. We also urge that the rule provide that, whether the loan is delinquent or not, the lender may only debit the account for repayment if the entire payment due is available. Otherwise, the borrower may have the account swept to zero for an unaffordable payment and be left without sufficient funds for subsequent payments.

Both exemptions also share certain loan term conditions: not open-end; repayable in two or more substantially equal payments due at substantially equal intervals due no less frequently than monthly; and fully amortizing with a payment schedule that allocates payments to outstanding principal and interest and fees as they accrue only by applying a fixed rate of periodic interest to the outstanding balance of unpaid principal every repayment period.[654] We support these requirements as important to mitigating the harm an exemption from ability-to-repay may cause. We strongly agree that closed-end loans are "simpler and more transparent" for consumers and that permitting open-end loans would add complexity and risk without appreciable benefit (see section 10.6 for further). We also note, as the Bureau does, that these conditions generally mirror existing NCUA PAL requirements, including that the loans must be closed-end.

Both exemptions also prohibit prepayment penalties, which we support, while emphasizing our recommendation that origination fees be refunded pro rata on loans repaid early.[655] In addition, both exemptions would not exempt lenders from the limitations on unsuccessful payment attempts of § 1041.14, which we support.

Finally, both exemptions require that lenders making exemption loans report information either to each RIS or to a consumer reporting agency, which we support. The Bureau notes that 75% of federal credit unions currently report to consumer reporting agencies.[656] In addition, we urge that any lender that makes other covered loans in addition to longer-term exemption loans, and thus reports to RISs generally, be required to submit longer-term exemption loans to the RISs. This will provide other

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[653] Proposed § 1041.11(e)(1)(ii) and § 1041.12(f)(1)(ii).
[654] Proposed § 1041.11(b) and § 1041.12(b).
[655] Proposed § 1041.11(e)(1)(i) and § 1041.12(f)(1)(i).
[656] 81 Fed. Reg. at 48038

lenders making covered loans are more complete and detailed picture of a borrower's covered loan activity, relevant to their ability-to-repay determinations.

12.8. Payment-to-Income-Based Exemption Included in SBREFA Outline is Appropriately Excluded from the Proposal.

We strongly support the removal of a payment-to-income-based exemption from an ability-to-repay determination since the SBREFA outline. That proposal considered an exemption from an ability-to-repay requirement for longer-term loans of up to six months, so long as the loan's payments did not exceed 5% of a borrower's gross income (a payment-to-income, or PTI, ratio of 5% or less). The undersigned groups, along with a coalition of over 500 civil rights, consumer, labor, faith, veterans, seniors, and community organizations from all 50 states, strongly support its exclusion from the proposed rule.[657]

As we discuss in section 5.3 above, consideration of expenses is critical to underwriting for ability to repay. This exemption would have sanctioned a purely income-based approach, and without any of the cost limitations of the current proposed exemptions.

We understand that the Bureau's research suggests a correlation between payment-to-income ratios and levels of default. And yet, the Bureau's research found extraordinarily high default levels on online installment loans even at ratios of 5% or less. For one lender in the Bureau's data whose loans included both storefront and online loans, 28-30% of loans with PTI of 5% of less defaulted.[658] We note that 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.[659]

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 38-40% at PTI of 5% or less; this analysis included first-payment defaults.[660]

We further note that these high default rates even at 5% PTI or less are not surprising. The Bureau's general ability-to-repay standard takes a "residual income" approach, meaning that it considers income and expenses, rather than a debt-to-income approach as used in other markets. The CFPB explains this rationale, noting that for individuals with relatively low incomes, an assumption that debt is affordable based merely on the ratio of that debt to the borrower's income is less likely to be true.[661] Take, for

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[657] The undersigned and additional groups state their opposition to the exemption here: http://ourfinancialsecurity.org/wp-content/uploads/2016/06/Grouprelease.pdf; http://stopthedebttrap.org/wp-content/uploads/2016/06/stdt_5percent_jun2016.pdf

[658] Supplemental Findings at 17 (Figure 6), 22 (Figure 9) and n.31 at p.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.

[659] 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.

[660] Supplemental Findings at 18, 23, 24.

[661] 81 Fed. Reg. 47941: "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

example, a borrower with a family of four at the federal poverty level of $24,300 annually, $2025 monthly. A 5% PTI standard would assume that that borrower has an extra $101.25 each month, or $1,215 annually, that they can spare toward service of payday loan debt. This is not a safe assumption. A PTI standard also ignores the borrower's existing debt load or challenges meeting regular expenses.

We flag that the Bureau's statement that it may need to raise the limit to higher than 5% to accommodate certain depository loans is particularly alarming. The Bureau asks if a payment-to-income based exemption would be "necessary and appropriate to carry out the purposes and objectives of Title X." It would be neither, and we strongly urge the Bureau to keep this dangerous exemption out of the final rule.

While a rationale offered in support of a 5% PTI exemption is that it will facilitate banks' making small-dollar loans to their more vulnerable customers, we caution that the cost of this exemption would dramatically outweigh any benefits. First, the exemption does little to ensure affordability, yet risks sanctioning unaffordable loans to many borrowers. Second, an income-only exemption aimed at banks squarely undermines the FDIC and OCC's bank payday guidance, which requires consideration of income and expenses through review of checking account activity and has successfully kept abusive bank payday loans at bay.

Third, there is little reason to expect banks to markedly increase reasonably priced small dollar lending to financially vulnerable customers, so long as they can generate $17 billion annually in overdraft and NSF fees, much of which from those same customers.[662] A separate rulemaking is sorely needed to address those abuses, and it should do far more to steer banks toward fair and affordable small dollar credit than a PTI exemption would.

Finally, *even* assuming that bank-issued products issued under an exemption were affordable—which again, is not warranted—there is no evidence that more affordable bank-issued products will reduce unaffordable products, and they may well bourgeon them. 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 the 2008 interventions.

And in fact, the exemption would risk *bolstering* predatory lending in at least two ways. First, any lender, bank or non-bank, would be able to exploit the exemption itself. Second, lenders should be expected to use the exemption in an effort to weaken state laws. Over half of states have interest rate limits on longer-term loans. The sanctioning of a 5% PTI limit would give 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.

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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."

[662] CRL, *Broken Banking*, *supra*.

13. PAYMENT PROTECTIONS ARE WARRANTED AND SHOULD BE STRONGER: §§ 1041.13-15.

13.1. Overview.

Proposed § 1041.14 protects consumers from some of the harm that leveraged payment mechanisms can impose by generally prohibiting covered lenders from continuing to debit a consumer's account after two consecutive attempts have failed. Consumers routinely incur multiple NSF and overdraft fees as a result of payment attempts on covered loans, and we strongly support protections to limit this harm.

However, we urge that the proposed protections be strengthened in several respects. There is precedent and justification for prohibiting use of leveraged payment mechanisms for high-cost credit. If the Bureau does not wish to do so, we urge:

- Authority to debit an account should be revoked after one failed payment, not two consecutive ones.
- If the Bureau retains the proposed trigger of two consecutive payments, the payment authorization should also be revoked after the consumer has incurred three failures in a 12-month period, regardless of whether or not they are consecutive.
- Payment failures should be viewed as consecutive if there are failures in two consecutive months. At a bare minimum, any consecutive failures of regularly scheduled payments should trigger the reauthorization requirement, even if there are re-initiated, partial or fee payments in between.
- Failed payment attempts from all loans by the same lender should be included in what are considered consecutive payments.
- After two consecutive failures and then a third after a new payment authorization, a fourth attempt should not be permitted.
- Lenders that hold the consumer's deposit account should be barred from sweeping the account to negative, collecting partial payments, or imposing overdraft or NSF fees as a result of their own payments.

In addition to the protections and re-authorization requirements that are triggered after failed payments, we urge the CFPB to adopt additional rules to protect consumers from the harm of leveraged payment mechanisms. These include:

- All authorizations should contain a clear right to revoke. At a minimum, this requirement should be added for re-authorizations.
- Lenders should not be permitted to obtain an authorization for more than one payment channel, use wage assignments as a back-up mechanism, or use leveraged payment mechanisms for accelerated balances.
- Lenders should be required to comply with any applicable network rules. Any authorization that violates § 1041.14, network rules, or other applicable laws should be null and void and, if an EFT, an unauthorized payment under the EFTA. An attempt to collect via an unauthorized payment should also be an abusive debt collection practice.
- The CFPB should strengthen the Regulation E ban on compulsory use by prohibiting practices that coerce consumers into preauthorizing EFTs.
- The CFPB should take further action to protect consumers from overdraft fee abuses and to ban remotely created checks.

We support the proposed disclosures of upcoming payment transfers and the consumer rights notice after the lender's authorization has been revoked due to two consecutive transfers. These notices should be required to be in the language that the lender uses to communicate with the consumer. The upcoming transfer notice should also include information on the previous balance, last payment, and new balance. The electronic short forms should include more information when the notice is sent by email.

13.2. The Harm From Use Of Leveraged Payment Mechanisms Supports The Proposed Rule And Even Stronger Protections.

In Market Concerns – Payments, the Bureau seeks comments on harm caused by leveraged payment mechanisms in credit transactions.[663] We agree that these mechanisms cause considerable harm that supports the proposed rule and even stronger protections.

Leveraged payment mechanisms provide payday and car title lenders with first-in-line access to a borrower's financial account or income. This access puts lenders first in line to collect ahead of other creditors and bills that rely on voluntary payment. When collection attempts are successful, they are often successful only because the process forces a payment to the lender before the borrower meets other debts or basic living expenses. Whether collection attempts are successful or unsuccessful, they can trigger numerous fees from the consumer's financial institution and even lead to loss of the checking account and inability to get a new one. Lenders rely on the power of leveraged payment mechanisms instead of underwriting for ability to repay.

There is precedent for a complete prohibition on high-cost lenders' use of leveraged payment mechanisms. In 2006, Congress prescribed the terms of consumer credit extended to members of the military and their dependents as part of the Talent-Nelson amendment to the John Warner National Defense Authorization Act of 2007. These limitations included a prohibition on the use of a check or other method of access to a deposit, savings or other financial account maintained by the borrower, or the title of a vehicle a security for the loan.[664] This limitation was included after a Department of Defense report to Congress found that:

"Check-holding, a central feature of payday loans, is particularly risky for military borrowers. Every payday loan involves a prospective "bad" check. Military borrowers are required to maintain bank accounts in order to receive direct deposit of military pay and are subject to the Uniform Code of Military Justice that penalizes deliberately writing a check not covered by funds on deposit. Borrowers become trapped in repeat borrowing or renewals of loans in order to keep the check used to obtain the loan from bouncing, a key reason that payday loans are debt traps."[665]

In 2014, a subsequent report by the Department of Defense found that servicemembers were frequently required to use another leveraged payment mechanism, the military allotment system, to secure consumer credit. That report found that, of servicemembers who had taken out unsecured

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[663] 81 Fed. Reg. at 48049.

[664] 10 U.S. Code § 987(e)5-6.

[665] "Report On Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents." Washington, DC: Department of Defense, August 9, 2006. http://www.defense.gov/pubs/pdfs/report_to_congress_final.pdf.

credit, 42% were required to make payments using the military allotment system.[666] In addition, a series of investigations and enforcement actions surrounding the use and abuse of the allotment system further illustrated the harm caused by the use of the allotment system as a leveraged payment mechanism.[667] As a result, the Department of Defense prohibited the use of the allotment system to collect payments to purchase, lease or rent personal property in 2014.[668]

Given the risks of high-cost loans made by lenders who have insufficient incentive to ensure ability to repay, a complete prohibition on the use of leveraged payment mechanisms would be warranted. If not entirely prohibited, the evidence amply supports stricter limits than those proposed.

In 2016, the CFPB released a report that examined the outcome of payment attempts made by a set of online lenders.[669] These findings demonstrate two key points relevant to requiring reauthorization after a failed payment. These should both be considered in the important context that any NSF or overdraft on a covered loan is likely occurring *on payday*, when a borrower's funds are highest.

First, the fact that some payments are only successful due to overdraft demonstrates that a bounced payment is a particularly strong sign of distress. Second, additional payments attempts are far more likely to bounce than to succeed.

With respect to the first point, the report observed that many payment attempts succeed despite a lack of funds to cover the payment. In the study, the first time a payment was presented, 6% succeeded only because the payment overdrew the account and triggered an overdraft fee. On the second attempt, 10% went through for this reason. This suggests that a bounced payment is a particularly strong sign of distress.

A study by CRL also found many "invisible defaults"—payments that were successful only because they overdrew the account.[670] Many payday payments also left consumers with inadequate funds to cover other expenses, resulting in overdrafts fees shortly after the payday payment. One-third of payday borrowers experienced at least one invisible default in which their account was overdrawn on the same day that they made a payment to a payday lender. Nearly half of payday borrowers incurred an overdraft or NSF fee in the two weeks after a payday loan transaction, and 64% paid overdraft or NSF fees at some point.

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[666] "Report: Enhancement of Protections on Consumer Credit for Members of the Armed Forces and Their Dependents." Washington, DC: Department of Defense, April 2014. http://consumerfed.org/pdfs/140429_DoD_report.pdf at page 23.

[667] See "CFPB Takes Action Against Military Allotment Processor for Charging Servicemembers Hidden Fees." *Consumer Financial Protection Bureau*, April 20, 2015. http://www.consumerfinance.gov/newsroom/cfpb-takes-action-against-military-allotment-processor-for-charging-servicemembers-hidden-fees/ and "Statement by Secretary Hagel on Abuse of the Discretionary Allotment System by Financial Services Institutions." Department of Defense, June 27, 2013. http://www.defense.gov/Releases/Release.aspx?ReleaseID=16123.

[668] "New DoD Policy on Allotments." Washington, D.C.: Department of Defense, November 21, 2014. http://www.defense.gov/Portals/1/Documents/pubs/Fact-Sheet-on-New-DoD-Policy-Change-to-Allotment-System.pdf.

[669] "Online Payday Loan Payments." Washington, D.C.: Consumer Financial Protection Bureau, April 2016. http://files.consumerfinance.gov/f/201604_cfpb_online-payday-loan-payments.pdf.

[670] CRL, *Payday Mayday*, *supra.*

With respect to the second point, the CFPB's payments study also found that the more attempts online payday lenders made to debit a borrower's bank account after an unsuccessful attempt, the less likely they were to succeed. For example, among the transactions examined, 88% of first payment transfer attempts succeeded without triggering an overdraft, with 12% resulting in either an NSF fee or an overdraft. On the second attempt, only 21% of payments went through with sufficient funds, with 70% and 10% of second attempts resulting in NSF fees or overdraft fees, respectively. Third attempts had similar results, with only 20% of attempts succeeding and 73% and 8% of third attempts resulting in NSF fees or overdraft fees, respectively. These figures do not appear to support permitting a re-presentment—which has 21% chance of being successful without triggering an overdraft—before reauthorization is required. In addition, the Bureau found that 36% of borrowers who experienced a bounced payment had their checking account closed.

The experience of the consumers, consumer advocates and consumer attorneys with whom we work supports these findings. We frequently hear about consumers who are hit with numerous NSF and overdraft fees as a result of leveraged payment mechanisms and even lose their bank accounts.

We also have heard numerous stories of consumers who had difficulty stopping lenders from debiting their account and hurdles persuading financial institutions to accept stop payment orders for recurring payments.[671] The CFPB has also noted that consumers report having trouble stopping automatic charges.[672] The CFPB recently published advisories for consumers to help them revoke merchants' payment authorizations and to stop payment with their financial institutions.[673] The CFPB also published an advisory for financial institutions to remind them of consumers' rights.[674]

We agree that clear, enforceable rules are necessary, despite the existing network-specific protections that also play an important role in protecting consumers. Indeed, as discussed below, we urge that lenders be required to comply with the rules governing a particular payment device.

But private network rules do not provide a clear, consistent and generally applicable limit to repeated attempts to access a borrower's transaction account.[675] We agree with the Bureau's assessment that, while network rules are helpful, they are limited in scope, are difficult for consumers to understand or enforce, and are subject to change. For example, changes to the NACHA rules instituted in 2015 improved protections for transactions conducted through the ACH system.[676] Yet even longstanding ACH rules are routinely violated by financial institutions, by mainstream merchants, and by payday

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[671] National Consumer Law Center and New Economy Project. "RDFIs' Responsibilities to Consumers Regarding Stop-Payment Orders, Unauthorized Charges, Related Fees, and Orders to Close Accounts," September 29, 2014. http://www.neweconomynyc.org/wp-content/uploads/2014/11/letter.pdf.

[672] CFPB, Press Release, "CFPB Alerts Companies About Obtaining Consumer Authorization For Recurring Auto Debits" (Nov. 23, 2015), http://www.consumerfinance.gov/about-us/newsroom/cfpb-alerts-companies-about-obtaining-consumer-authorization-for-recurring-auto-debits/.

[673] Farrar, Davida, and Gail Hillebrand. "You Have Protections When It Comes to Automatic Debit Payments from Your Account." Washington, D.C., November 23, 2105. http://www.consumerfinance.gov/about-us/blog/you-have-protections-when-it-comes-to-automatic-debit-payments-from-your-account/.

[674] "CFPB Compliance Bulletin 2015-06: Requirements for Consumer Authorizations for Preauthorized Electronic Fund Transfers." Washington, DC, November 23, 2015. http://files.consumerfinance.gov/f/201511_cfpb_compliance-bulletin-2015-06-requirements-for-consumer-authorizations-for-preauthorized-electronic-fund-transfers.pdf.

[675] 81 Fed. Reg. at 48054.

[676] Discussed in detail at 81 Fed. Reg. at 48055.

lenders alike.[677] NACHA rules are not privately enforceable, and some courts have rejected efforts to enforce them through contract laws as well.[678]

Moreover, lenders routinely take authorization to use a broad array of leveraged payment mechanisms in ways that are unclear to the borrower. Lenders use multiple types of leveraged payment mechanisms as back-up methods to collect both regular payments and accelerated balances after default.

In 2014, CFA conducted a market scan of 84 individual lenders operating online and claiming tribal sovereign immunity through a relationship with one of 24 federally recognized Native American tribes. The market scan included a review of loan terms, pricing and the use of leveraged payment mechanisms to collect payments.[679] While the information collected was limited to lenders claiming tribal sovereign immunity and operating online, we believe that the findings are indicative of the market at large. In addition, CFA was limited to collecting information about the types of leveraged payment mechanisms accepted by lenders, rather than those that were required or incentivized. However, we believe that the findings of this analysis are indicative of a range of common payment mechanisms in this market.

Of the 84 lenders reviewed, 72 lenders or 85 percent of lenders, make accepted payment mechanisms publicly available on their websites. The remaining 12 lenders did not make any payment information publicly available. Of the 72 lenders with payment information publicly available, all of them accepted payments by ACH, 21 (29%) accepted debit cards, 29 (40%) accepted checks or money orders, 7 (10%) accepted wire transfers, 6 (8%) accepted credit cards, and 3 (4%) accepted remotely created checks. Of the lenders reviewed, less than half (32 or 44%) accepted only ACH, 18 (25%) accepted two payment mechanisms and 22 (30%) accepted three or more different payment mechanisms.

When lenders take multiple payment method authorizations, it is often unclear which mechanisms will in fact be used, and in what order, making it difficult to determine the steps a consumer would need to take to revoke authorization if necessary. While most of the online lenders in CFA's survey take authorization to debit a borrower's checking account using the ACH network, 55 percent also took authorization to use another network not subject to the NACHA protections.

The Bureau's recent enforcement action against Integrity Advance, LLC and its CEO, James R. Carnes is a good example of how use of multiple payment authorizations harms consumers. The Bureau found that the company routinely used multiple payment authorizations to continue debiting a consumer's account using remotely created checks, even after consumers revoked authorization for the company to access their accounts using the ACH network.[680] We have also encountered lenders who use the threat of an RCC for an accelerated amount to attempt to convince the consumer not to revoke ACH authorization.

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[677] *See* Letter from consumer groups to CFPB et al (Sept. 29, 2014), http://www.nclc.org/images/pdf/banking_and_payment_systems/regulator_rdfi_issues_letter_9292014.pdf.

[678] *See* NCLC, Consumer Banking and Payments Law § 5.15.6 (5th ed. 2013), updated at www.nclc.org/library.

[679] Information on file at Consumer Federation of America.

[680] "CFPB Takes Action Against Online Lender for Deceiving Borrowers." Washington, D.C.: Consumer Financial Protection Bureau, November 18, 2015. http://www.consumerfinance.gov/about-us/newsroom/cfpb-takes-action-against-online-lender-for-deceiving-borrowers/.

We agree with the Bureau's determination that consumers have little ability to avoid harm from lenders' use of leveraged payment mechanisms and that the rule is necessary to protection consumers.

13.3. Definitions: § 1041.14(a).

13.3.1. Payment transfer – in general: § 1041.14(a)(1).

Proposed § 1041.14(a)(1) generally defines "payment transfer" to mean "any lender-initiated debit or withdrawal of funds from a consumer's account" for the purpose of collecting "any amount due or purported to be due" on a loan.

We support Comment 14(a)(1)-2, which makes clear that transfers initiated by the lender's agent or payment processor are included.

We agree with the focus on lender-initiated debits; consumer-initiated debits do not pose the same concerns. The examples in Comment 14(a)(1)-5 of when a lender does not initiate a payment—payments by cash; payments initiated by the consumer through a service offered by the consumer's account-holding institution, or a court-ordered garnishment—are appropriate. However, we also urge the CFPB should keep an eye on developments in the payments world, as it is possible that the line between lender-initiated and consumer-initiated could begin to blur.

We note, as discussed in section 3.1 above, that the definition of "account" is currently too narrow, as it omits prepaid accounts and other newer types of accounts. However, we expect that the Bureau's newly announced prepaid rules will fill that gap.

We support the focus on "any amount due" and the examples given in Comment 14(a)(1)-3: a scheduled payment; a transfer for a smaller amount; collected of an accelerated balance; or a transfer to cover a late fee or other penalty. (However, as discussed in section 13.6.2 below, the CFPB should prohibit the use of leveraged payment mechanisms to collect accelerated balances.) All of these transfers can trigger NSF or overdraft fees, deprive the consumer of control over her account, and make it difficult to prioritize necessities. We also support Comment 14(a)(1)-4 making clear that transfers are covered even if the consumer disputes or does not legally owe the amount. Again, the same harm can result in those scenarios.

The definition of "payment transfer" includes electronic fund transfers (EFTs); signature checks, regardless how processed; remotely created checks (RCCs) or remotely created payment orders (RCPOs), and an account-holding institution's transfer of funds from a consumer's account held at the same institution. We agree that all of these devices should be included. As discussed above, lenders use a wide variety of payment mechanisms and often take authorizations for more than one mechanism.

As set forth in § 1041.14(a)(1)(i) and Comment 14(a)(1)(i)-1, we agree that all EFTs as defined in Regulation E should be covered, including but not limited to one initiated by a debit card or prepaid card.

Debit cards are sometimes used as payment devices for both recurring payments and payoff payments, as seen in the CFA market scan described previously. Recurring debit card payments can trigger overdraft, declined transaction or NSF fees just like an ACH payment can, and they are not covered by the opt-in rules of Regulation E.[681]

A July 2015 report released by the National Consumer Law Center also found that some prepaid cards sold by payday lenders allow lenders to make payment transfers that exceed the borrower's available balance, triggering additional fees, including overdraft fees.[682] In addition, declined transaction fees as high as $14.95 can be charged even for payments not initiated over the ACH network.[683]

We also support the inclusion of all EFTs and not just recurring preauthorized EFTs. As the CFPB has found and our organizations have frequently observed, lenders purport to offer single-payment loans often take payment authorizations that effectively result in recurring payments. Using the definition of preauthorized EFTs alone could result in evasions, as well as ambiguous and inconsistent enforcement as courts grapple with whether a payment is recurring at regular intervals.[684] In addition, even consumers who take out a single-payment loan can experience repeated NSF fees and other harm if a payment is presented multiple times. Thus, clear rules to prevent consumer harm from single-payment loans are important as well.

We agree that signature checks should be included, as under § 1041.14(a)(1)(ii) and Comment 14(a)(1)(ii)-1, regard of how they are processed. The impact on and harm to the consumer is the same, and yet the consumer has no idea how a check will be processed. Including both avoids evasions as lenders or financial institutions move between processes covered by the UCC or by Regulation E.

We agree with the inclusion of both RCCs and RCPOs in the definition of "payment transfer" under § 1041.14(a)(1)(iii) and (iv). RCCs and RCPOs are often used as back-up mechanisms if a consumer revokes or attempts to revoke authorization or stop payment of an ACH payment, as the CFPB found in the Integrity Advance case. RCCs and RCPOs can help lenders evade Regulation E and NACHA rules. We also have observed that lenders may use the threat of an RCC or RCPO to convince a consumer that it does no good to revoke authorization of the ACH payment. However, as discussed in section 13.6.8 below, we urge the CFPB to go farther and ban the use of RCCs and RCPOs altogether in consumer transactions.

We also that an account-holding institution's transfer of funds from a consumer's account held at the same institution should be covered, as under proposed § 1041.14(a)(1)(v) and Comment 14(a)(1)(v). For example, this type of transfer was used with deposit advance products. NSF fees and overdraft fees can result from these transfers as well and cause consumer harm.[685]

The CFPB observes that the proposed definition of payment transfer could apply to instances when a lender that is the consumer's account-holding institution exercises a right of set-off in connection with

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[681] 12 CFR 205.17(b)(1).

[682] "Payday Lender Prepaid Cards: Overdraft and Junk Fees Hit Cash-Strapped Families Coming and Going." Boston, MA: National Consumer Law Center, July 2015. https://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/Report_PaydayLendersPrepaid71515.pdf

[683] NCLC, Payday Lender Prepaid Cards at 14.

[684] *See* NCLC, Consumer Banking & Payments Law § 5.8.1 (5th ed. 2013), updated at www.nclc.org/library.

[685] *See, e.g.,* "The Extension of High-Cost Credit to Servicemembers and Their Families." Washington, DC: Consumer Financial Protection Bureau, December 2014. http://files.consumerfinance.gov/f/201412_cfpb_the-extension-of-high-cost-credit-to-servicemembers-and-their-families.pdf at page 6.

a covered loan—such as when the lender initiates an internal transfer from the consumer's account.[686] We agree that the definition of payment transfer does, and should, apply to set-offs. Whatever label is placed on the transfer, the impact on the consumer is the same—funds are taken automatically from her account, whether a loan is affordable or not, and can trigger NSF or overdraft fees.

To the extent that set-off is only used up to the amount of funds available to set off—and thus, the set-off does not trigger NSF or overdraft fees—it is still appropriate to include set-offs. If the set-off meets the definition of a failed transfer—it results in collection of less than the amount due—then the consumer has been left with *zero* funds in her account and is exposed to NSF and overdraft fees on any subsequent payment. Indeed, as a CRL study found, even if a payday payment does not itself trigger an immediate overdraft, nearly half of payday borrowers incurred an overdraft or NSF fee in the two weeks after a payday loan transaction.[687] These failed set-offs, like other forms of automated payments, reflect inability to repay and result in consumer harm that consumers cannot reasonably avoid. Indeed, set-offs that are used as a collection device can cause such severe harm that Congress prohibited them under credit card plans unless the consumer chooses to regularly repay the credit in that fashion[688]—in which case the set-off is just another form of preauthorized transfer. While financial institutions may retain a right of set-off for other mainstream lending products, the protections of this rule will only be triggered when a financial institution obtains a set-off right for a high-cost loan. Including set-offs in the payment protections is essential to avoiding evasions.

Finally, we support the proposed language in § 1041.14(a)(1) and Comment 14(a)(1)-1, which makes clear that the term "payment transfer" includes "but is not limited to" the specific types of transfers described. As institutions work to find faster ways to move payments and to avoid interchange fees, many institutions have developed agreements that allow them to move or settle funds among themselves without using any of the mechanisms described above. For example, the clearXchange and PopMoney networks allow payment transfers between multiple financial institutions that circumvent the ACH network entirely. As long as the result is a debit or withdrawal from the consumer's account that was lender initiated, the particular payment network appropriately does not matter. It can still result in NSF and overdraft fees, signaling inability to repay and causing consumer harm.

13.3.2. Definition of single immediate payment: § 1041.14(a)(2).

Proposed § 1041.14(a)(2) defines "single immediate payment transfer at the consumer's request." Our comments on the proposed exception under § 1041.14(d) are discussed in section 13.5 below. Here we confine ourselves to the definition.

The proposed definition includes two types of payments. Under § 1041.14(a)(2)(i), the transfer must be a one-time EFT initiated within one business day after the lender obtains the consumer's authorization. Under § 1041.14(a)(2)(ii), the transfer can be a signature check (processed either through the check system or the ACH system) processed within one business day after the consumer provides the check.

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[686] 81 Fed. Reg. at 48063.

[687] Susanna Montezemolo & Sarah Wolff, Center for Responsible Lending, Payday Mayday: Visible and Invisible Payday Lending Defaults (March 2015), http://www.responsiblelending.org/research-publication/payday-mayday-visible-and.

[688] 15 U.S.C. § 1666h.

We agree with the proposal to limit the definition (and thus the exception) to these two types of payments. Both are understood by consumers and have well defined laws governing them. Other types of payments (such as RCCs or RCPOs) are more subject to abuse.

We also agree that tight limits on how quickly the payments must be processed are essential to prevent evasions of this exception. We support Comment 14(a)(2)(i)-1, which makes clear that an EFT is initiated once it is sent out of the lender's control, such as when the lender or lender's agent sends it to a third party such as the lender's bank. Similarly, we support Comment 14(a)(2)(ii)-1, which provides a similar example using a signature check, as well as Comment 14(a)(2)(ii)-2, which makes clear that, for a check sent by mail, the clock begins when the lender receives it.

However, it would be helpful to add a second comment in both situations with examples of when the payment does not leave the lender's control. For example, if the lender sends the EFT or check to a service provider that does not immediately forward it to a bank for processing, then the exception does not apply.

13.4. Prohibition On Initiating Transfers After Failed Payment Transfers: § 1041.14(b).

13.4.1. The prohibition should be triggered after one failed payment transfer.

Proposed § 1041.14(b) prohibits lenders from initiating another payment transfer after two consecutive failed transfers. While we support this provision, we urge the CFPB to apply it after a single failed transfer.

Notably, payment attempts on covered loans are typically occurring on payday, when the consumer's funds should be highest, so any NSF or overdraft is a strong indicator of inability to repay. Further, as discussed above, the CFPB's study found that after the first failed transfer, 70% of the subsequent attempts failed, triggering NSF fees. Another 10% resulted in a payment but overdrew the account and triggered an overdraft fee—on top of the NSF or overdraft fee that the consumer already incurred on the first attempt. Only 21% of the second attempts were successful and did not trigger an NSF or overdraft fee.

Thus, the vast majority of these second attempts harmed consumers—without providing payment to lenders. Even those attempts that succeeded by overdrawing the account inflict serious consumer harm and should not be tolerated as they result in lenders collecting despite the consumers' inability to repay. Notably, the failure rate on the second attempt is little different from the third attempt, with 73% failing completely, 8% succeeding only because of an overdraft fee, and only 20% succeeding in payment without overdrawing the account. Thus, the same rationale that supports banning further attempts after the second consecutive failed transfer also supports a ban after the first failure.

We also note that applying the ban after the first failed transfer would simplify the rule considerably.

We support including all covered loans in the payments rule. All loans that are secured by payment transfers that can fail need the proposed protections.

13.4.2. Proposal to prohibit transfers after two consecutive transfers – in general: § 1041.14(b)(1).

Proposed § 1041.14(b) prohibits lenders from initiating a payment transfer from "a consumer's account" in connection with "the covered loan" after the lender has attempted to initiated two consecutive failed payment transfers from "the consumer's account."

We support this prohibition, though, as noted above, we urge it apply after one failed payment. But throughout the remainder of this section, we comment on the provision as proposed.

This provision is more than well-justified by the ample harm the leveraged payment mechanism inflicts, including lenders' misuse of leveraged payment mechanisms to collect loans despite a consumer's inability to repay and consumers' loss of control over their own accounts and other expenses.

We support Comment 14(b)-1, which makes clear that the prohibition applies to any attempt to collect payments that later fall due. Once a consumer has had two consecutive payment transfers fail—again, most likely on payday when funds are highest—the risk of harm from additional payment attempts is clearly too great. The consumer of course still owes the loan and the lender can attempt to collect it by other legal and fair means. But the consumer almost certainly does not have the ability to repay the loan, and the lender may have to face the consequences of making an unaffordable loan. The consumer has already suffered significant harm from the attempted payment transfers and should not be subjected to additional harm. In addition to imposing mounting fees and frustrating the consumer's efforts to prioritize necessities, continued debits may well lead to closure of the consumer's account, as the CFPB found occurred in 36% cases where a borrower had at least one bounced payment.

We further support the Comment's clarification that the prohibition applies to attempts to collect late fees or returned item fees. All of these attempts are likely to inflict overdraft or NSF fees on consumers and trigger other collateral harm, with a low probability of payments to the lender. The consumer has already suffered penalties from the fees inflicted by her financial institution as a result of the first two failed transfers.

We note some ambiguity in both the rule and the Comment on whether the prohibition applies to future attempts to debit any account or only "the" account where the first and second payment transfer failed. While many lenders may not take authorization to debit more than one account, we are aware of numerous lenders that consider other bank accounts in the borrower's name as eligible to process payments against. American Web Loans considers any additional bank accounts in the borrower's name, in addition to the account information explicitly provided by the, as described below:

If we extend credit to a consumer, we will consider the bank account information provided by the consumer as eligible for us to process payments against. In addition, as part of our information collection process, we may detect additional bank accounts under the ownership of the consumer. We will consider these additional accounts to be part of the application process.[689]

In another example, AAA Community Finance includes the following language in its privacy policy claiming the ability to debit an account even if the account information was not provided as part of the application:

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[689] https://www.americanwebloan.com/privacy-policy accessed 9/26/2016.

If we extend credit to a consumer, we will consider the bank account information provided by the consumer as eligible for us to process payments against. In addition, as part of our information collection process, we may detect additional bank accounts under the ownership of the consumer. We will consider these additional accounts to be part of the application process and eligible for payment retrieval.[690]

Under agreements such as these, consumers may close one account in an attempt to retrieve control over their finances only to find that the lender has submitted a payment against the new account at the same institution.

Any attempt to use an EFT to debit a second account should be considered unauthorized under Regulation E because the purported authorization would not be "clear and readily understandable."[691] NACHA rules contain the same standard, and the model ACH debit authorization form in NACHA's Operating Guidelines lists the depository name, routing number, and account number of the specific account authorized.[692] An authorization that purported to authorize a debit of another account that is not the one that the consumer was using for regular payments would also not be clear and readily understandable because it would not include clear information about the timing of the debit, which the CFPB has identified as one of "the most significant terms of an authorization" under Regulation E.[693] Under NACHA rules, as well, an authorization not taking effect until some future point in time that might never occur is not clear and readily understandable.[694]

Nonetheless, to avoid confusion and evasions, we urge the CFPB to revise the rule to state:

> *A lender must not initiate a payment transfer from a consumer's account in connection with a covered loan after the lender has attempted to initiate two consecutive failed payment transfers from ~~the consumer's account~~ <u>an account of the consumer</u> in connection with that covered loan.*

We also urge the CFPB to add a comment explaining that the lender may not debit a second account (unless the consumer provides a new authorization). These changes are necessary to protect consumers who do not have the ability to repay and can be subject to multiple fees and potential negative reports to ChexSystems that prevent them from opening up new accounts.

We also note that online lenders that are often operating illegally without state licenses are particularly notorious in continuing to debit consumer accounts and claiming broad authority to follow the consumer to other accounts. Thus, this clarification will help to stop illegal lenders. But we also support the clarification in Comment 14(b)-1 that the protections apply regardless whether the lender holds an otherwise valid authorization or instrument.

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690 https://www.aaacommunityfinance.com/Pages/privacypolicy.aspx accessed 9/26/2016.
691 12 CFR 1005.4(a)(1).
692 2016 NACHA Operating Guidelines app. G, Consumer Authorization for Direct Payment via ACH (ACH Debits).
693 CFPB Compliance Bulletin 2015-06, Requirements for Consumer Authorizations for Preauthorized Electronic Fund Transfers at 4 (Nov. 23, 2015), http://files.consumerfinance.gov/f/201511_cfpb_compliance-bulletin-2015-06-requirements-for-consumer-authorizations-for-preauthorized-electronic-fund-transfers.pdf.
694 See Affinion Benefits Grp., L.L.C. v. Econ-O-Check Corp., 784 F. Supp. 2d 855, 877 (M.D. Tenn. 2011) (interpreting NACHA standard).

13.4.3. Prohibit use of any leveraged payment mechanism, include wage assignment, after failed transfers.

The prohibition on further payment transfers does not apply to payroll deduction or wage garnishment. As discussed in section 13.6.3 below, we urge the CFPB to prohibit wage assignments on covered loans (and more broadly) or, at a minimum, to prohibit their use (or payroll deduction) as a back-up payment mechanism.

If the CFPB declines to follow those recommendations, it should revise § 1041.14(b)(1) to read:

> *A lender must not initiate a payment using a leveraged payment mechanism ~~transfer from a consumer's account~~ in connection with a covered loan after the lender has attempted to initiate two consecutive failed payment transfers from an account of the consumer in connection with that covered loan.*

This change would continue to generally apply the requirements of § 1041.14 and § 1041.15 only to payment transfers as defined in those sections, but would ensure that wage garnishments could not be used to evade the rules.

13.4.4. Definition of failed transfer; even a second attempt should be prohibited if the payment is returned due to a stop payment order or because it was unauthorized. § 1041.14(b)(1).

13.4.4.1. In general.

Proposed § 1041.14(b)(1) states that a payment transfer is deemed to have failed when it results in a return indicating that the account lacks sufficient funds. Comment 14(b)(1)-3 states that a transfer that results in a return for a reason other than a lack of sufficient funds, such as a return made due to an incorrectly entered account number, is not a failed transfer.

We do not object to not counting administrative returns such as incorrectly entered account numbers. Those returns have no impact on the consumer and do not indicate inability to repay.

However, we strongly urge the CFPB to broaden this provision to include returns when the consumer has stopped payment or when the payment was unauthorized. In those situations, it is especially critical that the lender stop attempting to debit the consumer's account. There is an increased chance that the loan is illegal. The consumer may also have stopped payment in an effort to regain control over her finances after having gotten stuck in an unaffordable loan.

While we urge the CFPB to prohibit all second attempts after a failed transfer, as discussed above, it is especially critical that no second attempt be permitted in these situations. While a stop payment order should in theory be effective in blocking second attempts, it may not be if the lender uses a different payment channel—i.e., by switching from an ACH to an RCC, or from a check to an EFT. Many banks do not have effective mechanisms to apply stop payment orders across different payment channels.[695] The same problem can occur if the consumer challenges a payment as unauthorized but the bank does not recognize another attempt to submit the payment in a different form.

It should also be deemed to be a failed transfer if the lender refrains from initiating a payment because it observes that there are not sufficient funds. For example, lenders might obtain bank account login information or use screen scraping services in order to be able to determine when the paycheck has been deposited. While the consumer may not incur an NSF or overdraft fee if the lender refrains from attempting a payment, permitting lenders to time the submission of their payments when the consumer does not have sufficient funds on the expected day helps the lender to collect despite the unaffordability of the loan. Thus, the consumer is more likely to experience NSF or overdraft fees due to other payments shortly thereafter.

It is especially important to deem an observation of nonsufficient funds to be a second transfer attempt. After the first failed transfer, the lender will have a strong incentive to prevent a second consecutive failed transfer in order to avoid invoking the prohibition. If one transfer has failed and a subsequent observation also indicates insufficient funds, the consumer almost certainly lacks ability to repay. Preventing future transfer attempts unless the consumer re-authorizes the payments is critical. If lenders can get a window into the account and time their debits the moment any money is there, they can evade the protections of the rule and collect unaffordable payments.

13.4.4.2. Failed transfers when the lender is the account-holding institution; sweeps to negative should be prohibited.

Proposed § 1041.14(b) also provides that, if the lender is the consumer's financial institution, a failed transfer is one that results in collection of less than the amount for which the transfer was initiated. The Bureau seeks comment on whether the provisions appropriately address situations in which a lender that is the consumer's account-holding institution initiates payment transfers that result in nonpayment or partial payment.[696]

We support the rule that a payment transfer is deemed to have failed if the account-holding institution fails to collect the amount for which the payment is initiated. There are no "returns" in this situation, so that cannot be the judge of a failed transfer. The institution controls the consumer's account and is able to make a transfer if there are funds. If the institution is unable to collect the payment, then the transfer clearly has failed.

We also support the part of proposed Comment 14(b)(1)-4 that makes clear that the transfer counts as a failed transfer regardless of whether the result is classified or coded in the lender's internal systems as a return for nonsufficient funds. The substance of the transaction is most important.

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[695] After a lawsuit and news article exposed problems that JP Morgan Chase customers had stopping payments on payday loan ACH payments, *see* Complaint and Jury Demand, Baptiste v. JPMorgan Chase Bank, N.A., No. ECF CASE (E.D.N.Y. Oct. 1, 2012), Chase implemented reforms under a settlement agreement. *See* Letter from Sheila Carson, JP Morgan Chase, to Josh Zinner, NEDAP (June 20, 2013), available online as companion material to NCLC, Consumer Banking & Payments Law (3d ed. 2013), updated at nclc.org/library.
[696] 81 Fed. Reg. at 48065.

However, we object to the part of Comment 14(b)(1)-4 that states that a return is not a failed return "if the lender merely defers or foregoes debiting or withdrawing payment from an account based on the lender's observation that the account lacks sufficient funds." While there may be no NSF or overdraft fees in this situation, the lender has still observed a consumer who in unable to repay. Future payment attempts could endanger the consumer's ability to meet necessities and result in overdraft or NSF fees in connection with other payments. If a lender observes a lack of sufficient funds on the day a payment is due on two consecutive occasions, then it is appropriate for the lender to stop attempting to initiate payment transfers unless the consumer provides a new authorization.

A lender that is the consumer's account-holding institution should also be prohibited from collecting account-related fees other than bona fide late fees under the loan agreement for deferring a payment transfer attempt when the borrower's account has insufficient funds. Any such fee would effectively consist of additional interest, changing the total cost of borrowing substantially, particularly for loans with shorter terms.

The Bureau seeks comment on whether account-holding institutions should be permitted to assess overdraft fees in conjunction with attempts to collect loan payments. The Bureau asks whether and how frequently such lenders make repeated payment withdrawal attempts through their internal systems in connection with proposed covered loans in ways that can be harmful to consumers.

We urge that a lender that is the consumer's account-holding institution be prohibited from sweeping an account below zero to collect a payment or from charging NSF fees or overdraft fees in connection with an actual or failed transfer. The lender can observe that the account lacks insufficient funds for the payment and should not be permitted to deliberately induce an overdraft or to profit from the consumer's inability to make the payment. NSF and overdraft fees are an account feature developed, at least originally, to address an inherent lag in processing checks and other payment devices. Internal systems have no such lag and, under no circumstances should a payment transfer attempt made through an internal transfer system trigger an NSF or overdraft fee.

In addition, the institution should be prohibited from collecting partial payments if the account balance is insufficient to collect the entire, scheduled payment. If the consumer does not have sufficient funds for the entire payment, then emptying the account will still leave her late on the loan while leaving her with no funds for necessities and subjecting her to NSF and overdraft fees.

Taken together, these recommendations would help any payment transfer attempt from triggering an NSF or overdraft fee. However, to ensure that future loan products or internal payment transfer systems are adequately covered by the protections in this section, we urge the Bureau to adopt an explicit prohibition on NSF or overdraft fees triggered by payment transfer attempts by a lender that is the consumer's account-holding institution.

13.4.4.3. All transfer attempts in connection with any loan from the same lender should be included.

Proposed § 1041.14(b)(1) prohibits subsequent payment transfers after two consecutive failures in connection with "that covered loan." In proposed comment §1041.14(b)-2, the Bureau clarifies that, when the prohibition is triggered, the lender is not prohibited under the rule from initiating a payment transfer in connection with a bona fide subsequent covered loan made to the consumer.[697]

The Bureau seeks comment on what additional provisions may be appropriate to clarify the concept of a bona fide subsequent covered loan, including provisions clarifying how the concept applies in the context of a refinancing. The Bureau also seeks comment on what additional provisions may be appropriate to clarify how the proposed prohibition on further payment transfers applies when a consumer has more than one outstanding loan with a lender, including situations in which a lender makes two failed payment transfer attempts when alternating between covered loans.

We strongly oppose permitting lenders to avoid the protections of the payments rule by making further transfer attempts in connection with other outstanding loans after the consumer has already suffered two consecutive failures on one loan. The impact on the consumer is the same: multiple NSF or overdraft fees and potential collection of payments despite inability to repay. The lender has records of all of the loans made to that consumer and has the ability to refrain from making subsequent transfer attempts on other loans.

The prohibition and reauthorization requirement should apply across all loans from a single lender or affiliate (or a single service provider or affiliate). For example, if a borrower has two outstanding loans, and an attempt to withdraw a payment fails for loan A, then no further payments on loan B should be permitted until reauthorization for loan A has been received.

Permitting otherwise could lead to evasions as lenders split their loans into smaller amounts and offer multiple loans. This would provide lenders the advantage of smaller payments that are more likely to go through, as well as the ability to collect on a second loan even if consecutive transfer failures block future transfers on one of the loans.

Consequently, we recommend that proposed § 1041.14(b)(1) be revised to read:

> *A lender must not initiate a payment transfer from a consumer's account in connection with a covered loan after the lender has attempted to initiate two consecutive failed payment transfers from the consumer's account.* ~~*in connection with that covered loan*~~

With respect to Comment 14(b)-2, if a "subsequent" loan is made after the transfer failures, new payment transfers should be permitted only if the new payment authorization qualifies for the exception in proposed § 1041.14(c). However, as discussed below, if the subsequent loan is a refinance, then a single payment failure should again trigger the prohibition. Thus, we recommend that this Comment be revised to read:

> *If a lender triggers the prohibition in § 1041.14(b), the lender is not prohibited under § 1041.14(b) from initiating a payment transfer in connection with a bona fide subsequent covered loan made to the consumer <u>if the lender has obtained a new payment authorization as provided in § 1041.14(c)</u>, provided that the lender has not attempted to initiate two consecutive failed payment transfers from the consumer's account in connection with the bona fide subsequent covered loan.*

[697] 81 Fed. Reg. at 48065.

13.4.5. Definition of first failed transfer: § 1041.14(b)(2)(i).

Proposed § 1041.14(b)(2)(i) describes three situations in which a failed payment transfer is considered to be the first failed transfer.

13.4.5.1. Include all loans from the same lender: § 1041.14(b)(2)(i)(A).

As discussed above, any two consecutive payment failures from the same lender should trigger the prohibition, even if they are on different loans. Thus, proposed § 1041.14(b)(2)(i)(A) should be revised to read that a payment transfer is the first payment transfer if:

The lender has initiated no other payment transfer from the consumer's account in connection with ~~the covered~~ any loan.

We also urge that a previous payment failure on a non-covered loan should also be considered a first failed payment transfer. As discussed earlier in these comments, we fear that lenders will use non-covered loans as bridge loans between unaffordable covered loans. If a payment transfer fails on a previous non-covered loan, the lender should be required to consider that a failed transfer. To permit otherwise would encourage evasions as lenders constantly refinance loans from covered to non-covered loans.

13.4.5.2. Failures in consecutive months should be "consecutive" even if there is an intervening payment: § 1041.14(b)(2)(i)(B).

Proposed § 1041.14(b)(2)(i)(B) effectively states that any successful payment transfer resets the clock to zero. It provides that a payment transfer is the "first" transfer if the immediately preceding payment transfer was successful.

Proposed Comment 14(b)(2)(i)-1(i) and (ii) provide examples illustrating this provision. Example (i) illustrates a lender that successfully re-presents a payment that bounced the first time, and then initiates a transfer attempt for the next payment, which then fails. The example explains that the re-presentment has reset the count to zero and the second bounce is deemed to be a first payment failure.

We object to this Comment. As discussed in section 13.2 above, even a single payment failure should trigger the rule and require reauthorization of the payment authorization. In addition, as discussed in section 13.6.1 below, even if the CFPB retains a rule generally requiring two consecutive payment failures, it should also prohibit future transfer attempts if there are three payment failures, even if nonconsecutive, in any 12-month period.

Moreover, even if the CFPB retains the requirement for two consecutive failures, if a payment attempt has failed for two consecutive months, clearly the consumer is struggling with inability to repay and is suffering NSF and/or overdraft fees on her account. The fact the lender has managed to collect a payment between two due dates does not change that situation. Thus, we urge the CFPB to view payment failures as "consecutive" if there are failures in two consecutive months even if there is an intervening successful payment in between.

We also urge a consecutive rule to be based on two consecutive months, not just two consecutive payments (i.e., two biweekly or semimonthly payments). The Bureau bases other provisions in the rule on an assumption that consumer expense cycles are about 30 days long; we present evidence suggesting that for borrowers of covered loans, they are likely much longer (see section 8.8.1 above). But even assuming a monthly cycle, it may be that only the payments that coincide with rent due dates once a month will bounce. The payment attempts are clearly causing consumer injury and reflect an unaffordable loan even if the payments in between are successful. Moreover, it is important to consider that successful payments in between may only be successful because they are paid via high-cost overdraft.

In addition, as discussed in the next section, even if the CFPB rejects our suggestion to count failures in consecutive months, we urge the CFPB not to permit a smaller payment to reset the failure clock.

We support the example in Comment 14(b)(2)(i)-1(ii), which provides that a cash payment in between two failed payment transfers does not reset the clock to zero. A cash payment does not indicate that a consumer has funds in her account and that payment transfers can be safely made. The cash may have come from a friend or family member, or be the result of aggressive debt collection practices.

13.4.5.3. After two consecutive failures and then a third following a new authorization, a fourth should not be permitted: § 1041.41(b)(2)(i)(C).

Proposed § 1041.41(b)(2)(i)(C) provides that a payment transfer is the first payment transfer if it is the first to fail after the lender obtains a new payment authorization pursuant to § 1041.41(c). In other words, once there is a new authorization, two new consecutive failures are required before the authorization is revoked again.

We oppose this rule. If there have been three consecutive failed transfers, the lender should not be permitted to subject the consumer to a fourth. As the Bureau's study shows, after each consecutive failure, the likelihood of success keeps going down. A fourth attempt will only add fees for the consumer and increase the chance that the bank account will be closed. The new payment authorization was likely the result of aggressive debt collection tactics or inappropriate refinancing of a consumer who lacked ability to repay. As written, this proposal could provide an incentive to make a new loan or refinance a loan for the purposes of having the borrower skip a payment, masking the unaffordability of the prior loan.

13.4.6. Second consecutive payment transfer: § 1041.14(b)(2)(ii).

Proposed § 1041.14(b)(2)(ii) defines a failed transfer as a second consecutive failed transfer if the previous transfer was a first failed transfer. The rule clarifies that a "previous" transfer includes one initiated at the same time or on the same day as the second transfer. Comments 4(b)(2)(ii)-1 and -2 illustrate these provisions.

The Bureau seeks comment on what additional provisions may be appropriate to clarify how the prohibition applies when a lender initiates multiple payment transfers on the same day or concurrently and two of those payment transfers fail.[698] We agree with the proposed rule and Comment. There

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[698] 81 Fed. Reg. at 48066.

should be no exception for multiple transactions presented in the same day or in close proximity to a previous payment.

Proposed Comment 14(b)(2)(ii)-3 states that a single immediate transfer pursuant to § 1041.14(d) does not reset the transfer count, and thus if that single transfer fails, the lender may not re-initiate it unless the lender obtains a new authorization. We support that Comment. At that point a consumer has been subject to three failed payment transfers and multiple fees. The lender should not be permitted to attempt a fourth transfer and subject the consumer to even greater harm. (Our other comments on the exception for single transfers are discussed below.)

The Bureau also asks whether the rule should specifically provide that, after a first failed payment transfer, initiating a successful payment transfer or series of payment transfers for a substantially smaller amount (but larger than a nominal amount) tolls the failed payment transfer count at one, rather than resetting it to zero, given that such an amount may not sufficiently indicate that the consumer's account is no longer in distress.

We strongly urge the CFPB to add a provision clarifying that a re-initiated payment in any form (smaller or the same amount) or an intervening payment of a late or returned item fee does not reset the transfer count. If two consecutive regularly scheduled payments fail, the harm to the consumer is the same even if the lender manages to extract some or all of the payment from the consumer in between. The consumer is clearly struggling with inability to repay and with the impact of NSF and overdraft fees. Permitting variations in amounts to reset the count is also likely to result in subterfuge of the proposed protections and to injure consumers. The two failed attempt trigger should apply to partial payments as well as any attempts to collect additional fees, including but not limited to late fees.

The Bureau also seeks comment on what amount may be appropriate for a substantially smaller amount, such as any amount up to 10 percent of the first failed payment transfer's amount, or whether a higher amount threshold up to 25 percent or more is needed to indicate to the lender that the account is no longer distressed. We urge the Bureau to require that only a full, successful, regularly scheduled payment agreed in the repayment schedule be considered sufficient evidence that an account is no longer in distress. If two regularly scheduled payments fail, then smaller payments in between, even if they are 75% or even 100% of the payment amount, do nothing to mitigate the injury to consumers from the leveraged payment mechanism or the unaffordable loan.

Additional discussion of how late payments should be treated is provided in response to proposed §1041.14(c)(2)(iii) below. In addition, as discussed above, we urge the CFPB to define "consecutive" transfer fails to include consecutive months even if there is an intervening successful transfer, no matter what the amount.

13.4.7. Different payment channels: § 1041.14(b)(2)(iii).

Proposed § 1041.14(b)(2)(iii) provides that a failed transfer is a second consecutive failed transfer regardless of whether the first transfer was initiated through a second payment channel. Comment 14(b)(2)(iii)-1 provides an example of this rule using a lender that first submitted an ACH debit and then, after it was returned, processed a remotely created check, with the attempts counting as the first and second failed payment transfer, respectively.

We strongly agree with this provision. As discussed above, payday lenders often require authorization for multiple payment channels. Lenders also use multiple channels to evade consumers' rights under any particular channel. If the lender could simply turn to a different form of payment to evade the protections of the payment rule, the rule would be meaningless.

The Bureau asks whether it should tailor protections to each specific leveraged payment mechanism.[699] We agree with the Bureau that tailoring protections to each specific leveraged payment mechanism would not only increase complexity but would leave consumers vulnerable. A global presentment limit that applies to all types of leveraged payment mechanisms is necessary to protect consumers and prevent evasion.

Lenders across the market accept multiple payment mechanisms. If consistent protections are not applied across all channels, the proposed protections will be too easy to evade.

13.4.8. Exception to the prohibition if the lender obtains the consumer's new and specific authorization for the terms of the withdrawals: § 1041.14(c).

13.4.8.1. In general: § 1041.14(c)(1).

Proposed § 1041.14(c)(1) provides an exception to the prohibition on additional payment transfers after two consecutive failed transfers. The exception permits the consumer to provide a new authorization for recurring payments under the conditions described in § 1041.14(c)(2).

We do not generally object to this exception. However, we have serious concerns about new authorizations that are obtained in connection with a refinancing. We urge, first, that any refinancings preceded by an unsuccessful payment attempt be subject to a presumption of inability to repay, as discussed in section 11.4.2 above. Second, we urge that the failed transfer count merely be tolled, not reset, with a new payment authorization in connection with a refinance, as discussed in section 13.4.4.3 above. If the first payment under the refinanced loan fails, then the lender would be prohibited from additional transfers.

We support Comment 14(c)(1)-1, which makes clear that the requirements of § 1041.14(c)(2) are in addition to, not instead of, any other authorization requirements under applicable laws. Regulation E, for example, has certain requirements for preauthorized EFTs. In addition, as discussed in section 13.6.5 below, we urge the CFPB to require covered lenders to comply with the network rules governing the payment system used.

13.4.9. Contents of the authorization.

13.4.9.1. We support the requirement that a new authorization to use a leveraged payment mechanism include details of the scheduled payment: § 1041.14(c)(2)(i).

In proposed §1041.14(c)(2)(i), the Bureau requires consumer authorization of the core elements of the transfer. We agree and urge the Bureau to only permit further payment collection attempts using a

[699] 81 Fed. Reg. at 48064.

leveraged payment mechanism if the lender obtains the consumer's new and specific authorization for the terms of future withdrawals.[700] This provision contains an exception for re-initiated payments under § 1041.14(c)(2)(ii) and late fees under § 1041.14(c)(2)(iii). Those are discussed below.

We support the requirement that the new and specific authorization include the date, amount, and payment channel of each additional payment transfer authorized by the consumer. The consumer needs to know all three elements in order to try to ensure that the account has sufficient funds available.

Knowing the payment channel is also important in case the consumer wishes to stop payment or exercise other rights in connection with that payment channel. As discussed above, financial institutions have different rules and processes for different types of payments and need to know what channel a payment is coming in through to be able to assist the consumer.

We urge the CFPB to add a comment to this provision that makes clear that lenders cannot include authorization for alternative payment mechanisms. The requirement that the consumer authorize "the specific … payment channel" can only be complied with if one specific payment channel is authorized. In fact, as discussed under section 13.6.2 below, we urge the CFPB to impose this requirement more generally on all lenders that use leveraged payment mechanisms.

We also urge the CFPB to add a requirement that the payment transfer authorization form be clear and readily understandable. That requirement applies when the transfer authorizes a late or returned item fee under § 1041.14(c)(2)(iii)(A) and (B) and for the disclosures that must be provided to the consumer under § 1041.15. But for some reason, the CFPB did not include a clear and readily understandable requirement for the payment authorization form under § 1041.14(c) generally. We believe that such a requirement already applies to EFTs under Regulation E, but it may not for RCCs or some other payment devices. It is essential that the key form that the consumer signs to authorize a payment transfer be clear and readily understandable.

We support Comment 14(c)(2)(i)-1, which explains that the specific authorization terms "must be included in the signed authorization obtained from the consumer …." That is consistent with the requirements for ACH payments under NACHA rules[701] and the general Regulation E requirement that EFT authorizations be clear and readily understandable.[702]

We further urge the CFPB to make clear, as discussed in section 13.6.6 below, that an authorization that does not contain the required terms not only violates this rule but also, if the payment is an EFT, is unauthorized for purposes of Regulation E.

We support Comment 14(c)(2)(i)-2, which explains that the specific date means the month, day and year of each transfer.

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[700] 81 Fed. Reg. at 48068.

[701] *See* 2016 NACHA Operating Rules §§ 2.3.2.2(a), 2.3.2.4; NCLC, Consumer Banking & Payments Law § 5.3.1.2 (5th ed. 2013), updated at nclc.org/library.

[702] **12 C.F.R. § 1005.4(a)(1); Comment10(b)-6 to Regulation E.**

We support Comment 14(c)(2)(i)-3, which explains that a transfer that is larger than the specific amount authorized would violate the prohibition of § 1041.14(b) unless the conditions under § 1041.14(c)(2)(iii)(B) for adding a late or returned item fee are satisfied. We discuss those conditions below.

We strongly oppose Comment 14(c)(2)(i)-4, which states that a payment transfer complies with the requirement for authorization of the "specific amount" even if the transfer is smaller. As the CFPB has observed and we have found among the consumers and constituencies we serve, lenders sometimes change the payment amount in order to evade stop payment orders. Financial institutions typically require consumers to identify the exact payment amount in order to stop payment. Their systems may identify the incoming payment by using that amount.

Permitting lenders to initiate smaller payments that are not specifically authorized also enables lenders to collect unaffordable loans and makes it more difficult for consumers to control their finances. In addition, consumers have a harder time identifying the payments they have made or still owe on a loan if the amounts are different from what they expect.

13.4.9.2. Payment details on open-end lines of credit.

The Bureau asks whether proposed §1041.14(c)(2)(i) sufficiently addresses the specific amount requirement's application in instances where the consumer has credit available on a line of credit, or whether specific provisions should be included to clarify the requirement's application in these instances.

We urge the Bureau to include more details on the specific authorization requirements for any payments scheduled as part of a line of credit. The authorization should list the range of minimum payments assuming minimum and maximum utilization of the credit line. The dates should be listed assuming that the consumer initially fully utilizes the credit line, does not take any further advances, and pays the minimum until the credit line is fully paid off.

For example, if the minimum payment is $25 but it could go as high as $200 if the credit line is fully utilized, then the payment authorization could list the payments as:

> March 1, 2018: $25-$200*
> April 1, 2018: $25-$200*
> [Etc. – with each date listed.]
> *Depending on the outstanding balance.

Providing an example in the comments would be helpful.

13.4.9.3. Application of specific date requirement to re-presented transfers: § 1041.14(c)(2)(ii).

Proposed § 1041.14(c)(2)(ii) permits the lender to re-present a failed transfer once on a different date from that specified in the authorization, provided that it is not a second failed transfer prohibited by § 1041.14(b). We do not object to this narrow exception to the date requirement but stress the importance of the general rule that consumers otherwise must authorize the specific date of the transfer.

13.4.9.4. Special date and amount requirements for late or returned item fees: § 1041.14(c)(2)(iii).

Proposed § 1041.14(c)(2)(iii) permits a lender to initiate a payment transfer to collect a late or returned item fee without including the specific date or amount in the payment authorization. However, the lender may do so only if the consumer has authorized such a transfer through a clear and readily understandable authorization that specifies the highest amount of such fees and the payment channel that may be used.

We support this requirement and believe that knowing the highest possible amount and payment channel are important, for the reasons discussed earlier. We support Comment 14(c)(2)(iii)(A)-3, which requires the lender to assume factors that result in the highest amount possible.

However, we urge the CFPB to permit a fee that varies in amount only if the manner in which the fee will be calculated has been disclosed to the consumer in clear and readily understandable terms, the consumer has agreed to such fees and only if the consumer is notified of the payment transfer to collect the fee as proposed in § 1041.14.

Proposed § 1041.14(c)(2)(iii)(A) and (B) permit a payment transfer that includes the fee alone, or that includes both the original payment amount and the fee, but in either case the consumer must authorizes such transfers through a clear and readily understandable authorization. We support that requirement. In addition, lenders should be permitted to initiate a separate payment for a fee only if the consumer gets advance notice of that debit in the same manner as they do for a regular payment. Otherwise, they would have to add it to the regular payment and provide the notice itemizing the fee.

A successful payment transfer that merely covers a fee should not reset the failure count. The fact that a $10 or $20 fee is successfully deducted from the consumer's account does nothing to prevent—and indeed, exacerbates—the harm of two consecutive regular payments that fail.

13.4.10. Timing, Manner and Memorialization of New Authorizations: § 1041.14(c)(3).

Proposed §1041.14(c)(3) sets forth additional requirements for new authorizations, including the timing of the new authorization and the means of providing the disclosures required under § 1041.15; the general requirement that the authorization be "signed"; and the memorialization of the authorization.

The Bureau seeks comment on all aspects of the proposed approach for obtaining authorizations and, in particular, whether the proposed approach would provide adequate protections to consumers and whether it would achieve the intended goal of reducing lender costs and burdens by being compatible with existing systems and procedures.[703] We generally support the proposed three-step process that requires the notification, authorization in writing, and memorialization of the consumer's authorization for additional payment transfers.

[703] 81 Fed. Reg. at 48070.

13.4.10.1. Provision of payment transfer terms to the consumer; electronic communications: § 1041.14(c)(3)(ii).

Proposed § 1041.14(c)(3)(ii) permits the lender to request a new authorization from the consumer no earlier than the date on which the lender provides the consumer rights notice required by § 1041.15(d). That notice states that the lender is no longer permitted to make withdrawals from the consumer's account and that the lender may contact the consumer about their payment choices going forward.

However, we do not note any requirement that the consumer rights notice be provided *before* the lender requests, or the consumer provides, a new authorization. We assume provision of the notice beforehand is the Bureau's intent, as the timing requirement of this provision would make no sense otherwise. The consumer clearly should be given notice that the lender no longer can debit the account before deciding whether to provide a new authorization. However, nothing appears to prevent a lender from first obtaining the consumer's new authorization and then, afterwards, providing the consumer rights notice the same day. We urge the CFPB to add an explicit requirement that the consumer rights notice be provided before a request for a new authorization (or simultaneously, as permitted under Comment 14(c)(3)(ii)(A)-3). See also the next section regarding the timing of consumer signatures.

Proposed § 1041.14(c)(3)(ii) requires the authorization request to include the specific terms required by § 1041.14(c)(2)(i) (date, amount, payment channel) and, if applicable, the statements required if the transfer includes a late or returned item fee. Comment 14(c)(3)(ii)-2 permits the lender to offer the consumer different options with different dates, amounts or payment channels—either in the initial request or in a follow-up request. We do not object to this Comment, but we urge the CFPB to clarify that the request must be provided in a way that allows the consumer to choose one option, not that gives the lender the authority to initiate the payment in different ways.

The provision gives the lender several options for delivering the authorization request to the consumer, including in writing by mail or in person, without restriction.

Under proposed § 1041.14(c)(3)(ii)(A), the authorization terms may be provided by email if it is in retainable form and the consumer (1) has consented to receive electronic disclosures under § 1041.15(a)(4) or (2) agrees to in the course of a communication *initiated by the consumer* in response to the consumer rights notice. We support the requirement that the request may be provided by email only under those two circumstances. Lenders should not be permitted to use email if it is not clear that the consumer has consented to and can easily access information that way.

We also support the limitation that the authorization terms may be provided electronically only by email in a retainable form, not in another electronic manner such as through a mobile app or text message. The payment authorization terms are a critical document that the consumer must be able to retain, print out, and refer to in the future. Any information available online should remain available for three years. It should also be required to be readable on both full screens and mobile devices.

Comment 14(c)(3)(ii)(A)-2 states that the E-Sign Act does not apply to provision of the terms and statements to the consumer electronically, but that an electronic authorization by the consumer is valid only if it complies with the signature requirements of the E-Sign Act.

The E-Sign Act provides important protections that ensure that consumers are able access and retain electronic communications. E-Sign should be followed for electronic communications and disclosures. While the proposed rule replicates much of the E-Sign Act, it does not require that consumers confirm their ability to receive and view electronic communications. Without that confirmation, all of the important disclosures and notices required through this rule may go to an incorrectly entered email address or an email address that is not actually available to a consumer without electronic access. It is not a difficult step to require consumers to simply click on a link in an email to confirm that they are able to receive information electronically.

However, it is critical that Comment 14(c)(3)(ii)(A)-2 maintains E-Sign Act requirements for the consumer's signature consenting to the receipt of electronic communications (and, later in Comment 14(c)(3)(iii)(A)-1, for the signature on the new payment authorization itself). The protections of the Act are essential to help ensure that the "signature" is valid.

The rule should also be clear that if the lender does not comply with the requirements for electronic communications, then any notices provided in that manner do not fulfill the notice requirements.

Proposed § 1041.14(c)(3)(ii)(B) also permits lenders to provide the terms of the authorization and consumer rights statements orally by telephone, but only if the consumer affirmatively contacts the lender in that manner in response to the consumer rights notice and agrees to receive the terms in that manner. We do not object to this provision but support the narrow exception that is limited to telephone contacts initiated by the consumer. Proposed Comment 14(c)(3)(ii)(B)-1 makes clear that, while the lender may contact the consumer by telephone to discuss repayment options, the authorization terms and consumer rights notices may not be provided orally in that phone call. This helps to prevent an aggressive debt collection call from being used to pressure the consumer into a payment authorization. The lender would either have to provide the information in writing (paper or electronic), or the consumer would have to call back. In general, providing the information in writing is preferable. We also note that the memorialization must be provided in writing.

13.4.10.2. The authorization form should include a right to revoke authorization.

As discussed in section 13.6.5 below, all lenders that use leveraged payment mechanisms should be required to give consumers a right to revoke the authorization through a clear and readily understandable notice in the payment authorization form and memorialization. Even if the CFPB declines to specify requirements for lenders generally, it is essential that any new payment authorization form contain notice of this right and inform consumers of the manner to exercise it. This requirement is already a part of NACHA rules for ACH payments. As discussed below, we also urge that the CFPB require compliance with any applicable network rules.

13.4.10.3. Consumer signatures on and memorialization of the authorization request: § 1041.14(c)(3)(iii).

Proposed § 1041.14(c)(3)(iii)(A) requires that a new payment authorization be signed or otherwise agreed to by the consumer in writing or electronically in a retainable format that memorializes the terms and agreement. For the reasons discussed earlier, we support Comment 14(c)(3)(iii)(A)-1, which makes clear that the E-Sign Act requirements for electronic signatures apply.

The consumer's signature can be obtained no earlier than when the consumer receives the consumer rights notice or the date on which the consumer receives the notice by mail. Here again, as discussed in the previous section, it is not completely clear that the consumer rights notice and payment terms must be provided *first.* The consumer must have some opportunity to read and understand the notice and terms, even if she signs the agreement a few minutes later. The CFPB should make it explicit that the notice and terms must be provided *before* the consumer signs the authorization.

Proposed § 1041.14(c)(3)(iii)(B) permits the consumer to authorize the payments by telephone but only if the lender records the call and retains the recording (which is what the E-Sign Act would require). But in that situation in this proposal, proposed § 1041.14(c)(3)(iii)(C) requires the lender to provide the consumer with a retainable memorialization form (in writing or electronically under the conditions discussed earlier) no later than the date by which the first new payment is initiated. We support Comment 14(c)(3)(iii)(C)-2, which makes clear that the recording of the telephone call does not satisfy the requirement to provide the consumer with a memorialization.

13.4.10.4. Expiration of authorization: § 1041.14(c)(4).

Proposed § 1041.14(c)(4) makes the authorization null and void if either the lender subsequently obtains a new authorization or two consecutive payment transfers fail. We support this provision.

We also urge the Bureau to make the authorization null and void if the lender fails to comply with the requirements of § 1041.14(c). The Bureau has carefully thought through authorization requirements to ensure that consumers understand what they are authorizing. If the lender fails to comply with those requirements, the authorization should be ineffective. Specifying that the authorization is null and void will help consumers to be able to enforce these requirements and will trigger the unauthorized transfer provisions of Regulation E. This will help to prevent evasions and encourage compliance.

13.5. Exemption for Single, Immediate Payment Transfers: § 1041.14(d).

Proposed §1041.14(d) exempts a lender from the consumer authorization requirements of § 1041.14(c) in a narrow situation where the consumer seeks to make an immediate, single payment. We agree with this narrow exception, which will enable consumers to make payments that are due that day without being coerced into a new, broader recurring payment authorization.

As discussed in section 13.3.2 above, we agree with the definition of "single immediate payment transfer" in § 1041.14(a)(2), including the narrow timeframe and the limited payment channels that may be used. These limitations are necessary to prevent evasions.

Proposed § 1041.14(d)(2) permits the lender to accept the consumer's authorization for a single payment "no earlier than" the date on which the lender provides the consumer rights notice or when the consumer affirmatively contacts the lender, whichever is earlier.

In the former situation, as discussed earlier, this provision should require the notice to be provided "before" the consumer authorizes the payment, although it may be done on the same day. We agree with the example in Comment 14(d)-3 of affirmative contact by the consumer, which permits the lender to initiate a payment when the consumer calls after noticing bounced payments on her bank statement.

We support Comment 14(d)-2, which makes clear that a single immediate payment transfer may not be re-presented if it fails. The exception for single transfers is after two previous transfers have failed; if the single transfer then fails as well, the consumer should not be subjected to a fourth failed transfer.

We also agree with the Comment's clarification that the lender may initiate any number of single immediate payment transfers, as long as each one is authorized by the consumer and the other requirements are met. This option gives the consumer more control and the ability to make payments without agreeing to a new recurring authorization.

13.6. Additional Recommendations to Strengthen the Payment Protections.

13.6.1. Prohibit additional transfers after three failed transfers in 12 months and prohibit a second new authorization.

As discussed in section 13.2 above, we urge the CFPB to prohibit additional transfers after only one failed transfer. If the CFPB instead retains the proposal to apply the prohibition only after two consecutive failed transfers, we urge the Bureau also to prohibit additional transfers (absent a new authorization) if the consumer has three failed transfers in a 12-month time span. The only exception would be for single immediate transfer requests.

Despite the protections afforded by the proposals, consumers will still be exposed to the danger of repeat failed transfers. Unless the proposal is strengthened, lenders will be able to use smaller transfers to avoid consecutive failures. Failures might happen only when the biweekly payment comes before rent day. Or the consumer might have frequent payment failures that just do not happen to be consecutive. Any of these circumstances indicate inability to repay and harm from lender use of the leveraged payment mechanism to collect.

Thus, even if there are not two consecutive payment failures, the prohibition of proposed § 1041.14(b) should apply if there have been three payment failures in the previous 12 months. If the lender has made an unaffordable loan and continually injures the consumer through failed payment transfers, there needs to be a limit. The technicalities of whether failures are consecutive should not get in the way of protecting consumers.

In addition, lenders should be permitted only one chance to get a new payment authorization—whether on the original loan or on a refinanced loan. Lenders are likely to use aggressive debt collection tactics to persuade consumers to reauthorize recurring transfers after the payment authorization has been lost. Lenders will push cash-out refinancings as a way to address the unaffordability of the existing loan.

A lender might be allowed one additional bite of the apple, but should not be allowed a second. The dangers of the leveraged payment mechanism, and of inappropriate unaffordable refinancings, require a limit to the lender's ability to undercut the protections of § 1041.14(b).

The only exception should be for single immediate payment transfers. Consumers should be allowed to authorize single payments. They can also set up consumer-initiated recurring payments through their own bank's website. But lenders should not be allowed to continually misuse leveraged payment mechanisms.

13.6.2. Prohibit use of back-up payment channels and use of leveraged payment mechanisms to collect accelerated balances.

As discussed in section 13.2 above, lenders regularly take authorization to use more than one payment channel to collect a payment. Alternative methods are used to defeat consumers' rights to stop payment, to challenge unauthorized payments, or to revoke authorization. The potential use of different channels is also confusing for consumers and makes it more difficult for them to understand their rights.

Lenders should be prohibited from obtaining more than one leveraged payment mechanism or taking a back-up mechanism through another channel. The CFPB has already proposed this requirement in § 1041.14(c) when the consumer provides a new payment authorization after the first has been lost. This requirement should apply generally to the original payment authorization as well.

Obtaining multiple payment authorizations to collect single, regularly scheduled recurring payments and the collection of accelerated balances after a default is not a regular practice in other industries that use payment transfer mechanisms to accept payments. For example, many utilities and telecom providers accept ACH payments, paper checks, credit, or debit payments. Yet these merchants typically provide a straightforward merchant-side revocation process and do not take multiple authorizations that would remain in force even if authorization to use another mechanism were revoked.

We appreciate the CFPB's proposal to impose global presentment limits that apply across multiple payment channels. But the use of multiple channels can still pose problems, as discussed above. For example, an RCC can be used to defeat a stop payment order on ACH payments, even before there have been two consecutive failed transfers. Indeed, if the RCC succeeds, the lender will avoid consecutive failures.

In part, this problem will be addressed if the CFPB takes our recommendation to prohibit additional transfers after even one failure for a stop payment or unauthorized payment. But even then, it will help consumers to understand the terms of their loans and to control their account if they know specifically what payment channel the payment will always be processed through.

13.6.3. Prohibit back-up authorizations for payroll deductions or wage assignments.

The definition of "payment transfer" covered under § 1041.14 does not include payroll deductions or wage assignments. While those leveraged payment mechanisms do not trigger overdraft fees or NSF fees (at least not directly) they do permit lenders to collect unaffordable loans.

The FTC engaged in an extensive rulemaking when it adopted the Credit Practices Rule, explaining why wage assignments are unfair and deceptive and why they should be banned. The FTC found that it was unfair and deceptive for creditors to use wage assignments as a collection device:

The preponderance of the record establishes that consumers suffer substantial injury when wage assignments are used as a collection device. Wage assignment, unlike garnishment, occurs without the procedural safeguards of a hearing and an opportunity to assert defenses or counterclaims. The use of wage assignments causes interferences with employment relationships, pressure from threats to file wage assignments with employers, and disruption of family finances. Wage assignments are particularly harmful because they cause injury to consumers who may have valid reasons for nonpayment.[704]

However, it permitted payroll deduction plans that authorize as series of deductions "as a method of making each payment."[705]

Unfortunately, the FTC also permitted wage assignments that are revocable at the will of the debtor. It intended to enable the debtor "to stop the wage assignment before injury occurs."[706] The FTC did not anticipate that wage assignments buried in fine print would be used as the same terrorizing collection devices that it was banning rather than as a convenient and voluntary way of repaying a loan.

Some lenders take broad authorizations that could allow them to collect from any future employer, in ways that consumers do not anticipate. For example, the Payday Loan Store of Illinois, Inc. includes this language in fine print buried in its contracts:

To secure payment of your loan and interest on your loan at the rate shown and subject to the provisions of applicable law, you hereby assign, transfer and set over to us wages, salary, commissions and bonuses due or subsequently earned from your present employer(s) for a period of three (3) years from the date of this wage assignment and from any future employer within a period of two (2) years from the date of this wage assignment. If you are in default of your agreement, we will have the right to collect the amount due from your present or future employer(s). You may revoke this assignment of Wages at will with written notice to us. This assignment shall remain effective as to any borrower who does not revoke this wage assignment.[707]

Clearly, this is a collection device of the type prohibited by the FTC, not a convenient method of making the loan payments.

While the CFPB may choose not to apply the same protections to payroll deductions that it is requiring for other leveraged payment mechanisms, it should prohibit use of *any* leveraged payment mechanism—including any form of payroll deduction or wage assignment—as a back-up method after a first failed transfer. These wage assignments pose all of the dangers that the FTC outlined in its rulemaking and permit lenders to collect unaffordable loans.

Permitting wage assignments as a back-up mechanism would open up a huge loophole. Many lenders would put those clauses into their contracts and threaten to use them—interfering with borrowers' employment—if the consumer attempts to revoke authorization of another payment method. The controls that the CFPB is putting in place after two failed transfers will provide little protection, as lenders will just go after consumer's wages through their employers.

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[704] 49 Fed. Reg. 7740, 7757 (Mar. 1, 1984).
[705] 49 Fed. Reg. at 7760.
[706] 49 Fed. Reg. at 7760.
[707] Contract on file with Consumer Federation of America.

13.6.4. Strengthen compliance with the EFTA ban on compulsory use.

The EFTA and Regulation E prohibit lenders from requiring consumers to repay credit through preauthorized EFTs ("PEFTs"). But as the CFPB has observed, covered lenders use a variety of tactics to get around that ban and to effectively require electronic repayment. When a lender is able to steer the vast majority of its borrowers into repaying automatically, the lender's incentive to underwrite appropriately is considerably reduced, as the CFPB has found. Lenders that do not reply on automatic repayment as part of their underwriting regime, like banks that offer mainstream credit cards, do not typically engage in manipulations to steer consumers towards automatic payments.

We have several suggestions to ensure that consumers have a meaningful choice of how to repay covered installment loans and to prevent lenders from evading the ban on compulsory of use of preauthorized EFTs. Our view is that some of the recommendations below are already what Regulation E requires, but lender practices do not reflect that. Ideally, the CFPB will clarify and enhance Regulation E for all parties in a future rulemaking. For present purposes, the CFPB could limit coverage to covered lenders.

1. Prohibit lenders from making PEFTs the default payment method from which the consumer has to opt out. We believe that this is already the law, and the CFPB can clarify this in a comment and cross-reference to Regulation E. The CFPB should also make clear that PEFTs are being used inappropriately as a default method if the loan application does not give the consumer a clear, readily understandable, and equally easy choice of other payment methods.
2. Prohibit use of RCCs or RCPOs as the sole alternative to PEFTs. RCPOs are (or should be viewed as) EFTs, and thus compulsory use is still required if they are the only alternative. The CFPB also has the authority to prohibit use of RCCs to evade the ban on compulsory use.[708]
3. Until they can be banned (see section 13.6.8 below), cover both RCCs and RCPOs under Regulation E.
4. Prohibit "discounts" that are so large as to be coercive. Any price disparity that increases any payment by more than 10% should be viewed as coercive.
5. Prohibit nonmonetary incentives, such as delayed loan disbursement. Regulation E permits a "monetary" incentive, but there is nothing in Regulation E that permits nonmonetary incentives, and the CFPB could make that clear. For the desperate borrowers who take out high-cost loans, any delay in loan disbursement is coercive.
6. Extend the compulsory use ban to single payment loans.
7. Make clear that consumers have the right to revoke authorization of PEFTs upon no more than 3 business days' notice, as discussed in the next section.

13.6.5. Make clear that consumers have a right to revoke authorizations and require compliance with network rules.

[708] For a longer discussion of the reasons that remotely created checks and remotely created payment orders are outdated and should be prohibited for consumer transactions, see Letter from NCLC et al. to Chairman Ben Bernanke, Board of Governors of the Federal Reserve System (Dec. 13, 2013), http://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/rcc-fed-comments12132013.pdf.

The CFPB has published importance guidance for consumers about their right to stop lenders and other merchants from using preauthorized EFTs to debit their accounts, with model forms for revoking payment authorization. While the EFTA does not provide an explicit right to revoke authorization of preauthorized EFTs, that right is implicit in the Commentary to Regulation E, and some courts have agreed that consumers have that right.[709]

NACHA rules provide an explicit right to revoke authorization of preauthorized ACH transfers. The right to revoke and the manner to do so must be part of the authorization form itself.[710] Preauthorized payments can also be made by a debit card through the card networks (Visa, MasterCard, American Express and Discover), and those payments are covered by Regulation E rules for preauthorized transfers.

A right to revoke authorization for remotely created checks is less clear. Remotely created payment orders (RCCs that were never printed as payment checks and were presented as electronic images) should be covered by Regulation E.[711] RCCs may be as well if the payment began with an authorization that the consumer provided electronically.[712] But regardless of the Regulation E coverage, a right to revoke authorization of RCCs and RCPOs is even more important than for ACH debits and other EFTs, where rights and bank processes are clearer.

To implement the CFPB's guidance, clarify rules for both consumers and lenders, and protect consumers from the problems discussed earlier, the CFPB should require that any leveraged payment mechanism provide the consumer with a right to revoke authorization. The right should be described in the authorization form as under NACHA rules.

The consumer should have a right to revoke authorization upon giving the lender three business days' notice. Lenders should not be allowed to specify inordinately long notice periods that defeat the right to revoke authorization.

Consumers should be allowed to communicate their revocation by mail, by email, by delivering a written notice, and through any other written communication channel that the lender uses to communicate with the consumer. At a minimum, a mail and email address should be provided in the payment authorization memorialization.

In addition, this rule should specifically require all lenders to comply with any applicable network rules for the payment channel they are using. Thus, they would be required to comply with NACHA rules, Visa rules, or any other applicable rules. Making this requirement part of this regulation is important,

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[709] *See* NCLC, Consumer Banking & Payments Law § 5.8.4.2 (5th ed. 2013), updated at nclc.org/library.
[710] "An authorization must: . . . (c) provide that the Receiver may revoke the authorization only by notifying the Originator in the time and manner stated in the authorization. For a Single Entry scheduled to occur in advance, any such revocation right shall afford the Originator a reasonable opportunity to act on such revocation prior to the initiation of the Entry." 2016 NACHA Operating Rules § 2.3.2.3(c); NCLC, Consumer Banking & Payments Law § 5.3.7.2.3.
[711] NCLC, Consumer Banking & Payments Law § 5.1.3.8.4.
[712] S*ee* Featherstone v. GFG Loan Co., 2000 WL 294119 (N.D. Ill. Mar. 17, 2000) (payment originated with the promissory note, not the check, and thus payday loan agreement sufficiently ambiguous as to whether it authorizes transfers in violation of EFTA that court denies lender's motion to dismiss); Taylor v. Halsted Fin. Servs., Ltd., 2000 WL 33201925 (N.D. Ill. Jan. 13, 2000) (granting class certification of claim that payday lender violated EFTA by conditioning credit on agreement that writing of check authorized electronic debits).

because the rules may not be privately enforceable, and it also may not be clear of the CFPB's authority to enforce them. Certainly, any use of a payment channel without complying with the rules for that payment channel would be unfair, deceptive and abusive.

13.6.6. Make clear that use of leveraged payment channels without complying with applicable authorization requirements results in an unauthorized payment and abusive debt collection practice.

If a lender fails to comply with the authorization requirements for a payment channel—including those set out in this rule, in other laws, and in network rules—then any purported authorization should be null and void and any resulting payments should be deemed unauthorized. This rule is necessary to provide incentives for compliance and to prevent evasions.

If the payment is an EFT, then the Regulation E provisions governing unauthorized transfers should apply. If the payment is a check, then UCC rules for unauthorized checks would apply.

In addition, an attempt to collect a payment by use of an unauthorized payment channel should be an abusive debt collection practice. If a third party debt collector does so, the payment initiation should be a violation of the Fair Debt Collection Practices Act. If it is a first party lender that makes the unauthorized payment, then it violates the Dodd-Frank Act (as well, hopefully, as future rules the CFPB will promulgate governing first party creditors).

13.6.7. The Bureau's proposed limit on presenting payments will not protect consumers whose transactions are covered through overdraft.

Limiting the re-presentment of payments will take some steps to reduce the high and unpredictable fees that consumers face when payday and car title lenders have unfettered access to their checking accounts to collect payments. However, the Bureau's proposed payment rules are only effective for those borrowers for whom the payment attempt failed. They do not protect borrowers whose payments succeed only because the bank paid the transaction through overdraft, likely charging the consumer a fee the equivalent of an NSF fee as a result.

This important fact supports the stronger rules we have urged above. We also urge the Bureau to move forward with a separate rulemaking to rein in unfair and abusive overdraft fee practices.

13.6.8. The use of remotely created checks and remotely created payment orders presents a heightened, unavoidable risk that cannot be adequately addressed under the proposed rule and should thus be prohibited for covered credit transactions.

Remotely created checks (RCCs) and remotely created payment orders (RCPOs) should be prohibited entirely for covered credit transactions, and, as we have stated in previous comments, in all consumer transactions.

In supplemental comments submitted by consumer groups in response to the Federal Reserve Board and the Consumer Financial Protection Bureau proposed changes to Regulation CC, we noted that RCCs and RCPOs are used by payday lenders (storefront, internet and tribal), internet scammers, and merchants in high-risk industries such as gambling advice, psychic readings, pyramid sales, terminated merchants, pawn brokers, bail bondsmen, debt reduction services, and loan modifications. We also noted widespread use of RCCs and RCPOs to evade consumer protections, to compromise consumers' control over their bank accounts, and to facilitate unlawful, fraudulent, unfair, deceptive and abusive practices.

Much of the continuing use of these payment devices is due to inertia, and safer electronic payment systems can substitute in these situations with lower risks. We support the FTC's rule banning the use of RCCs and RCPOs in transactions covered by the Telemarketing Sales Rule (TSR) and note that the FTC has outlined a compelling case describing the pervasive misuses of RCCs and RCPOs that justify a ban in telemarketing sales. However, the FTC's rule does not apply to transactions that do not involve a telephone call and do not fall under the TSR.

When used as a leveraged payment mechanism for covered credit transactions, RCCs and RCPOs should be banned entirely because they are too easy to use to debit bank accounts without consumer consent. They also lack the consumer protections available for other electronic payment methods and operate through the check clearing system, which lacks the systemic controls to police fraudulent and unlawful use. RCCs and RCPOs are also unnecessary in light of the wide availability of modern electronic payment systems. There is compelling evidence that their usefulness for a handful of legitimate uses is outweighed by their risks and urge the Bureau to prohibit to use of RCCs and RCPOs for loans made under this rule.

13.7. Notification of Upcoming Payment Transfer Attempts and the Consumer Rights Notice Provide Valuable Information and Reduce the Likelihood of Harm From Failed Payment Transfer Attempts.

The Bureau seeks comment on proposed §1041.15(a) on its approach to the form of disclosures and notification of upcoming payment transfer attempts. We agree with the Bureau's determination that notification of upcoming payment transfer attempts is reasonable and appropriate. This notification is particularly important given the limited effectiveness of the protections described in proposed §1041.14(b) in light of bank overdraft practices or if the lender uses remotely credited checks or payment orders (which we urge the Bureau to prohibit for the purposes of making payments on covered credit). Advance notice of a payment transfer is also especially important for open-end credit, where the amount due may be less clear to the consumer.

13.7.1. We support the general form of disclosures: § 1041.15(a).

We generally support the requirements under proposed § 1041.15(a) for the form of the disclosures of upcoming payment attempts and the consumer rights notice. In particular, we support the requirement that disclosures be clear and conspicuous; be in writing unless the consent requirements for electronic communications are satisfied; be retainable; have segregated information; be in machine readable text; use the model forms; and be permitted in foreign languages.

The segregation requirements are especially important. Lenders should not be permitted to obfuscate the notices by combining them with other information.

We urge the CFPB to require the disclosures to be provided in a foreign language (and also in English) if the lender uses a foreign language to communicate with the consumer in oral, email, or written contacts.

With respect to electronic communications, we especially support the consumer consent requirements, the requirement that email be one of the electronic options, that consumers have the right to revoke consent, and that consent be automatically revoked if the lender receives notice that consumer is unable to receive the disclosures (i.e., if an email is returned). We also support Comment 15(a)(4)(i)(A)-1, which requires that the consumer pick a particular electronic method, and does not allow lenders to take general consent for any electronic method the lender chooses. Borrowers can benefit from the timely delivery of disclosures available through electronic means, but we support the proposal that electronic communications be an option, not a requirement. Borrowers who prefer paper communications must have that choice. See also our discussion in section 13.4.10.1 and 13.4.10.3 above about electronic communications.

The Bureau seeks comment on whether additional requirements should be required for notices that are sent by text message or other mobile application.

We recognize that both lenders and consumers may prefer to provide and receive notifications by text message, but messages sent in this manner are more difficult to retain. We urge that, in circumstances where notices are provided by text or other electronic delivery method where the entirety of notice cannot be displayed, that the notice, in its entirety, be provided at a persistent URL that is available to the consumer for at least three years after the final scheduled payment of the loan. As part of the notice, borrowers should be notified that they have the option to print the entirety of the notification from the URL or email, send the disclosure by email, or request that it be mailed at any time, up to three years after the final scheduled payment of the loan.

We particularly support Comment 15(a)(4)(ii)(A)-1, which makes clear that consumers may revoke consent for electronic communications through any reasonable means, including orally. We have often seen lenders who make it quite easy to consent to electronic communications but impose obscure or cumbersome methods for revoking consent. Consumers should be able to easily choose how best to receive information.

We urge the CFPB to require lenders to provide a memorialization of consent to electronic communications and to include both a telephone and email address that can be used to revoke consent. We also urge the CFPB to require lenders to make it simple for the consumer to respond in the same manner that the lender provides the memorialization, such as by responding to an email or text message. Lenders should not be permitted to use no-reply emails or texts.

13.7.2. The proposed terms of payment notices provide important information in light of severe harm leveraged payment mechanisms can cause: § 1041.15(b).

The Bureau seeks comment on proposed §1041.15(b), which describes the information required in and timing of notifications of upcoming payment transfer attempts. Advance notification of an upcoming payment attempt is necessary to increase the likelihood that consumers will be informed about upcoming payments and have an opportunity to avoid harm.

As previously noted, 6% of first payment transfer attempts and 10% of second payment transfer attempts result in an overdraft fee.[713] In these circumstances, payment transfers result in a negative balance, high and unpredictable fees and additional hardship and do not trigger the prohibition on future payment transfers in §1041.14(b). Likewise, the Bureau has recognized that consumers seeking to revoke authorization or block a payment presented as a remotely created check or payment order would be unable to gain access to the check number—information necessary to successfully process the request by many financial institutions. Providing advance notice of an upcoming payment, in addition to the necessary information to block any payment that a borrower believes is unauthorized or to change their payment transfer preferences, is critical to provide the borrower even a chance at avoiding the harm of an unaffordable loan or payment.

We support the timing requirements of proposed § 1041.15(b)(3) for both mail and electronic delivery. Both a minimum and maximum number of days before the payment are appropriate so that the notice is timely but the consumer still has time to take action.

We support the content requirements of proposed § 1041.15(b)(4), including an identifying statement, the date of the upcoming payment attempt, the payment amount, the consumer account (truncated if necessary to protect borrower's privacy), loan identification information (truncated if necessary to protect borrower's privacy), payment channel, check number (including if an RCC or RCPO is used), annual percentage rate, payment breakdown, lender name and contact information, and a description of any unusual attempts, for example, if the payment transfer attempt will include any additional fees authorized under proposed §1041.14. We note that a check number for an RCC or RCPO is especially important. It is also important to remind consumers of the APR that they are paying on the loan, as that information is often obscured, and consumers should be aware of the APR should they consider reborrowing or refinancing.

The special warning for varying payments is also important. For open-end credit, where there may be no regularly scheduled amount, we urge the CFPB to require use of the varying amount notice any time the payment is different than the previous one.

We urge the CFPB to prohibit use of different payment channels rather than allowing the lender to simply notify the consumer of a change. As discussed above, different payment channels provide different sets of protections for borrowers, and lenders should not be permitted to change the channel at will to evade those protections or confuse the borrower. While we support proposed Comment 15(b)(4)(ii)(E)-1 (which requires disclosure of the payment channel) if the CFPB permits multiple payment channels, the example itself demonstrates the complexity of permitting different payment channels.

We urge that Comment 15(b)(4)(iv)(D) be revised to require a breakdown of any fees rather than an aggregated amount. Consumers should be informed about the components of each payment, for example, how much of the payment is a late fee and how much is the finance charge.

[713] "Online Payday Loan Payments." Washington, D.C.: Consumer Financial Protection Bureau, April 2016. http://files.consumerfinance.gov/f/201604_cfpb_online-payday-loan-payments.pdf.

When a returned payment is re-initiated, the CFPB should propose simpler language than the technical term "re-initiate." For example: "We are depositing your check a second time because it bounced the first time."

We also urge that some additional information be included in the payment notice. It would be helpful for the payment notices to inform consumers of the previous balance, last payment, and new balance on the loan. Also, instead of the term "principal" in the model forms, a more understandable term would work better, such as "balance." For example:

Previous balance:	$500.00
Last payment:	$ 50.00 ($47.02 interest and $2.98 principal)
New balance:	$497.02

Including this information could help consumers to understand how their payments are being applied to see the dangers of high-cost loans where payments do not reduce principal. While the proposed payment breakdown is intended to achieve this aim, this additional information may aid consumers' understanding.

The Bureau seeks comment on whether information should be provided without any advance notice of an upcoming payment transfer attempt. We do not believe so. Timely notice before each payment will best ensure that consumers know what payments to expect from their account. We oppose any exemption to the protections provided in proposed §1041.14 and §1041.15 for any subset of lenders covered by the scope of the rule.

The Bureau also seeks comment on whether less frequent notifications would provide a similar level of protection. Notice of upcoming payment should be provided in advance of all regularly scheduled payments in order to most appropriately address the harm outlined in the section entitled Market Concerns – Payments. For financially distressed consumers, notice before every payment is a reasonable and necessary protection.

13.7.3. Limited exemptions to the notification requirement are acceptable in limited circumstances: § 1041.15(b)(2).

We do not object to the limited exceptions to the payment notice requirements for loans made under § 1041.11 or 1041.12; for the first payment after consumer consent to a new authorization under § 1041.14(c); or for a single immediate payment request. However, those are the only exceptions that should be allowed.

We oppose restricting the notification requirement to unusual payment transfer attempts, such as upcoming payments that may vary in amount as a result of an accrued late fee or additional principal payment. We also oppose limiting notification of upcoming payment transfers to circumstances where a payment amount varies outside of a previously specified range. Providing a range does not give consumers the specific information they need about the upcoming debit.

13.7.4. The electronic short notices should be expanded: § 1041.15(c) and (e).

Proposed § 1041.15(c) and (e) permit the lender to provide truncated information in an email, text or other electronic delivery channel when the consumer consents to electronic delivery of the payment notice and consumer rights information notice. The electronic short forms omit much valuable information but include a link to the full notice.

Consumers are more likely to view the short notice than to click through and view the long notice. So it is essential that as much information as possible be provided in the short form.

If the consumer has consented to receive communications by email, short notices generally should not be permitted. The notices are not long, and a full notice can easily be provided in email. At most, the lender should be permitted to omit sensitive personal information like account numbers that might not be safe to send by email.

If the consumer has consented to receive communications by text message or through a similar medium that does not handle long content well, the short forms are acceptable, but the Bureau should add this sentence form the long notices: "Contact Willow Lending at 1-800-555-5555 if you have questions or wish to stop this withdrawal."

13.7.5. The consumer rights notice provides important information: § 1041.15(d).

We support the requirement for a consumer rights notice as required under proposed § 1041.15(d). We support the proposed timing, as well as the content requirements: identifying statement; last two attempts were returned; identification of consumer account; loan identification; federal law prohibition; breakdown of information about previous unsuccessful payment attempts; and CFPB information.

14. INFORMATION FURNISHING REQUIREMENTS TO REGISTERED INFORMATION SYSTEMS ARE CRITICAL TO THE RULE AS A WHOLE: § 1041.16

14.1. Overview.

Section 1014.16 outlines the information that lenders must furnish to registered information systems (RIS) for the purposes of determining a consumer's borrowing history to enable compliance with the proposed rule. The requirement to report to the RIS is critical to enable compliance with provisions addressing loan flipping restrictions and ensuring the borrower's ability to repay without reborrowing. The reporting will also provide data on a borrower's loan performance (like delinquencies, defaults, and collections activity) on covered loans that lenders should be required to consider in making a reasonable ability-to-repay determination.

The recommendations we provide below are made with those functions of the reporting in mind:

- We support requiring lenders to report covered loan information to every registered information system.
- The CFPB should mandate that specific consumer identifying information be furnished and mandate strict matching criteria.

- The information the proposal requires be reported is generally appropriate but should be expanded consistent with existing state databases.

14.2. Lenders Should Be Required To Furnish Covered Loan Information To All Registered Information Systems: § 1041.16(a)-(b).

Proposed § 1041.16(a) requires lenders to furnish information about covered loans to all RISs. We support the proposed reporting requirements. As discussed at 15 below, we encourage the CFPB to host the covered loan database; if it does not, the best alternative is to have multiple RIS to whom lenders are required to furnish information.

Having multiple RISs to which lender could choose to report would make the RISs more responsive to the desires of payday lenders, creating greater incentives to please lenders than to properly do their jobs. We base our concerns on very clear historical precedent, because giving furnishers the choice of CRA is the current situation with credit reporting and the nationwide CRAs. This has led CRAs to develop procedures and systems to accept furnisher's information uncritically and not to respond to problems raised by consumers. We fear the same will occur with RISs unless the lenders are mandated to report to all of them.

Permitting lenders to furnish to only one RIS would also make use of the RIS's more cumbersome, as a lender would need to obtain reports from all RIS's to make sure that the information was complete. Or, the RIS's would need to complete data sharing agreements.

14.3. The CFPB should mandate that specific consumer identifying information be furnished and mandate strict matching criteria: § 1041.16(c)(1)(ii).

The Bureau has asked for comment about whether proposed § 1041.16(c)(1)(ii) should require particular items of identifying information to be furnished about covered loans. We believe it clearly should. The CFPB should require lenders to provide the borrower's full name, address, phone number, date of birth, and most importantly, full Social Security Number (SSN). More importantly, CFPB should mandate a set of strict matching criteria that uses this information to properly match borrowers to the correct file at a RIS.

As the CFPB well knows, one of the thorniest issues in credit reporting, and consumer reporting generally, is how to appropriately match a consumer to the correct CRA file based on identifiers. Consumer groups have long criticized the nationwide CRAs for having overly lax matching criteria, resulting in the phenomena of "mixed files" and "merged files," when the credit information relating to one consumer is placed in the file of another consumer or the files of two consumers are merged together when a credit report is produced. Mixed and merged files are two of the most devastating types of errors that can occur in credit reporting.[714] They occur largely because the nationwide CRAs do not use sufficiently rigorous criteria to match consumer data precisely.

Mostly importantly, they do not match information based on all nine (9) digits of the consumer's SSN. Instead, they will match information based on seven of nine (7 of 9) digits of an SSN if the consumers' names are also similar. Thus, in addition to requiring lenders to provide full SSN and other critical

[714] For a discussion of mixed and merged files, *See* National Consumer Law Center, Fair Credit Reporting § 4.3.3 (8th ed. 2013), *updated at* www.nclc.org/library.

identifiers to a RIS, the CFPB must mandate the type of matching criteria that a RIS must use, most critically full SSN information.

14.4. The Information To Be Reported Should Be Expanded: § 1041.16(c)

14.4.1. Overview.

The Bureau approaches the reporting requirements in three parts: information required to be provided at loan consummation, information required to be provided while the loan is outstanding, and information required to be provided once the loan ceases to be outstanding. The Bureau seeks comments on a range of issues related to the substance and timing of these requirements. We address each of these three time periods in turn, and then offer a list of data points we urge be required on each reported loan, most of which lenders already report in over half of states with existing database requirements.

The Bureau proposes to exempt from RIS reporting requirements longer-term exemption loans made under §§ 1041.11 and 1041.12. We support the Bureau's proposal that that longer-term exemption loans be required to report to either the RIS or credit reporting agency so that covered lenders subject to ability-to-repay determinations will be able to see borrowing history on longer-term exemption loans.

14.4.2. Information required at loan consummation: §1041.16(c)(1).

The Bureau proposes the following information be reported at time of loan consummation for all covered loans subject to RIS reporting requirements:

- a unique loan identifier;
- a unique customer identifier;
- identification of whether the loan is short-term, longer-term, or longer-term balloon payment;
- whether a short-term loan is subject to the ability to repay requirements or is a short-term exemption loan; and
- whether the loan is a longer-term loan subject to the ability-to-repay requirements.

We support requiring these elements be reported but urge that the Bureau require the information underlying these determinations be reported as well. For example, lenders should include the date of consummation, contractual loan due date, and amount and timing of payments, to determine whether the loan is a short-term or long-term loan—not just check a box indicating whether it is one or the other.

For covered short-term loans only, the proposal would require reporting the loan consummation date. This requirement should extended to all loans required to be reported.

For short-term exemption loans only, the proposal would require reporting the principal amount borrowed. This requirement should be extended to all loans required to be reported.

For closed-end loans, the proposal would require reporting the fact that the loan is closed-end, the date that each payment is due, and the amount due on each payment. We support these reporting requirements, and urge that the Bureau also require reporting at consummation the loan consummation date, the total number of payments required, and loan due date. We also support the proposed requirement that lenders update the RIS if the lender changes the due date, loan payments, and amount of each payment.

For open-end credit, the proposal would require reporting the fact that the loan is open-end, the credit limit, the date on which each payment is due, and the minimum amount on each payment. We support these proposed reporting requirements while urging also the loan consummation date be required.

The Bureau seeks information on whether, upon the effective date of the furnishing requirements, loans outstanding at the time should be required to be added. We strongly urge so. This is particularly critical for any consumer protection focused on limiting a borrower's days of indebtedness in a 12-month period. This requirement is feasible. At the time Kentucky's database requirement became effective in April 2010, the state required the uploading of outstanding transactions made prior to the database, which were noted in the annual report as "historical transactions." [715]

The Bureau proposes that the information provided at the consummation of the loan be provided "no later than the date of consummation or as close in time as feasible after that date." To ensure the accuracy of RIS reports and the determinations that rely on them, we urge the Bureau to eliminate the "as close in time as feasible" approach.

14.4.3. Information required while a loan is outstanding: § 1041.16(c)(2).

Proposed § 1041.16(c)(2) would require lenders to furnish any information previously furnished "within a reasonable period" of the event that causes the information previously furnished to be out of date. The Bureau seeks comment on whether lenders should have a more flexible timing requirement for reporting information while the loan is outstanding. We oppose anything more flexible than the timing requirements proposed for the information to be provided at the time of the loan consummation. Specifically, the information should be furnished no later than the date on which the changes to the terms of the outstanding loan are made.

The Bureau seeks comment on whether it should require any additional information about a loan while it is outstanding, such as information about payments made on the loan. We urge the Bureau to require payments made on the loan, along with principal and charges still owed after each payment, the number of days that a borrower is delinquent on a payment, and whether the loan is refinanced or renewed. If refinanced or renewed, the lender should also report (1) the amount of principal paid down on the original loan at time of renewal, (2) the amount of principal owed after renewal, and (3) all the other requirements for a loan at consummation. These are important to enable compliance with provisions addressing repeat flipping of longer-term loans, particularly when little to no principal has been paid down. Further, they are important to the lender's ability-to-repay determination more broadly.

[715] See for example, Commonwealth of Kentucky Deferred Presentment Transaction System, Report on Kentucky Payday Lending Activity for the Year Ending December 31, 2010, Prepared for the Commonwealth of Kentucky Department of Financial Institutions, by Veritec Solutions, LCC.

14.4.4. Information required when loan ceases to be outstanding: § 1041.16(c)(3).

Proposed § 1041.16(c)(3) would require the following be furnished when a loan ceases to be outstanding: (i) the date on which the loan ceased to be outstanding, and (ii) for a closed-end loan: (A) whether all amounts owed in connection with the loan were paid in full, including the amount financed, charges included in the total cost of credit, and charges excluded from the total cost of credit; and (B) if all amounts were paid in full, the amount financed and charges included in the total cost of credit but excluding any charges excluding from the total cost of credit.

The Bureau's reporting requirements for loans ceasing to be outstanding are significantly lacking.

First, the requirements above should be retained but strengthened as follows:

- If a loan is paid in full, charges excluded from the total cost of credit should still be required to be reported.
- Amount financed and charges included and excluded from the total cost of credit should be reported separately.
- The proposal should clarify that charges not included in the total cost of credit include any fees associated with late payment on the loan, including both late fees and returned item fees.

Second, critically, the above requirements for short-term loans, must apply to longer-term loans as well.

Third, the information should include information about delinquency, defaults, or charge-offs. All of these are highly relevant to a consumer's borrowing history. We urge the following for both short- and longer-term loans:

- the date on which a borrower became delinquent,
- the date on which the lender determined the loan to be in default, and
- the date on which the lender charged-off the loan.

This data is important to an ability-to repay determination generally. It is also important to protections against unaffordable longer-term refinancings, including loans made by different lenders, as we propose in section 11.

Finally, the Bureau should require that lenders report collections activity to the RIS, such as the date in which collections activity begins. This includes a record of any failed payment transfer, particularly those transfers that trigger a prohibition on further payment transfer attempts and the reauthorization requirement. While other lenders do not have obligations under § 1041.14 or § 1041.15, the fact that payment authorization has been revoked is critical information of which they should be aware.

With respect to timing, we again urge that a loan that ceases to be outstanding should be reported no later than that date, with no vague "as soon as feasible" option.

14.4.5. Additional recommended required information, generally supported by feasibility at state level.

The Bureau should require a standard set of fields for each loan transaction, as many states already require for participation in a state-level compliance reporting system or database. In addition, as noted above, raw data should be collected in favor of information that lenders could more easily inaccurately report. For example, lenders should be required to provide the loan consummation date and the loan due date, as well as the size and timing of each payment, to determine whether it is a short-term or long-term loan—rather than as currently proposed which simply requires the lender to indicate whether it is short-term or longer-term.

Towards this end, we would recommend that the following variables be furnished for each covered loan required to be reported in the RIS. Notably, most of this information is already provided by lenders to state regulators in more than half the states in which payday lenders make these high-cost loans. While these requirements exist in varying combinations depending on the state, they evidence that lenders have the ability to provide this information for compliance and enforcement purposes.

- Unique customer identifier
- Unique loan identifier
- Date transaction entered (if a renewal or refinance, date renewed/refinanced, with an indicator that it is a renewal/refinance of a previous loan)
- Whether the loan is open-end or closed-end
- For open-end loans, each periodic assessment of ability-to-repay and the outcome of that determination
- Whether the loan has a balloon payment
- Contractual due date
- Loan amount
- All-in APR at time of transaction
- Interest
- Charges for ancillary products by type of product charged (e.g., no-file insurance, car club, credit insurance, life or disability insurance)
- All other charges included in total cost of credit
- All other charges excluded in total cost of credit
- Number of loan payments due at time of origination
- Amount needed for pay off
- Date loan paid off
- Number of loan payments made at time of repayment
- Amount paid to pay off loan
    - Loan amount
    - Charges included in total cost of credit
    - Charges excluded from total cost of credit
- For a renewal or refinance, the amount of principal owed at time of the renewal or refinance.
- Date loan became delinquent
- Date loan put into default
- Date loan charged off
- Date car repossessed
- Charges collected for late fees, default fees, and NSF Fees
- Collection activity
- Failed payment collection attempts, particularly those that result in revocation of payment authorization.

14.4.6. CFPB and State enforcement agencies should have access to all RIS data.

We urge that both the CFPB and State enforcement agencies have full access to the RIS data. This is essential to robust enforcement of the rule.

15. REGISTERED INFORMATION SYSTEMS: § 1041.17.

15.1. Overview.

Section 1041.17 establishes a new category of consumer reporting agency (CRA) called registered information systems (RIS). These would be private companies that would serve as repositories of information regarding covered loans. The Bureau would be responsible for registering and supervising them, but would not be contracting with them.

We strongly support the need for the function the RISs serve in the proposed rule, and if the Bureau does not take on that function itself, we support the RIS approach. However, we do urge the CFPB to consider housing the database itself or having a contractor designated by the Bureau to house the information. The CFPB asks about such an alternative in the Supplementary Information.[716] Under this alternative, lenders would be required to furnish information to the Bureau or its contractor and to obtain a report from the same source as well. We support this approach because we believe it would give consumers better protections and be less prone to error.

Decades of experience with the nationwide CRAs and specialty CRAs has taught us that, when it comes to private companies, the interests of consumers are always ultimately subsumed to the interests of profits. The nationwide CRAs have consistently taken actions to favor furnishers and users of credit reports over consumers, because the former are their customers.[717] Thus, the nationwide CRAs automatically defer to furnishers when a consumer disputes an error in a credit report, like a judge who always rules for one side.[718] The best way to avoid these problems is to make the database a public function.

Indeed, at a conceptual level, consumer reporting is inherently a public good, serving the role of a public utility, and any new systems should be constructed as such. While the evolution of credit reporting in this country resulted in private companies taking on this function, we have an opportunity to start from scratch and build a better system. We urge the CFPB to consider taking on this role itself (via a contractor), much as the 14 states with covered loan databases have done.

Some industry members have raised the idea of having one main registered information system, with RIS reports distributed by resellers. Unless this RIS is fulfilling the role as a government contractor, we oppose this idea. Giving any one company a monopoly of the RIS function would place far too much power in the hands of one CRA. We well know the perils and harms when three companies (aka the three nationwide CRAs) have an oligopoly over critical databases necessary for the credit system. The lack of care, accuracy, attention to consumer interests, and level of consumer harm from the Big Three

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[716] 81 Fed. Reg. at 48090.

[717] For a discussion of the various problems with the nationwide CRAs, *See generally* National Consumer Law Center, Fair Credit Reporting (8th ed. 2013), *updated at* www.nclc.org/library.

[718] *Id.* at § 4.5.6.

nationwide CRAs are well-documented.[719] Creating a monopoly for covered loan information by having only one RIS serve that role would be even worse.

15.2. Compliance With FCRA Is Essential: §1041.17(b)(3) and (4).

The proposed rule and accompanying Commentary make clear that any registered information system must comply with all of the federal consumer financial laws, including the FCRA. Proposed 1041.17(b)(4) requires a RIS to have a program designed to ensure compliance with federal consumer financial laws. Comment 17(b)(3) notes that part 1041 does not supersede the consumer protection obligations imposed under other Federal law or regulation, giving the FCRA as an example. We support this requirement and believe it must be an absolutely fundamental condition for registered information systems.

There is no question that a RIS will fit the definition of a "consumer reporting agency" and RIS information will be a "consumer report" under the FCRA. It is both important and only fair that the protections of the FCRA be applied to RIS information. These requirements are not overly complicated or onerous, but are basic, fundamental principles of fair information use—that a database use reasonable procedures to ensure the maximum possible accuracy of information, that consumers have the right to dispute errors, that consumers have access to information about themselves, that the information is only used for permissible purposes, and that consumers be informed when their information is used against them. None of these requirements should be controversial or burdensome.

15.3. There Should Be Prohibitions on the Use of RIS Information for Marketing and Non-Credit Uses.

The Bureau solicits comment on whether to impose restrictions on the use of information furnished pursuant to proposed Part 1041 beyond the restrictions contained in the FCRA. We strongly urge restrictions on information furnished beyond those in FCRA. Most particularly there should be a restriction against using the RIS information for marketing and prescreening. In addition, RIS information should not be used for non-credit purposes, such as employment or insurance decisions.

The risks of RIS information being used for marketing high-cost credit is extremely great. RIS data will be a treasure trove for lenders to sell covered loans, other high-cost credit, as well as "last dollar" debt settlement services and other scams to distressed borrowers. Such a risk can be seen with the enforcement actions against subprime specialty CRAs Clarity and Teletrack, which both illegally sold lists of subprime borrowers for marketing purposes. And such a risk is understandable given the high costs of customer acquisition, which the Bureau itself notes can be between $150 and $200, even up to $297 per customer.[720] A ready-made list of prior covered loan borrowers is a juicy target.

The FCRA already prohibits the use of consumer reports for marketing purposes. Thus, consumer reports (and the information in them) may not be sold to lead generators or markets, hence the enforcement actions against Clarity[721] and Teletrack.[722]

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[719] *Id.* at § 4.1.3.
[720] 81 Fed Reg. at 47878.
[721] In re Clarity Servs. Inc., File No. 2015-CFPB-0030 (C.F.P.B. Dec. 3, 2015) (consent order).
[722] *See* FTC, Press Release, Consumer Reporting Agency to Pay $1.8 Million for Fair Credit Reporting Act Violations; Company Provided Sensitive Consumer Credit Information to Marketers In Violation of Law (June 27, 2011),

However, the FCRA does permit CRAs to sell lists of consumers who meet certain criteria to companies who wish to make them a "firm offer of credit."[723] These offers are typically referred to as "prescreened" offers. In theory, consumers benefit from these offers, because they are given an offer of credit. In reality, a "firm offer of credit" is usually just a marketing pitch with nothing firm about it, as companies are permitted to ask for new applications and to reject applicants. Unfortunately, too many courts have held that illusory offers that fail to specify the amount or terms of credit are sufficient under the FCRA for prescreening.[724] In addition, it would be impossible to make a firm offer of credit for covered loans (other than exemption loans) because the lender would not have complied with the ability-to-repay requirements before making an offer.

A prohibition on prescreening is critical because any marketing use of RIS information will make it very difficult to detect illegal violations. Prescreening creates a blurry line between permissible and non-permissible marketing activity using consumer reports. Thus, a bright line prohibition—making it easy to enforce and easy to detect a violation—is preferable to a gray area regime where it is unclear what is permitted and what is not.

We also urge the CFPB to limit the use of RIS information for credit purposes only. RIS information should not be used for other FCRA-covered purposes, such as employment, insurance or rental housing. Otherwise, the creation of RIS will ultimately cause great harm to covered loan borrowers if employers or landlords deny them jobs or housing simply for the fact of taking out covered loans. The use of employment background checks has already unnecessarily harmed many consumers.[725] Giving employers private information about the consumer's use of high-cost loans would infringe on their privacy and further victimize vulnerable consumers.

The CFPB has the authority to prohibit the use of the RIS for marketing, prescreened offers, employment, insurance, housing and other noncredit purposes. The CFPB has created the requirement for RIS's and the licensing requirements, it can set the conditions on their use as part of its determination of how RIS's can best be used to protect consumers from unfair, deceptive and abusive practices. The Bureau would not be prohibiting CRAs generally from these uses. In addition, the FCRA already imposes limitations on the use of consumer reports for various purposes (including marketing), and the CFPB has broad authority under that statute.[726]

15.4. The Bureau Should Mandate the Development and Use of a Standardized Data Reporting Format: § 1041.17(b)(1).

CFPB solicits comment on whether proposed § 1041.17(b)(1) should require that registered information systems use particular data standards or transmit and process information furnished in a

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https://www.ftc.gov/news-events/press-releases/2011/06/consumer-reporting-agency-pay-18-million-fair-credit-reporting; U.S. v. Teletrack, Inc., FTC File No. 102 3075, 1:11-CV-2060 (N.D. Ga. June 24, 2011) (stipulated final judgment).

[723] 15 U.S.C. § 1681b(c)(1)(B)(i). See 15 U.S.C. § 1681a(l) (defining "firm offer of credit or insurance").

[724] For a further discussion and examples of these illusory offers, see National Consumer Law Center, Fair Credit Reporting § 7.3.3.3.3 (8th ed. 2013), *updated at* www.nclc.org/library.

[725] *See* Persis Yu, NCLC, Broken Records (April 2012), http://www.nclc.org/issues/broken-records.html.

[726] "The Bureau may prescribe regulations as may be necessary or appropriate to administer and carry out the purposes and objectives of this title, and to prevent evasions thereof or to facilitate compliance therewith." 15 U.S.C. § 1681s(e).

manner consistent with any particular existing standard. We believe that the answer to that question is a resounding "yes," and that CFPB should mandate the existence of a standardized data reporting format for RISs, and require lenders to furnish information using that format. We think the Bureau should develop this standardized format if the industry does not, because existing standards are not sufficiently tailored for the purpose of reporting covered loans.

A standardized reporting format is critical to ensure the accuracy, completeness and utility of the information in RIS. That is why the guidelines issued by the CFPB recommend that furnishers should be: "Using standard data reporting formats and standard procedures for compiling and furnishing data, where feasible . . . ."[727] At least one federal Court of Appeals has noted the importance of having a common "language" for consumer reporting, stating:

> [I]f (furnishers) in that industry are to communicate meaningfully among themselves within the framework of the FCRA, it proves essential that they speak the same language, and that important data be reported in categories about which there is genuine common understanding and agreement. Likewise, if [the CRA] is to "insure maximum possible accuracy" in the transmittal of that data through its reports, it may be required to make sure that the criteria defining categories are made explicit and are communicated to all who participate.[728]

A standardized data reporting format would respond to industry concerns that requiring lenders to engage with multiple RISs will be inefficient and time consuming.[729] With a standardized data reporting format, a lender could simply submit the same report to all of the RISs. The CFPB itself has noted that the costs of furnishing information to multiple RISs "could be reduced substantially with appropriate coordination concerning data standards."[730] And according to the Supplementary Information, the Small Business Review Panel Report is of the same thinking, as it "recommended that the Bureau consider streamlining the requirements related to furnishing information about the use of covered loans, including ways to standardize data to be furnished pursuant to the proposal."[731]

16. RECORD RETENTION AND REPORTING REQUIREMENTS TO THE BUREAU SHOULD BE ENHANCED: § 1041.18.

16.1. Overview.

Section 1041.18 provides compliance program and record retention requirements. We support both. But we urge expansion of the record retention requirements, requiring lenders to:

- retain records longer than 36 months when needed to substantiate RIS/CRA reporting;
- retain additional data; and
- report aggregate data to the Bureau annually.

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[727] 12 C.F.R. Pt. 1022, Appx. E, § III(b)

[728] Cassara v. DAC Services, Inc., 276 F.3d 1210, 1225 (10th Cir. 2002)).

[729] For example, these concerns appear to have been raised in an ex parte meeting between Clarity and the CFPB on August 10, 2016. CFPB, Written Summary of Ex Parte Communication from Clarity Services, Inc., about Proposed Regulations for Payday, Vehicle Title, and Certain High-Cost Installment Loans memo, August 10, 2016.

[730] 81 Fed. Reg. at 48090.

[731] 81 Fed. Reg. at 48093.

We further urge that the Bureau create a searchable database by state and by lender and publish an annual report, including state-level data, based on the data lenders have reported.

16.2. The Record Retention Requirements are Critical and Should Be Expanded § 1041.18(b).

We strongly support the requirements of section §1041.18(b). The record retention requirements are absolutely essential to enforcement of, and thus compliance with, the rule. We make several recommendations below.

16.2.1. The proposed time period of 36 months should be longer if needed to substantiate RIS/CRA reporting: § 1041.18(b).

Proposed § 1041.18(b) would require lenders to retain records for 36 months after the date a covered loan ceases to be outstanding. This retention timeframe should be longer if a delinquent loan continues to be reported to any RIS or other CRA, because the lender should be required to retain the information in order to substantiate any reporting to a CRA. We also note that record retention requirements are longer than 36 months in at least two states.[732]

Lenders should be required to retain information in the event there is a dispute over an item of information in a RIS or other CRA, or if there is another need for the lender to demonstrate that the reported information is accurate and not misleading. A requirement that a lender only be required to retain information for 36 months means that lenders disposing of information thereafter would not be able to substantiate any reporting older than three years. This would appear to be contrary to the intent of the CFPB Furnisher Accuracy and Integrity Guidelines, which require that furnishers "[m]aintain[] records for a reasonable period of time, not less than any applicable recordkeeping requirement, in order to substantiate the accuracy of any information about consumers it furnishes that is subject to a direct dispute."[733]

Thus, proposed 1041.18(b) should require that a lender retain covered loan information as long as needed to substantiate any reporting to a CRA, but not less than a period of 36 months. In the alternative, proposed 1041.18(b) should include a caveat that "this requirement does not affect any record retention requirement under any other federal or state law, including any requirement to retain records to substantiate information furnished to a CRA."

Proposed 1041.18(b)(1)(i) includes RIS reports amongst records to be retained. We support this requirement. However, we note that retaining RIS reports means a lender will be required to comply with the Standards for Safeguarding Consumer Information.[734] An explicit reference should be made to the Safeguards rule.

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[732] Oklahoma requires record retention for four years: (https://www.ok.gov/okdocc/documents/1.%20Oklahoma%20Deferred%20Deposit%20Lending%20Act.pdf); North Dakota for six years (N.D. Cent. Code 13-08-011, http://www.legis.nd.gov/cencode/t13c08.pdf.)
[733] 12 C.F.R. Pt. 1022, Appx. E, § III(c).
[734] 16 CFR Part 314.

16.2.2. Additional data should be required to obtained and reported in aggregate form to the Bureau: § 1041.b(1)-(5).

We support requiring retention of the data the Bureau has proposed be retained. But we urge expanded record retention, as well as reporting aggregate data to the Bureau at least annually. This is needed to facilitate enforcement and is particularly warranted in light of covered lenders' history of evasive practices. In addition, some substantive recommendations we have made throughout this rule would warrant additional data retention for enforcement purposes.

For example, we urge retention data sufficient to provide the following aggregated data reported to the Bureau and state regulators. We emphasize that these are examples and by no means an exhaustive list:

- *With respect to the ability-to-repay determination*, the percentage of loan and borrowers for whom*:*
    - a housing locality-based estimate is used;
    - housing expense is based on shared housing;
    - obligations are treated as joint obligations;
    - income and major financial obligations are not based on verification evidence alone;
- *With respect to all presumptions of unaffordability*, the percentage of loans and borrowers*:*
    - with loans made during a presumption of unaffordability (for short-term loans, broken out by first and second presumption period, and for longer-term loans, broken out by the reason for the presumption), and the reason the presumption was overcome (i.e., higher income or lower obligations);
    - with applications during a presumption period for which the presumption is not overcome;
    - under an exception to a presumption of unaffordability (broken out by the type of exception);
    - that are not covered by the rules (i.e., non-covered loans) during a presumption period.
- *With respect to loan performance, for each category of loan:*
    - Late payments, delinquency, default, and charge-off rates, per loan and per borrower;
    - Stage at which multi-payment loans default and average amount collected at point of default;
    - Reborrowing rates, per loan and per borrower;
    - Failed payment rates, including failed payroll deductions;
    - Late fees, returned item fees, and any other penalty fees or charges imposed.
    - Vehicle repossessions;
    - Debt collection expenses;
    - Use of third-party debt collectors;
    - Lawsuits filed and judgments won;
    - Post-judgment remedies employed (i.e., wage or bank account garnishment);
    - Post-default and post-judgment interest imposed;
    - Debt sales.

16.3. The Bureau should provide a publicly accessible database and publish an annual report providing both national and state-based data.

We urge the Bureau should create a searchable database by state and by lender that enables the public to examine key indicators, such as type of loans made and delinquency, default and reborrowing rates. Just as the consumer complaint database provides helpful information about industry trends and particular companies, so would aggregate data about the experience under the new rules and practices by particular lenders.

In addition, the Bureau should use retained records and aggregated data reported by lenders to produce an annual report. This report will provide important transparency around the effectiveness of the rule and shed light on provisions of the rule that may need strengthening. Given the important role state regulation plays in the markets covered by the rule, state-level data should be included.

17. THE PROHIBITION AGAINST EVASION MUST BE STRONGER: § 1041.19.

17.1. Overview.

Section 1041.19 proposes the following provision addressing evasion:

> "A lender must not take any action with the intent of evading the requirements of proposed part 1041."

The Bureau explains that it is proposing the anti-evasion provision for two primary reasons. The first is to address future conduct taken with the intent to evade, which cannot always be anticipated. The Bureau notes that a broad anti-evasion also has the advantage of not adding additional provisions, and thus further complexity, to the rule. We support this general approach while urging that any clearly foreseeable evasions are most effectively addressed within the substantive provisions of the rule itself, even if it adds complexity; we have made several recommendations of specific provisions throughout these Comments.

The second reason the Bureau offers is that anti-evasion measures are appropriate given the historical background of the markets for covered loans. We clearly support this rationale, as discussed in detail at 2.6 above.

We have two primary recommendations to the evasion provision which we believe are necessary in order for it to achieve its aims:

- First, we urge the Bureau to drop the "intent" requirement, as it risks gutting the entire provision.
- Second, we urge the Bureau to revise several of the proposed illustrative examples and to provide additional ones to strengthen and clarify the standards determining what will be considered evasion. Among other concerns, it should be clear that, when considering shifts in lender practices to evade the rule, the relevant point in time should be the issuance of the SBREFA outline.

We discuss each below.

17.2. An "intent" standard threatens to gut the anti-evasion provision.

The Proposed Commentary elaborates on when an action is taken "with intent."[735] It provides:

- The form, characterization, label, structure, or written documentation of the lender's action shall not be dispositive.
- Rather, the "actual substance" of the lender's action, as well as other relevant facts and circumstance, will determine whether there is intent to evade.
- If an action is taken "solely for legitimate business purposes," there is no intent to evade.[736]
- By contrast, if a consideration of all relevant facts and circumstances reveals the presence of a purpose that is not a legitimate business purpose, there may be intent to evade.
- An action taken with the intent to evade may be knowing or reckless.
- Fraud, deceit, or unlawful or illegitimate activity may be relevant to a finding of intent but are not a prerequisite to such finding.

The Bureau notes that the "intent" provision has precedent in the CFTC's anti-evasion rules under Dodd-Frank. Despite the clarification in the Comments, we fear that a rule that focuses on "intent" will make it difficult for the Bureau to prove state of mind even when the impact and purpose of a practice are clear.[737] Instead, we urge the Bureau to revise this provision to state:

> *The provisions of this rule shall apply to any person making, offering, or arranging covered loans or engaging in practices that evade the rules by any artifice, devise, or subterfuge.*

This proposal is similar to anti-evasion rules in state lending laws and captures the spirit of evasion without a direct requirement to prove "intent" or state of mind.[738]

17.3. Several examples provided, which would essentially condone evasive action, should be strengthened.

The Bureau provides four illustrative, non-exhaustive examples that "may show" intent to evade.[739] While we appreciate the aim of these provisions, we have two significant concerns: (1) they represent evasive activity so foreseeable that it should be addressed within the specific provisions of the rule itself; and (2) they represent activity that is so clearly an evasion that they may suggest that anything less clearly evasion may not be. We take each example in turn:

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[735] Proposed Comment 19-1.

[736] The Bureau notes precedent for this "solely" approach in CFTC anti-evasion rules under Dodd-Frank.

[737] For example, HOEPA's evasion clause requiring a "pattern or practice" of evasion was a difficult bar for standard for plaintiffs to establish. *See, e.g.*, *Cazares v. Household Finance Corp.*, 2005 WL 6418178 (C.D.Ca. July 26, 2005).

[738] *See, e.g.,* Ala. Code § 5-18-4(c) ("[This Act applies] to any person who seeks to evade its application by any device, subterfuge, or pretense whatsoever including, but not thereby limiting the generality of the foregoing: The loan, forbearance, use or sale of credit (as guarantor, surety, endorser, comaker, or otherwise), money, insurance, goods or things in action; the use of collateral or related sales or purchases of goods or services or agreements to sell or purchase, whether real or pretended; and, receiving or charging compensation for goods or services, whether or not sold, delivered, or provided and the real or pretended negotiation, arrangement, or procurement of a loan through any use of activity of a third person, whether real or fictitious").

[739] Proposed Comment 19-2.

- **Example 1** provides that as a matter of course, after issuance of the final rule, the lender begins offering a monetary or non-monetary incentive (e.g., the opportunity to skip payment) to obtain a leveraged payment mechanism or vehicle title after 72 hours. Prior to issuance of the rule, the lender took the leveraged payment mechanism or vehicle title at origination.

This clearly foreseeable evasion concern should be addressed within the substantive provisions, as discussed at section 4.4 above.

If the Bureau does not change the 72-hour provision, it should add another evasion example for financial institutions and open-end lenders that unilaterally change the terms of an account—either the credit account or the deposit account—after 72 hours to add a wage assignment, automatic transfers, or other leveraged payment mechanism.

This example raises an additional broader concern: The relevant timeline for a shift in the lender's practices should not be issuance of the final rule. It should be the issuance of the SBREFA outline. This approach would be consistent with an "all facts and circumstances" approach, given that the direction of the Bureau's rule was clear at that point, and a shift after that point in time is certainly a relevant fact or circumstance. The Bureau should also make clear, generally, that an evasion does not have to represent a *change* in a lender's practice, as new entrants may enter the market evading the rule from the start.

We support the Bureau's suggestion that obtaining personal property at origination and then releasing it in exchange for a leveraged payment mechanism or vehicle title after origination would be an evasion.[740] Again, this should be addressed in the rule itself by broadening the scope (i.e., by covering all loans if the lender has a policy or practice of offering an incentive for providing a leveraged payment mechanism or vehicle title).

- **Example 2** is a covered 14-day balloon loan for which the contract provides for a recurring late fee, equal to the lender's rollover fee, as a remedy, automatically triggered in the event of a consumer's delinquency. The lender doesn't attempt to collect on the loan other than the late fee for 90 days and also gives non-delinquent consumers who express an inability to repay the principal the option of paying the penalty fee.

The Bureau asks whether it should modify the definition of loan sequence or covered longer-term loan to address this example. We do recommend such modification, as described at 3.5 above. If the Bureau does not modify the definition, we support this as an example of evasion but recommend strengthening it by eliminating the assumption that the delinquency fee is the same as the rollover fee, as it could be slightly or substantially different than the rollover fee and this would still appear to be evasion. In addition, the Bureau should emphasize that a scenario could lack other elements in this example and still be evasion.

- **Example 3** is a 60-day loan with four payments due every 15 days with a leveraged payment mechanism and a total cost of credit of less than 36% but a penalty rate of 360 per annum (more than 10 times the contract rate). The scenario is otherwise like Example 2; in addition, the lender did not include the penalty rate prior the issuance of the final rule.

[740] 81 Fed Reg. at 48113, n.914.

The Bureau solicits comment on whether it should address this concern by modifying the existing definition of covered loan. We recommend the rule provide that the total cost of credit must include the penalty rate if the lender reasonably expects that a significant number of borrowers will trigger the penalty rate.

If the Bureau retains this example, the Bureau should use a far lower penalty rate for this example—one 10% more than the contract rate; again make clear that not all of these elements need be present; and make the relevant point of comparison not prior to issuance of the final rule but prior to the SBREFA outline.

- **Example 4** provides that as a matter of policy and practice, after one ACH for the full amount is returned for insufficient funds, the lender makes a second transfer the next day for $1.00. If it succeeds, the lender immediately splits the full payment in two and makes them at the same time, resulting in two NSFs in the vast majority of cases. This policy and practice began shortly prior to the effective date of the rule; before that time, the lender re-presented for the full amount.

As discussed in detail in our discussion of § 1041.14, the proposed prohibition on initiating payment transfers from a consumer's account after two consecutive failed payment transfers is insufficient to protect consumers and prevent evasion. We urge the Bureau to strengthen the proposed prohibition by prohibiting the initiation of further payment transfers after any previous failed attempt; see section 13. This modification is warranted by the Bureau's payments research and greatly simplifies the proposed protection.

Specific rules are better in this situation than reliance on the anti-evasion provision. But if the Bureau permits the failed payment transfer count to be reset by a re-initiated or smaller payment, it should add an example of an evasion such as this:

- The consumer's regularly scheduled $100 payment transfer fails. The lender re-initiates the transfer for $20 and is able to collect that $20. The next regularly scheduled payment of $100 also fails. The lender continues to use the leveraged payment mechanism without complying with § 1041.14 or § 1041.15.

17.4. Additional examples of evasion should be provided.

We appreciate that the Bureau emphasizes that the list of examples is not exhaustive and that, in particular, other loan contract structures, like those containing other types of extraordinary remedies or with deferred interest rates, could cause similar concerns.[741]

In addition, the Bureau should make clear that it will pay special attention to other industries to which lenders have already indicated their intent to expand or migrate—including, at a minimum, pawn, rent-to-own, and any high-cost installment loans not covered by the final rule—for evidence that the lenders are evading this rule by shifting similar debt trap, unaffordable lending practices to those products.

[741] 81 Fed. Reg. at 48114.

Generally, as discussed throughout our comments, we recommend addressing clearly foreseeable evasions by modifying the substantive provisions of the rule themselves. *To the extent the Bureau does not adopt those recommendations*, we urge that it provide examples in the anti-evasion Comments aimed at preventing those evasions, in addition to those we note in section 17.3 above. In particular, we urge that it address:

1. ***Avoiding the scope in its entirety:***
    a. Claiming the loan is a retail installment sale, potentially using kiosks in stores for borrowers to purchase products that are either worthless or overpriced, or are offered by unrelated third parties. This "product" could even be a prepaid card, whereby the consumer buys money on credit.
    b. Claiming the loan is a sale, lease, or service, with cash back.
    c. "Grandfathering in" longer-term lines of credit by establishing them before the effective date of the rule.
    d. Offering faux "credit cards," including those that can be used for purchases of items, as well as cash advances (see section 4.7.1 above).
    e. Claiming that the loan is a pawn of an item that is worth less than the amount of the loan (see section 4.7.2 above).
    f. Claiming that a loan given to an individual, secured by access to the individual's personal bank account, wages or vehicle, is being made for business purposes (see section 4.10.3 above).
    g. Claiming that any loan to a consumer who is a student is a private education loan (see section 4.7.4 above).
    h. Requiring or providing a borrower incentive to provide a power of attorney that would allow the lender to take a security interest in a vehicle at a later date.

2. ***Evading the ability-to-repay determination requirements:***
    a. Misrepresenting recurring utility costs; for example, obtaining borrower statement that borrower will cancel her cable service after taking out the loan;
    b. Renting out co-signers, whereby the lender establishes an affiliated third-party that serves as a guarantor on the loan, in exchange for a fee from the borrower.

3. ***Evading the flipping restrictions applicable to short-term loans and longer-term balloon loans:***
    a. Evading coverage as a longer-term balloon payment loan by charging a balloon payment falling narrowly outside the definition of balloon payment (see 3.2 above).
    b. Shifting a portfolio to short-term open-end loans that function as closed-end loans (see 8.11 above).
    c. Styling rollovers as advances on a credit line that must be repaid within 45 days.
    d. Setting minimum payments on the credit line that do not reduce principal.
    e. Avoiding the rules for longer-term balloon loans by requiring that an open-end advance be repaid before a new advance may be taken out, or by requiring the advance be repaid in full at some point.

4. ***Evading the provisions for short-term loans by shifting to longer-term loans*:**
    a. Using statutes they generally have not used before to offer products unrelated to the intent of the state legislature, for example, making payday loans under a

mortgage statute (OH) or under a credit card statute (IL Financial Services Development Act).

5. ***Evading the protections for longer-term exemption loans:***
   a. Using aggressive debt collection tactics to push the default rates below 5% on longer-term exemption loans under § 1041.12.

Again, we emphasize that many of the above examples are only needed *if* the Bureau does not modify substantive provisions of the rule as we recommend. See additional discussion of payday lender evasion tactics at 2.6 above.

17.5. The example of what is *not* intent to evade is overly broad.

The example the Bureau provides of what is *not* intent to evade is making a 30-day loan product prior to the effective date and, as of the effective date, moving to a 46-day loan and utilizing one of the longer-term exemptions.[742] We would urge the Bureau to modify this example so that the second loan is a PAL loan, the costs of which are clearly defined, rather than any longer-term exemption loan no matter how questionable the terms may be (for example, an origination fee exceeding $50 on a relatively small, relatively short-term term longer-term loan).

18. THE PROPOSED SEVERABILITY PROVISION IS IMPORTANT AND APPROPRIATE: § 1041.20.

We strongly support the rule's proposed severability provision: "The provisions of this rule are separate and severable from one another. If any provision is stayed or determined to be invalid, it is the Bureau's intention that the remaining provisions shall continue to be in effect."

The proposed rule is critical to protect consumers from harm. Should certain provisions be stayed or ruled invalid, there are others that would still provide substantial needed protection to consumers.

19. THE BENEFITS OF THE PROPOSED RULE FAR OUTWEIGH ITS COSTS (Dodd-Frank Act Section 1022(b)(2) Analysis).

19.1. Overview.

The Bureau's cost/benefit analysis required under Dodd-Frank § 1022(b)(2) thoroughly demonstrates that the benefits of the proposed rule far outweigh the costs.[743] The Bureau solicits comment on its preliminary analysis, and we offer some observations, noted here and discussed further below.

First, access is most appropriately construed broadly. Households with lower credit scores are served by a range of credit products. Unaffordable payday and vehicle title loans generate their own demand rather than meeting consumers' credit needs. And the 90 million Americans living in states without payday lending deal with cash shortfalls without unaffordable payday loans and the harms they cause.

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[742] Proposed Comment 19-3.

[743] This section requires the Bureau to assess the potential benefits and costs to consumers and covered persons, including (1) potential reduction in access "to consumer financial products and services," (2) impact on depository institutions and credit unions with $10 billion or less in total assets, and (3) impact on consumers in rural areas.

Second, the proposed underwriting requirements, with our proposed recommendations, are not too costly to be feasible.

Finally, some statements the Bureau makes in the cost/benefit analysis reinforce the need to strengthen the rule.

19.2. "Access" Is Most Appropriately Construed Broadly.

The Bureau is required to consider the potential reduction in access to "consumer financial products and services." "Access" is appropriately construed broadly—not as access to covered payday and car title loans, but to all forms of credit used by consumers likely to use payday and car title loans.

19.2.1. Households with Lower Credit Scores Are Served by a Range of Credit Products.

A review of the credit market for households with lower credit scores shows that they are predominantly served by other credit not covered by this rule—all of which borrowers are more likely to have the ability to repay than the extremely high-cost products covered by this rule.[744]

Credit cards are the dominant one. After a temporary constriction in this market following the financial meltdown, new subprime credit card accounts have increased every year since 2009. They surged in 2015, with more than 10 million new cards issued to subprime borrowers, up 25 percent from a year earlier.[745] In total, subprime consumers have 176 million credit card accounts.[746] Aggregate subprime and deep-subprime credit card limits increased in the first half on 2016 to their highest point in five years, totaling $6.4 billion.[747]

Subprime credit cards cost a fraction of the cost of a payday or car title loan. Most studies show that at least half of borrowers have at least one credit card, and often multiple cards. One study found that of payday borrowers that had a credit card, two-thirds had substantial unused availability remaining on their credit cards on the day that they took out a payday loan.[748] To the extent subprime borrowers lack availability on a credit card, that is not an indication that subprime borrowers do not have access

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[744] Several of the points that follow were included in an op-ed by Mike Calhoun, CRL President, to the Washington Post, "Think there's no good alternative to payday loans? Think again," June 29, 2016.

[745] http://fortune.com/2016/05/20/americans-credit-card-debt-is-set-to-hit-1-trillion-this-year/. Subprime credit cards increasing: http://www.wsj.com/articles/u-s-household-debt-rose-35-billion-to-12-3-trillion-1470754800 "Among people with credit scores between 620 and 660, the share that had a credit card rose to 58.8% in 2015 from a low of 54.3% in 2013. Among those with scores below 620, the number of people with a credit card increased to 50% from a low of 45.6% two years ago. Both figures for 2015 are the highest since 2008."

[746] CFPB, The Consumer Credit Card Market (2015), http://files.consumerfinance.gov/f/201512_cfpb_report-the-consumer-credit-card-market.pdf. Figure 4 at 33 shows 630 million total credit card accounts, while the report notes that 28% of total credit card accounts are held by consumers with subprime scores, at 34.

[747] Experian Credit Cornerstone, Sept. 22, 2016.

[748] CRL, *Shark-Free Waters* at n.15 (citing Sumit, Argawal, Paige Marta Skiba, and Jeremy Tobacman. "Payday Loans and Credit Cards: New Liquidity and Credit Scoring Puzzles?" The American Economic Review, Papers and Proceedings, 99(2) (2009): 412-17). The study matched administrative dataset of payday and credit cards. This study excluded payday loan applicants who did not receive a payday loan. The Bureau cites research finding that 80% of applicants lack available credit on a credit card; this figure both those who received a payday loan and those who didn't, and it includes applicants with no credit card. 81 Fed. Reg. at 47921.

to credit generally, but an indication that they are struggling to repay even the much lower-cost debt they already carry.

Federally insured depositories are another source of credit for subprime borrowers. As the Bureau notes, 700 federal credit unions participate in the National Credit Union Administration's "payday alternative loan" program, making loans up to $1,000 lasting up to six months long. And banks and credit unions originated 3.8 million installment loans to non-prime consumers (credit scores below 660) in 2015.[749] A study has found that approximately 65% of payday borrowers with credit union accounts had available liquidity in their accounts (checking and savings) and/or on an unused line of credit,[750] representing average extra interest paid of $88 over six and a half months.[751]

Pawn loans also serve a significant portion of the subprime market. While they pose concerns about harms to borrowers as well, (1) they are typically significantly less expensive than payday loans; and (2) there is an exit strategy if the borrower can't repay. The lender keeps the pawned item, and the borrower walks away, owing nothing further. There are more than 11,000 pawn storefronts nationwide[752] with more than 30 million customers.[753]

A number of other sources of liquidity are becoming more prevalent to help cash strapped consumers. These included employer and non-profit employer-based emergency loan programs,[754] loans from religious institutions,[755] and extended payment plans from suppliers of consumer services such as utility and telecommunication companies.[756] Reputable national credit counseling agencies can also be helpful in contacting creditors and arranging for extended payments at lower interest rates.[757] Additionally, a growing list of local nonprofits and community centers offer emergency debt counseling and financing assistance for such items as rent, transportation, and utilities.[758]

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[749] Importantly, payday loan borrowers are not typically among the nation's "unbanked" consumers, as lenders typically require that they have a checking account from which the lender can extract payment.

[750] Some banks and credit unions offer reasonably priced overdraft lines of credit made available to account holders in good standing with rates in the 13 to 19% range. For those account holders that don't qualify, some institutions will make available alternative payday lines of credit (APLOCs) for emergency purposes with slightly higher rates and also charging an upfront fee. Good repayment history on an APLOC can move an account holder to the less expensive overdraft line of credit. *E.g.*, Genesee Co-op Federal Credit Union: http://www.genesee.coop/overdraft-line-of-credit and http://www.genesee.coop/alternative-payday-line-of-credit-aploc

[751] Susan Payne Carter, Paige Marta Skiba, and Jeremy Tobacman. *Pecuniary Mistakes: Payday Borrowing by Credit Union Members*, Pension Research Council WP 2010-32, (2010).

[752] http://www.consumerfinance.gov/policy-compliance/rulemaking/rules-under-development/notice-proposed-rulemaking-payday-vehicle-title-and-certain-high-cost-installment-loans/.

[753] https://www.nationalpawnbrokers.org/about/pawn-industry-faqs/.

[754] *See*, *e.g.*, the Community Loan Center of Dallas, a CDFI that provides funding and support for local employers for making responsible emergency loans to employees of up to $1000 for 12 month at 18%. http://www.clcofdallas.org/.

[755] *See* "Churches step in with alternative to high-interest, small-dollar lending industry," Washington Post, January 9, 2015. Available at: https://www.washingtonpost.com/news/get-there/wp/2015/01/09/churches-step-in-with-alternative-to-high-interest-small-dollar-lending-industry/.

[756] *See*, *e.g.*, payment plans available from Consumers Energy: https://www.consumersenergy.com/uploadedFiles/CEWEB/SHARED/AssistancePrograms.pdf

[757] For the types of services that are offered, *see* https://www.nfcc.org/.

[758] See Nerdwallet website at https://www.nerdwallet.com/payday-loan-alternatives?page=1&sort_key=loan_amount.

19.2.2. Unaffordable payday and vehicle title loans generate their own demand rather than meeting consumers' credit needs.

In evaluating the credit landscape for subprime borrowers, it is important to keep in mind that payday and vehicle title loans do not typically provide new credit; they just flip previous unaffordable payday and vehicle title loans. As the Bureau finds, more than four in five short-term payday and vehicle title loans—85 percent of each—are reborrowed within 30 days of the previous loan. In other words, these products generate their own demand; the business model is built on creating a debt trap, not meeting credit needs.

19.2.3. The 90 million Americans living in states without payday lending deal with cash shortfalls without unaffordable payday loans and the harms they cause.

The Bureau's cost/benefit analysis describes what it characterizes as potential harms to borrowers from not being able to access a covered loan, while noting briefly how some consumers handle financial shortfalls in lieu of taking out a payday loan.[759] We urge this analysis be bolstered by further discussion of the demonstrated benefits brought by the absence of unaffordable payday loans.

A comprehensive cost/benefit analysis should include full consideration of the benefits reported for those who are already protected from the harms the Bureau aims to address, as well as the credit products those consumers access. More than 90 million Americans live in states where high-cost payday lending is prohibited. They are not harmed by unaffordable payday loans.[760] And they are served by a range of other credit products and non-credit strategies. Further, former payday borrowers living in states where payday lending is now illegal report being better off with the absence of payday lending.[761]

A North Carolina Commissioner of Banks study, following the exit of payday lenders from that state, studied how low- and moderate-income consumers in the state dealt with financial hardships.[762] It found that the absence of payday lending had no significant impact on the availability of credit in North Carolina and identified an array of financial options that low- and moderate-income consumers used, including credit cards and/or cash advances, which 62% used.[763] The study also conducted focus groups of former payday borrowers, the large majority of which reported that the absence of payday lending had had a positive impact on their household.[764]

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[759] 81 Fed. Reg. at 48129, 48141.

[760] In states that restricted payday lending, the vast majority (95%) of "would-be borrowers" chose not to use payday loans in any form (including online and storefront options). The Pew Charitable Trusts, *Payday Lending in America: Who Borrows, Where They Borrow, and Why*, July 2012.

[761] CRL, *Shark-Free Waters* at 10 et. seq., from which the ensuing discussion of studies following the departure of payday lenders from a state is largely drawn.

[762] Center for Community Capital, University of North Carolina at Chapel Hill, *North Carolina Consumers after Payday Lending: Attitudes and Experiences with Credit Options*, Prepared for the North Carolina Commissioner of Banks, Nov 2007. http://ccc.sites.unc.edu/files/2013/08/NC_After_Payday.pdf

[763] *Id.* at 6 (21% reported using credit cards/cash advances; 30% reported assistance from friends and family).

[764] *Id.*

Seven years after Arkansas began enforcing its constitutional usury cap of 17% against payday lenders, 100 former payday borrowers were surveyed. [765] They reported that they use credit cards (21%), pawn (19%), and loans from banks or credit unions (12%), as well as build savings (14%), increase income (12%), and use financial assistance from friends and family (36%) to deal with shortfalls. [766] And they too report that they are better off without payday loans.

A recent study on consumer borrowing after payday lending was prohibited in several states found that reductions in the number of payday borrowers were offset by increases in the number of pawn shop borrowers. [767] The authors state that this is likely a result of former payday borrowers switching to pawnshop borrowing as a substitute credit product.

A recent paper examines the substitution of fringe (payday) loans with less costly mainstream credit after the passage of the Military Lending Act (MLA), which made certain loans to the military over 36% illegal. The paper showed that likely military borrowers showed *increased* access to credit card borrowing after the restrictions placed on payday lending by the MLA. Credit limits increased by an average of 17-25% on total credit card accounts following passage of the MLA. [768]

Further, several academic studies find evidence of financial harm to consumers when comparing those consumers that reside in locations that have access to payday loans versus those that do not. For a complete discussion of those studies, see CRL's recent research brief. [769]

We note that the Bureau's discussion of studies on the costs and benefits of payday loans notes that the studies generally find that access leaves borrowers worse off, while access may benefit consumers in certain circumstances, like an unusual dip income or spike in expenses. [770]

CRL has investigated the claim that a payday loan benefits consumers in such circumstances. We use average annual frequencies of dips and spikes in both income and expenses, based on evidence for low and moderate income households from the U.S. Financial diaries (USFD) study, [771] and model expected volatility for three income levels: $25,000, $31,000, and $40,000. [772] The model calculates the

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[765] Covington, Meredith, and Jennifer Johnson, *Into the Light: A Survey of Arkansas Borrowers Seven Years after State Supreme Court Bans Usury Payday Lending Rates*, Southern Bancorp Community Partners, April 2016. http://southernpartners.org/assets/sbcp_policy-points-vol-43-payday-lending_20160628.pdf.

[766] *Id.* Indeed, payday borrowers also frequently turn friends and family for help ultimately pay off their payday loans, but in worse financial condition than they were before the payday loan. Pew Charitable Trusts, Payday Lending America: Who Borrows, Where They Borrow, and Why, July 2013, http://www.pewtrusts.org/~/media/legacy/uploadedfiles/pcs_assets/2012/pewpaydaylendingreportpdf.pdf.

[767] Neil Bhutta, Jacob Goldin, and Tatiana Homonoff. *Consumer Borrowing After Payday Loan Bans, July* 13, 2016. (Note: the states studied were Arizona, Montana, and New Hampshire.) For further discussion of this paper, see *Shark-Free Waters* at 4.

[768] Roman Galperin and Kaili Maricio. *Tough Times Borrowing: Effects of Fringe Lending Regulation on Credit Standing, Search, and Access,* April 2016.

[769] CRL, *Shark Free Waters* at 5-6.

[770] 81 Fed. Reg. at 48131.

[771] Morduch, Jonathan and Anthony Hannagan. 2015. *Income Gains and Month-to-Month Income Volatility: household evidence from the US Financial Diaries*. US Financial Diaries Project. https://www.stlouisfed.org/~/media/Files/PDFs/Community%20Development/Econ%20Mobility/Sessions/MorduchPaper508.pdf.

[772] In the detailed recording of monthly household finances for 244 households, USFD found that, on average, these households experienced 2.5 months out of 12 when income fell by more than 25% of average and 2.6

probability that a consumer that takes a $500 loan in Month 1 because of a dip in income or spike in expenses (or both) recovers over the following two month period.[773] Generally, we find that the probability is low of recovering by the end of Month 3 from an income dip or expense spike that occurs in Month 1, and that the loan merely exacerbates illiquidity by the end of the three month period, despite providing a cash flow boost in Month 1.

Consumers across the three income groups who are in an income/expense combination where they take a loan have a very high probability of experiencing *negative* cumulative cash flow in *both* Months 2 and 3, ranging from 77% to 47% (lowest income level to highest). Alternatively, the probability of having *positive* cumulative cash flow for *both* Month 2 and 3 is very low ranging from 9% to 33% (lowest income level to highest). *Even if one reduces the assumed level of expenses by 10%*, the probabilities of negative cumulative cash flow in both Months 2 and 3 are still substantial, particularly for the $25,000 and $35,000 income level. With *reduced* expenses, the probability of experiencing *negative* cumulative cash flow in *both* Months 2 and 3 was 47% for the lowest income level, 30% for the middle income level, and 18% for the highest income level.

Further, at **Appendix B** to these comments, we provide CRL's previously published critiques of several research papers suggesting benefits of payday loans.

19.3. The Proposed Underwriting Requirements, With Our Recommended Enhancements, Are Not Too Costly to Be Feasible.

First, it is clear that the proposed underwriting requirements are reasonable and not cost-prohibitive. After initial set-up costs, which the Bureau does not project to be cost-prohibitive, the Bureau estimates that a fully automated ability-to-repay determination, which is has designed the rule to permit lenders to do, would take "essentially no time." Dollar costs would include $0.50 for a report from a registered information system; $0.55-$2.00 for a specialty credit report including a housing estimate; and additional small cost for lenders relying on an electronic service to gather verification evidence for income (like checking account or payroll records). While we urge that these requirements

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months when income rose more than 25% of average. They also looked at expense volatility and found that, on average, households experienced three months where expenses fell more than 25% below average and two months where expenses rose by more than 25% of average. CRL used this reported frequency of "spikes" and "dips" in monthly income and expenses to model the probabilities of various three sequential month combinations of income (spike = 125%, dip= 75%, and average= 100%) and expenses (spike dip, average, same ratios) for a household, assuming independence between the three levels of income and three levels of expenses for any one month and also between months. This results in 729 different combinations with associated probabilities of occurrence. We then used these combinations to derive three consecutive monthly cash flows for three different household average annual income levels, $25,000, $31,000, and $40,000. Matched levels of limited expenses (including housing, food, and transportation) were taken from the BLS Consumer Expense Survey for the income buckets associated with each of the three income levels. Two levels of limited expenses were modeled: 100% and 90%.

[773] For purposes of the model, in the interest of isolating loans taken in response to an income dip or expense spike, we assume that if a consumer is in a 3 month income/expense combination where there is a dip in income or a spike in expenses (or both) in Month 1, he/she will take out a $500 balloon loan in Month 1. The income/expense combinations that do not meet these criteria are eliminated from the rest of the analysis. The loan is assumed to have a fee of $15/100 ($75 total). Consumer receives $500 loan proceeds in Month 1 and pays back $500 loan plus the $75 fee in Month 2. While we use a $500 loan, a $350 loan would not significantly impact these findings, as the only impact would be the difference in the fee on the two loans—about $26.

be strengthened in certain respects, our recommended changes would still permit a largely automated underwriting process. Further, fintech companies have shown eagerness to develop solutions that will streamline compliance.

Moreover, as the Bureau notes, the reduction in defaults that would be expected from making a reasonable ability-to-repay determination should significantly offset the added costs of making that determination. We note our recommendations aimed at ensuring the rule does in fact result in a significant reduction in defaults at section 7 above.

19.4. Some Statements in the Cost/Benefit Analysis Reinforce the Need to Strengthen the Rule.

Some of the Bureau's statements in the cost/benefit analysis seem to acknowledge the ways in which lenders may try to evade the intent the rule, reinforcing the need to strengthen it.

With respect to scope, the analysis notes that lenders may defer selling credit insurance until after 72 hours to keep the total cost of credit at the outset at below 36%.[774] This supports including credit insurance regardless of when it is sold. See 3.9 above.

With respect to the upfront ability-to-repay determination, the Bureau notes that, had it not proposed a short-term exemption, "borrowers would not have the benefit of the step-down in loan size across a loan sequence of loans, which the Bureau believes will reduce the likelihood that borrowers will default on their covered short-term loans."[775] An ability-to-repay determination should better designed to prevent default than a series of three loans with no clear correlation to the financial circumstances of the borrower. This concern supports less lender discretion in the upfront ability-to-repay determination requirements and a requirement that defaults be low in the absolute.

With respect to the presumptions framework in the short-term space, the Bureau's discussion on the impact of the rule on loan volume notes: "If borrowers who currently take out these long sequences would respond to the sequences being cut short by returning to borrow again as soon as they can [i.e., 31 days later], the impact of the reborrowing restrictions on loan volume would be less."[776] This recognizes that presumptions of unaffordability can be avoided by delaying the new loan until shortly following the 30-day period, supporting the appropriateness of a 60-day over a 30-day presumption period.

With respect to moving borrowers from a balloon loan into to longer-term non-balloon loan, the Bureau states that the presumption of unaffordability will rarely be triggered given the exception for smaller payments: "This situation is unlikely to occur frequently, as a covered longer-term loan would normally have payments that are substantially smaller than the payment for a covered short-term loan or the balloon payment of a covered longer-term balloon-payment loan." This exception, which the Bureau acknowledges here would swallow the presumptions rule, poses undue risk of substantial harm, encouraging bait and switch of borrowers using unaffordable balloon loans; see section 11 above.

Finally, with respect to longer-term loans more generally, the Bureau makes several statements or assumptions about the future longer-term loan market. The Bureau notes that lenders may adjust

[774] 81 Fed. Reg. at 48139.
[775] 81 Fed. Reg. at 48149.
[776] 81 Fed. Reg. at 48121.

their product mix to longer-term loans, which may reduce harm because longer-term loans are (1) more predictable and (2) "ultimate repayment is more likely." It notes that "borrowers may be less likely to end up in a loan that is substantially more expensive than they anticipated." We refer to our discussions noting that evidence suggests tomorrow's longer-term market will look different from today's (section 2.5.5); that extraordinarily high interest rates have not historically been sanctioned on longer-term loans (section 2.5.1); how longer loans can create deeper debt traps than short-term loans (sections 10.2 and 10.3); that income and expense volatility pose greater challenges on these loans (section 10.4); and our concerns about serial refinances of longer-term loans (section 11). In light of the observations made in those discussions, we fear the Bureau's statements here are unwarranted, and that stronger upfront underwriting and restrictions on refinancings and defaults are critical to a rule that prevents abusive and unfair practices with respect to longer-term loans.

20. THE RULE SHOULD MAKE CLEAR THAT OFFERING OR COLLECTING A LOAN IN VIOLATION OF STATE LAW IS AN UNFAIR, DECEPTIVE, AND ABUSIVE PRACTICE.

As noted at section 2.4.1, a substantial number of states with have strong laws in place to protect their residents from the harm of unaffordable payday and vehicle title loans, including usury limits. These states can and do enforce their laws with actions that have resulted in millions of dollars of debt relief and restitution.[777] But, as the Bureau notes and as discussed at 2.6.2, payday lenders exploit loopholes in state laws or simply disregard state laws altogether. And as the Bureau has recognized through enforcement action, it has an important role to play to help prevent that from happening.

The Bureau explicitly recognizes in the proposal that state usury limits are more protective of consumers than the Bureau's proposed rule.[778] While the Bureau does not have authority to enact a usury cap, it does have authority to prevent lenders from violating stronger state level protections and making illegal loans. Even in states that do not have strong laws, licensing requirements generally apply to non-depository lenders and other limits may apply. Unlicensed loans are unlawful and may be void or uncollectible under state law.

The CFPB should protect consumers from illegal loans and strengthen the enforceability of state laws by declaring in this rule that offering, collecting, making, or facilitating loans that violate state usury, licensing, or other consumer protection laws is an unfair, deceptive, and abusive act or practice. By making such violations a violation of federal law, CFPB will offer states additional, and stronger, tools to crack down on illegal lending and effectively enforce their laws, including stronger penalties than state laws provide.[779]

This provision would be consistent with enforcement actions recently taken by the CFPB, particularly in the CashCall case, where a judge recently affirmed the Bureau's position that the collection and servicing of loans made in violation of state usury and licensing laws, which are thus uncollectable or void under state law, is a UDAAP violation.[780]

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[777] *See* CRL, *Ending the Cycle of Evasion, supra.*
[778] The Bureau, of course, lacks the authority to establish a usury limit.
[779] For further discussion of this and other issues of particular importance in states without payday lending, *see* Letter from groups from 13 states without payday lending to CFPB, May 24, 2016, *available at* http://www.neweconomynyc.org/2016/04/news-release-new-economy-project-allies-urge-cfpb-issue-strong-payday-lending-rule/.
[780] CFPB v. CashCall, 2016 WL 4820635 (C.D. Cal. Aug. 31, 2016).

21. THE EFFECTIVE DATE SHOULD BE REDUCED TO 12 MONTHS.

The Bureau has proposed an effective date for the rule of, generally, 15 months after publication of the final rule in the Federal Register. We appreciate that the Bureau aims to balance providing consumers with needed protection while giving covered persons adequate time to comply with all the rule.

We urge the Bureau to shorten this effective date to 12 months, in light of the urgent need for protection from the abusive and unfair practices the rule addresses. One year is a reasonable period of time within which to expect lenders to be compliant.

We also urge the Bureau not to grandfather open-end lines of credit opened prior to the effective date. Any new advances taken after the effective date should be fully covered by the rules. Otherwise, lenders may rush to open credit lines before the effective date to evade the rules. Lenders typically retain the right to amend the terms of open-end credit lines, and certainly the right to close them, and they can easily conform their credit lines to the rule's requirements just as other lenders can.

22. CONCLUSION

We appreciate the challenge presented by the task before the Bureau and the great efforts CFPB is making to protect consumers. The Bureau's proposed rule takes the right fundamental approach, but we urge significant changes in order to ensure the rule prevents the unfair and abusive practices it identifies. Many of our recommendations are rooted in efforts to prevent evasion by an industry with a rich history of evasive practices. We thank the Bureau for its consideration of our comments; we would be happy to discuss them further.

APPENDICES:
APPENDIX A: Individual Borrower Experiences with Payday and Car Title Loans
APPENDIX B: Critiques of Selected Payday Lending Studies by Center for Responsible Lending
APPENDIX C: CRL, CFA, NCLC Research Addressing Payday and Vehicle Title Lending, 1998-present

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Appendix A
Individual Borrower Experiences with Payday and Car Title Loans

Introduction

Consumers across the country are devastated by the impacts of payday, car title, and other high-cost loans. The stories below highlight real customers' experiences with predatory lending and illustrate the harms associated with these loans. Stories were collected from a variety of sources. The Center for Responsible Lending has an established relationship with some of the victims who recounted their stories. Other stories were obtained by Freedom of Information Requests for complaints and original loan contracts that were sent to the consumer protection agencies of certain states. Borrowers' experiences were also derived from news articles and other media sources.

Coding

Following each story, one or more code is applied, indicating the following:

Type of harm experienced, based on the categories of harm the Bureau identifies in its proposal:

"**1**" Borrower endures long loan sequences, including frequent loan renewals, loan flipping, or long cycles of taking out one loan to pay another.

"**2**" Borrower experiences delinquency and/or default, including lender and bank fees triggered by the loan itself, aggressive debt collection, and loss of a vehicle.

"**3**" Borrower suffers collateral harms from making unaffordable payments, including defaulting on other major financial obligations or basic living expenses.

Other loan features:

"**LT**" Long-term loan

"**CT**" Car title loan

"**SL**" Small loan with principal of $200 or less.

Asterisks following an annual percentage rate (APR) indicate approximate APR as calculated by CRL staff, based on the information provided by the borrower.

Borrower Experiences

1. Arthur, a 69-year-old warehouse worker and grandfather of seven, started with a loan of $200 from Advance America. The loan eventually increased to $300. Every payday, rather than defaulting or coming up short on bill money, Arthur went into the Advance America store and paid a fee of $52.50 so Advance America would not deposit his check for the full loan amount. Advance America flipped the loan over a hundred times, until his total interest paid was an estimated $5,000. The clerks knew him by name and often had his paperwork ready for him

when he came in. Payday lenders have a name for consumers they see every payday: “26ers”— because they pay up every two weeks, 26 times a year. In Arthur’s case, they saw him once a month rather than every two weeks, but only because his repayment came from his monthly Social Security check.
Source: *Caught in the Trap: The real story from payday lending borrowers* – CRL Issue Brief, June 2010
(1, 3, SL)

2. Mary is a single mother who has owned her one-story brick house in New Castle, Delaware for nearly a decade. After falling behind on the mortgage payments, she applied for and received a 135% APR payday installment loan from California-based, LoanMe. Mary, who works part-time as a dietary aid and receives disability payments, immediately put the money toward the mortgage and repaid the loan in the first month to avoid paying high interest, she said. It still wasn't enough to make her current on the mortgage, so she applied for a second loan in the spring. This time, she was approved for $3,100 with an APR of 135%. She has up to 47 months to repay the loan – meaning that she will pay approximately $16,500 in principal, fees and interest if it takes her the entire time. "I make monthly payments to make sure they are not coming after me, but with interest that won't do much," she said. "Now I'm left with this bill, plus my mortgage. I'm in worse shape now."
   Source: http://www.delawareonline.com/story/news/local/2016/08/26/lawmakers-eye-caps-changing-payday-lending-industry/87632062/
   (1, 2, 3, LT)

3. In September 2011, Pauline, a 96-year old widow living on Social Security income and a small pension each month, received a $450 payday loan from Allied Cash Advance with an APR of 360%. To circumvent the Virginia’s payday lending law, the company framed its product as an open-end credit agreement rather than a payday loan. Although she made payments to Allied totaling $597, her balance remained at $776.20. Company representatives threatened Pauline numerous times, telling her they would deal “harshly” with her for failure to pay and falsely asserting that failure to pay the loan constituted fraud and could result in jail time. Pauline believed the criminal threats were real and suffered significant distress and anxiety as a result.
   Source: *Pauline Honey v. Allied Title Lending LLC*, 12-00045, Filed 9/14/12, United States District Court for the Western District of Virginia
   (2, 3, LT, OE)

4. Virginia regulations for payday and car title loans. To avoid these regulations, payday lenders encouraged consumers to enter into open-end credit agreements. Allied Title Lending offers car title loans and open-end credit agreements at the same locations where the company (previously called Allied Cash) had operated as a payday lender. James and his wife, who live solely on their Social Security income, fell on difficult times financially and entered into a “Motor Vehicle Equity Line of Credit Agreement” with Allied Title Lending to assist with their struggles. James agreed to borrow $2,160 at an annual interest rate of 182.5%. Although James has never made a late payment in the five years that Allied Title Lending has continued to collect on the contract, the company has threatened James the entire time that if his payments were late, his vehicle would be repossessed. The company repeatedly tricked James into collecting much more than what was actually due under the contract by telling him he could pay off the loan more quickly if he paid more than the minimum payment each month. Allied Title Lending categorized

the loan as an open-end line of credit, but no money in excess of the original loan amount was ever made available to James, and he has paid back more than $16,000 on his $2,160 loan.
Source: *James F. Lam v. Allied Title Lending, LLC*, United States District Court for the Eastern District of Virginia
(1, 2, LT, OE)

5. Christopher received a $500 payday loan from CashNetUSA, with a total repayment of $625. He had to roll the loan over to the next month five subsequent times, meaning that he paid a $125 fee each time with none of the fee going toward paying off the principal. As a result, he paid $1250 total on his $625 loan. A few months later, CashNetUSA told Christopher they had increased his credit line to $1,500. He obtained the $1,500 loan with a total repayment of $1,875. When payment was due, Christopher did not have the money to repay the loan and contacted CashNetUSA prior to the due date to arrange a payment plan. The company debited a $375 rollover fee from his checking account and then took the entire $1,500 loan amount from his account anyway. Christopher did not have enough money in his account to pay the loan, so he accrued $934.82 in NSF fees from his bank and was unable to pay any of his other bills, including child support and rent. In order to prevent eviction, he took out another payday loan from CashNetUSA for $1,500 to pay his rent, further perpetuating the cycle of debt.
   Source: Florida Attorney General's Office, 2007
   (1, 2, 3)

6. Sandra, a successful professional, worked diligently to keep up with her bills. In a tough time, she turned to payday lending. After several rollovers, Sandra's first loan was due in full. She couldn't pay it off, so she took a loan from a second lender. Frantically trying to manage her bills, she eventually found herself with loans from six payday lenders including Advance America, Check Into Cash, Check 'n Go, Urgent Money Express and two on-line lenders. She paid over $600 per month in fees, none going to pay down her debt. After writing checks to payday lenders totaling $9,200, she was evicted and her car was repossessed. "At the time it seems like the way out, but this is not a quick fix. It's like a ton of bricks," said Sandra.
   Source: *Caught in the Trap: The real story from payday lending borrowers* – CRL Issue Brief, June 2010
   (2, 3)

7. Edith, an Asheville, North Carolina single mother, cut down on her family's groceries, stopped driving her car, and kept her lights off to save electricity as she scrambled to pay the fees on her payday loans. She took out her first $300 payday loan, and then a second and third, trying to repay the first. Edith borrowed a total of $900, received $765 in cash and paid $135 in interest ($45 x 3) at the time she borrowed. She continued to pay $270 in interest every month ($135 twice a month) for well over a year because she could not afford to repay the $900 principal owed. Though she only received cash advances totaling $765, during the next year, she paid over $3,500 in fees alone, and still owed the original $900.
   Source: CRL website: *The Victims of Payday Lending*.
   http://www.responsiblelending.org/issues/victims-payday.
   (2, 3)

8. Vanessa obtained a $1,455 payday installment loan from The Cash Store. She was to make twelve payments over six months of $357 each, paying a total of $2,832 in finance charges, reflecting an APR of 581%. Although she certified that the payment on principal and interest did

not exceed 25% of her income, Vanessa could not keep up with her loan in addition to her ongoing monthly expenses. She paid $2,100 over four months for the loan but still owed $1,600—more than the original principal amount. She was forced to close her bank account after incurring too many overdraft fees, and she has worse credit than when she obtained the loan. She is still facing a legal debt collection action. Vanessa has testified before the Texas Legislature to tell her story, saying, “The short of it: I, like so many Texans who got payday loans, was sunk.”
Source: Loan contract on file with CRL
(1, 2, 3, LT)

9. Sherry was a struggling, working single mother who made 15 monthly payments totaling approximately $3,000 on the $1,000 payday installment loan she obtained from Western Sky. The loan required an automatic draft of 24 monthly payments of $198, which carried an APR of 233%. Sherry could not afford the payments, but continued to make them despite falling further behind on her mortgage and other bills and incurring overdraft fees from her bank. When she was offered a trial loan modification to resolve her mortgage delinquency, she attempted to stop the automatic electronic payments being made to Western Sky but was initially unsuccessful. As a result, her first trial payment on her mortgage modification was returned for insufficient funds and the mortgage company cancelled the modification. Although she initially took out the loan to improve her financial situation, it deepened her financial distress and even caused her to lose her initial chance to save her home from foreclosure.
Source: Loan contract on file with CRL
(1, 2, 3, LT)

10. Oscar Wellito took out a $100 loan American Cash Loans, LLC after he went bankrupt. He was supporting school-aged children while trying to service debt obligations with two other small loan companies. He earned about $9 an hour at a Safeway grocery store, which was not enough money to make ends meet, yet too much money to qualify for public assistance. “That's why,” he testified, “I had no choice of getting these loans, to feed my kids, to live from one paycheck to another paycheck.” He needed money for groceries, gas, laundry soap, and “whatever we need to survive from one payday to another payday.” His loan carried a 1,147.14% APR and required repayment in twenty-six biweekly installments of $40.16 with a final payment of $55.34. Thus, the $100 loan carried a total finance charge of $999.71.
Source: *State ex rel. King v. B & B Investment Group, Inc.*, 2014-NMSC-024, 329 P.3d 658
(2, LT, SL)

11. Delores, a 78-year-old retiree, borrowed $730 at an APR of 300% from Wisconsin Auto Title Loans when she needed new tires for her 1992 Buick Park Avenue. The company required her to turn over the spare key and title to her vehicle. A month later on the due date, her loan had grown to $1,027 and she couldn’t afford to pay it. The amount due was more than her entire Social Security check. Because she couldn’t imagine giving up her vehicle, she began to borrow money from other sources just to pay the interest on the car title loan, never making a dent in the principal. She eventually sold her car for $1,000 to help pay the debt.
Source: Yeoman, Barry. “Sudden Debt.” AARP Magazine September & October 2006: 108-113, 128. Print.
(2, 3, CT)

12. Jane, a 79-year-old woman, obtained a $380 payday loan from SpeedyCash with a 259% APR to help pay for her daughter's cancer medication. She earned $922 in social security benefits and paid a rent of $430, the lender did not ask her about her ability to repay the loan and simply required proof of income. Despite making 16 monthly payments of between $65 and $95, Jane still owes $500 on the loan. She has never made a late payment although she owes other bills because that would allow the lender to take the funds straight from her account. She reasons, "I would rather not pay my light bill than for the [payday loan company] to take all the money I need to pay my rent."
    Source: Video on file with Texas Appleseed.
    (3)

13. Lauren received a car title loan from TitleMax for $817.19, with an initial APR of 66.02%. She was charged monthly for automobile insurance coverage, which the company claimed was voluntary. However, TitleMax required certain stipulations if customers wanted to use their own auto insurance, including paying the policy through the maturity date of the transaction in advance, listing the company as a lien holder on the insurance policy, and carrying a deductible of no more than $500. Lauren could not afford to pay her insurance premium in advance, and as a result had to pay TitleMax monthly for auto insurance in addition to the loan principal and interest. As she could not afford to pay off her loan in full each month, Lauren was forced to refinance the loan 13 times. Each renewal resulted in an increase in the monthly auto insurance premium she was charged by TitleMax. She eventually surrendered her 2004 Chevy van to the company because she could not afford to repair it. At the time of surrender, her balance on the loan had ballooned to $3,883.35 and she had been charged $4,128.55 in fees and other charges over the course of the loan.
    Source: Florida Office of Financial Regulation, 2014
    (1, 2, 3, CT)

14. Fearing she and her family would soon lose their home, Jessica obtained a $1,900 car title loan from Instaloan in October of 2013. It was marketed as a no-credit-check collateral loan, but she did not understand what that meant. When she asked the company representative, he told her that it was a car title loan but he wasn't allowed to tell customers that. Jessica was told that she was required to purchase their auto insurance even though the contract terms indicated the insurance was voluntary. Over the next 13 months, she paid more than $4,000 for her $1,900 loan, and none of her payments have been applied toward the principal of her loan. Recently, she moved from Florida to Arizona. She called Instaloan to ask for their address so she could send her payment via mail and was told she could not mail a payment because the company needed to receive the payment and a signature on the loan renewal on the same day. Instaloan told her the only option was to contact another title loan company and have them buy out the loan at the payoff amount. The company representative recommended that she contact TitleMax, which she realized was the same company as Instaloan. No one from TitleMax has returned Jessica's phone calls, and she is worried that her vehicle will be taken.
    Source: Florida Office of Financial Regulation, 2014
    (1, 2, CT)

15. Shirley, an elderly woman on a fixed income, received a car title loan from TitleMax for $2,453.29. She did not understand that the loan had to be repaid in one lump sum or it would be flipped each month and she would accrue new finance charges. Because she was unable to pay the full amount of the loan at once, TitleMax flipped the loan six times. Despite the fact that

Shirley paid over twice the principal amount of the loan to the company, including $1326.01 for the company's auto insurance, TitleMax still repossessed her vehicle when she was unable to make a monthly payment.
Source: Florida Office of Financial Regulation, 2014
(1, 2, 3, CT)

16. James, a 67-year-old on a fixed income, obtained a $500 car title loan from TitleMax in May 2013. He had hoped to be able to pay the loan off in three months; however, he has paid $957 over the past year and still owes $603.98 – over $100 more than the original loan principal. His loan has been flipped 14 times, and he does not understand why he is also charged a monthly auto insurance premium. After paying almost twice the original principal amount, James is now in danger of losing his vehicle as TitleMax claims he is 15 days late in making a payment.
Source: Florida Office of Financial Regulation, 2014
(1, 2, CT)

17. Deborah received a $2,000 car title loan from TitleMax in July 2014. Her loan has been flipped ten times and despite paying over $4,000 to the company, she still owes $1,785.73 – almost as much as the original amount of her loan. Over the course of the year that she's been paying on her loan, the APR has ranged from 43.33% to 46.48% and she has been forced to pay for costly auto insurance that she does not want and did not understand she would have to pay at the time she signed the contract. Representatives from the company have called her place of employment several times a day, putting her job at risk. When she was late on her payment to TitleMax, they sent a tow truck to her place of employment to repossess her vehicle.
Source: Florida Office of Financial Regulation, 2014
(1, 2, CT)

18. Sam received a $604.31 car title loan from TitleMax in July 2013, which carried an APR of 78.7%. His loan was flipped three times and he was forced to pay for auto insurance that he did not need or want. Although the loan contract indicated that the company's auto insurance was voluntary, he was told that his existing car insurance did not meet the company's requirements. The loan contract stated that the policy through TitleMax does not insure the customer against liability for bodily injury or property damage caused to others and does not suffice under Florida's law requiring all resident motorists to have auto insurance for personal injury protection and property damage. As a result, Sam paid $246.17 over four months for TitleMax's car insurance, in addition to the coverage he paid for under his existing insurance policy. Due to the high interest rate and unwanted insurance products, over four months Sam paid a total of $1,186.00 for a $604 loan.
Source: Florida Office of Financial Regulation, 2014
(1, 2, CT)

19. Betty was 78 years old and drove very infrequently when she decided to pursue a car title loan for $2,217.29 from TitleMax. The company required her to buy their auto insurance unless her current policy met their criteria. After realizing that she had paid $348.48 over three months for their additional auto insurance that she did not want or need, she decided to decline TitleMax's insurance and use her current coverage with Geico instead. She believed her insurance met TitleMax's requirements, but she received a call from the company telling her that she had to list them as the payee within fifteen minutes or be forced to pay $175.00 per month for their

policy. She believed she was being taken advantage of by TitleMax because she was elderly and did not understand what she was signing.
Source: Florida Office of Financial Regulation, 2014
(1, 2, CT)

20. Derek received a car title loan from TitleMax for $1,541.06 in May 2014. After paying on his loan for three months, his fourth payment was late. As a result, the company required that he take out an auto insurance policy even though he already had full insurance coverage through another provider and had listed TitleMax as the payee on that policy. He gave them documented proof of his current insurance policy but was told that he must purchase TitleMax's additional insurance although the form he was required to sign stated that the insurance was voluntary. When he attempted to make his payment of $98.00, Derek was told that he owed an additional $141.82 for the additional insurance. Derek could not afford the increased monthly payment and TitleMax is now threatening to repossess his car.
Source: Florida Office of Financial Regulation, 2014
(1, 2, CT)

21. Diego received a car title loan from TitleMax for $654.77 with an APR of 76.4% in September 2013. Over the next year, his loan was flipped eleven times. During this time, he was charged $334.30 extra for auto insurance financed through the company. Although he had a current auto insurance policy, TitleMax required that his policy be current through and including the next payment date. However, Diego found that the company would not accept his insurance policy because he paid his insurance premium each month on the day after his loan payment was due and therefore could not provide proof of insurance until the next business day after he had already renewed the loan.
Source: Florida Office of Financial Regulation, 2014
(1, 2, CT)

22. Phyllis received a car title loan from TitleMax for $643.73 that carried an APR as high as 115.6%. She has paid $2,190 on the loan over 18 months and still owes $261.64. Despite paying over three times the principal amount of the loan, the company has repossessed her vehicle twice, forcing her to pay an additional $400 each time to receive access to her vehicle.
Source: Florida Office of Financial Regulation, 2014
(1, 2, CT)

23. Jane received a car title loan from TitleMax in November 2013 for $4,335.86. Despite having paid $3,245 over the past eight months, the company says she still owes $3,686.73. She has paid $272.50 for auto insurance through TitleMax even though she already possesses a current auto insurance policy.
Source: Florida Office of Financial Regulation, 2014
(2, CT)

24. After her husband passed away, Rachel was short on cash and decided to obtain a car title loan from TitleMax in August 2014 for $3,000. After paying on the loan for a year, including over $2,000 in auto insurance she did not need or want, she had to return to her previous residence in Wisconsin to handle an issue with her husband's estate. When she called TitleMax to let them know she'd be sending her payment by money order, she was told that she had to make all payments in person because she was also required to renew the loan at the time of payment. A

company representative even told her that TitleMax sends an employee to the hospital to obtain payment and a signature on the loan renewal if a customer is hospitalized during the time a payment is due. She called several times after that to again see if she could make a payment over the phone or have a relative make a payment in person, but the company refused. Because she could not return to Florida to make a payment, TitleMax is in the process of repossessing Rachel's vehicle.
Source: Florida Office of Financial Regulation, 2014
(1, 2, CT)

25. Dan received a car title loan from TitleMax in October 2014 for $1,500, with an APR ranging from 47.2% to 51.9%. Over the past year, he has paid a total of $2,371.54, yet he still owes $1,415.53—almost the entire original loan amount. Although Dan informed the company that he had AAA Plus coverage and did not want to purchase any additional towing services, he was told he must pay $12.50 per month for a "tow package." In addition, he has paid a total of $1,357.80 in car insurance to the company.
Source: Florida Office of Financial Regulation, 2014
(1, 2, CT)

26. Shortly after a heart attack forced her to retire, Sandra was short on cash. Her ex-husband had fallen behind on his alimony payments, and she didn't receive enough income from her monthly disability checks to cover all her bills. She received a payday loan for $150 from First Southern Cash Advance to pay her overdue telephone bill. The next month, her husband still had not paid the alimony, so she was unable to repay the loan. As a result, she borrowed money from another payday lender, then from a third and fourth just to attempt to pay off one loan and the interest. By the time she sought help from a legal aid attorney, Sandra was forced to give up her apartment and move into a trailer in her brother's backyard.
Source: Yeoman, Barry. "Sudden Debt." AARP Magazine September & October 2006: 108-113, 128. Print.
(2, 3, SL)

27. Amy Keaton of Spring Hill, MO said during a public comment session that desperation led her to take out a $200 payday loan a year ago. "You get into that mindset when you are struggling that tomorrow will take care of tomorrow," Keaton said. "So I took out the loan, even though I knew that it wasn't a very good idea." Keaton said the lenders expected a payment of $297, and in return she would receive $250 for her bills. The amount she actually ended up paying escalated. "I was paying almost $100 a month just to take my own paycheck home," she said. Keaton will have her debt paid off this September with the help of Catholic Charities.
Source: http://www.kansascity.com/news/business/article81380962.html
(1, 2, SL)

28. Terrence Wise, who supports tighter regulation of the industry**,** said a $150 payday loan ended up costing him $400. "They were calling my job and harassing me at work," Wise said. "My employer told me I could be disciplined if they didn't stop harassing me. I had papers brought to my home serving me to court. And all of these things, they make you feel degraded."
Source: http://kcur.org/post/hundreds-rally-downtown-public-hearing-proposed-payday-loan-rules#stream/0
(2, SL)

29. Maryann Olson's monthly Social Security check wasn't enough to cover the cost of orthopedic shoes that she desperately needed so she turned to a payday lender. However, her $150 loan quickly turned into $1,900 in debt.
Source:http://www.oregonlive.com/opinion/index.ssf/2015/03/congress_must_crack_down_on_pa.html
(2, SL)

30. "We got a payday loan of about $200," Lara said. By the time payday came around the lender wanted $300. They were able to pay back the $300, but they came up short on their next payment. "So we took out another loan," Lara explained. And just like that, the trap door slammed down. "It's just so easy to get. So easy! You just bring a paystub down and you tell them how much you need," Lara said. "I kid you not, we did that dance for close to six months," Lara said. "It was horrible. Just unbelievably horrible." Finally, Lara had to beg her parents to help get them out of the cycle for good.
Source: http://www.tcdailyplanet.net/new-guidelines-nonprofits-help-curtail-predatory-payday-loans-in-minnesota/
(1, 2, SL)

31. Diana, a 71-year-old who lived on her Social Security income of $1,100 per month, took out a car title installment loan from Cash America for $1,533. The loan carried an APR of 98%, and she was required to make 13 payments of $195 each. $551 of the loan went to pay off an old lien. Diana subsequently obtained a Cash Plus 0% APR single-payment payday loan for $225 while her car title loan was outstanding. Cash Plus pursued criminal charges for "theft by check", which is essentially Texas's bad check law. There is now a warrant outstanding for Diana's arrest.
Source: Loan contracts on file with CRL
(2, 3, CT, LT)

32. John lived paycheck to paycheck. In December 2013, he took out a car title installment loan with Loan Max for $1,715, requiring 12 monthly payments of $391 each, totaling $2,969 (243% APR). John struggled to make the first two payments and was struggling to make the third. Two months later, in February 2014, he took out a $700 payday installment loan from Check N Go to stay current on his car title loan. The payday loan required 11 biweekly payments of $110 each (247% APR). Of the first payment of $110, only $14 went toward the loan principal. John defaulted on that loan after one payment and was incurring substantial overdraft fees as the bank threatened to close his account. He has no hope of keeping up with his loan payments, much less escaping the debt trap. The extreme stress prevents him from sleeping, and he likely will be forced into bankruptcy.
Source: Loan Max and Check N Go loan contracts on file with CRL
(1, 2, LT, CT)

33. In 2009, Pamela received a payday loan from Cash Transfer Centers for $960 on a two-week period, plus a finance charge of $259.20. The loan required payments of $160 in order to be paid off. Once Pamela saw that her monthly payments stayed the same while the interest on the loan continued to grow, she knew there was something wrong.
Source: Office of the Attorney General, Commonwealth of Kentucky, 2010
(2)

34. In 2010, Anne received a $1,000 payday loan, which required repayment every two weeks. However, her payments were doing very little to decrease the size of the loan, and eventually, she had paid $1,689 but still had an outstanding balance of $1,082. Moreover, because the bi-weekly payments were being drawn directly from her bank account, she began to incur overdraft fees from her bank and was forced to close her bank account to stop the overdraft fees.
Source: Office of the Attorney General, Commonwealth of Kentucky, 2010
(1, 2)

35. Mary received a $300 payday loan from Fast Cash Advance in late 2009. She repaid the $300 loan and upon learning that Kentucky had made internet payday lenders illegal in January of 2010, Mary closed her bank account in order to stop Fast Cash Advance from continuing to withdraw funds from her bank account. Fast Cash Advance sold her remaining debt to another company who then turned the account over to a collection agency.
Source: Office of the Attorney General, Commonwealth of Kentucky, 2010
(2)

36. Christine obtained a payday loan from US Fast Cash for $350 in May 2007. The contract stated that she would owe a total of $455, which reflects an APR of 496.73%. When Christine discovered that payday loans were illegal in Kentucky, she repeatedly contacted US Fast Cash to inform the company that she would instead pay a total of $411.61, the maximum amount allowed under State law for a $350 loan. However, US Fast Cash insisted that she owed $560 in payments and sent her a threatening and intimidating email accusing Christine of "unreasonable demands" and trying to "set the terms" of the loan and stating that no one "twisted [her] arm" to obtain the loan.
Source: Office of the Attorney General, Commonwealth of Kentucky, 2007
(2)

37. 500FastCash solicited Beverly via email to obtain a payday loan for $300, and she accepted. She had an agreement with 500FastCash to debit her bank account on Fridays as she is paid on those days. Instead, the company debited her account on Thursdays before she was paid, which resulted in extensive bank overdraft fees. Beverly's bank closed her checking account, and she has hired a bankruptcy attorney. Moreover, 500FastCash has put her employment in jeopardy. The company has harassed her at work, calling her office despite her numerous emails to the company stating that she is not allowed to receive personal calls during work hours.
Source: Office of the Attorney General, Commonwealth of Kentucky, 2010
(2, 3)

38. Kenneth obtained a $250 payday loan and paid a total of $389 on the loan. Shortly thereafter, he took out another $250 loan with an APR of 547.5%. He paid $75 toward the new loan, but combined with the overdraft fees he had already been charged on the first loan, he had paid a total of $500. Kenneth asked the company to mark his account paid in full as he had repaid the $500 total principal amount of the two loans, but the company refused and continued to call him even though he requested that all correspondence be in writing.
Source: Office of the Attorney General, Commonwealth of Kentucky, 2010
(1, 2)

39. Doris received a $350 payday loan from Ameriloan. She was disabled and living on Social Security, and made an arrangement with the company to debit her checking account four times on the days she received her payments. Instead, Ameriloan twice debited her account the day before she received her Social Security check and she incurred overdraft fees. Moreover, after taking out the four payments she and the company had agreed upon, Ameriloan told her she still owed $455.
    Source: Office of the Attorney General, Commonwealth of Kentucky, 2010
    (2, 3)

40. Carole received several payday loans in 2007 from different companies, including Ace Cash Express, Quik Cash, and Check 'N Go. She was on a fixed income consisting only of her disability payments, and she knew she could not afford to pay the balance of the loans. The companies never verified how many outstanding loans she had or whether she could actually pay the loans back. She notified each company that she wanted to pay the balance on her loans but could only pay $10 a month because she needed to have enough money to purchase her medication. Carole's son received a call from a person claiming to be a lawyer who told him that his mother was engaging in check fraud due to the outstanding payday loan. The caller instructed him to tell his mother to buy a prepaid card with $120 on it and to send her the routing number. She was collecting for a payday loan through Ace Express, which Carole could not to pay on, and the total loan price had ballooned up to $839.93. Carole could not afford to buy the prepaid card and was concerned that she would be sued by the company.
    Source: Office of the Attorney General, Commonwealth of Kentucky, 2010
    (2, 3)

41. Joseph received a $500 payday loan from Eastside Lenders with a $150 recurring payment every two weeks. After the company deducted $150 from his account three times for a total of $450, Joseph was told that he still owed $650. He sent Eastside Lenders an email to let them know that he was revoking his ACH agreement under the Federal Electronic Funds Transfer Act, but they continued to debit his account.
    Source: Office of the Attorney General, Commonwealth of Kentucky, 2010
    (2)

42. Dennis received a $300 payday loan, and was under the impression that he would owe a total of $390 on the loan. Every payday, $90 was debited from his bank account. The company continued to withdraw money, and by the time he was forced to close his bank account, he had paid a total of $990 on a $300 loan. After his account was closed, the payday lender began calling his place of employment despite Dennis's requests that all correspondence be in writing, and the company has threatened to sue him and garnish his wages.
    Source: Office of the Attorney General, Commonwealth of Kentucky, 2010
    (2)

43. In a 2012 court case initiated by the New Mexico Attorney General, Endow testified about her borrowing experience with FastBucks. She stated, "I didn't buy no TV. I didn't buy no jewelry. I didn't go on trips. It wasn't any joyous ride to go to the casino…It was basically to care of my family and put a roof over our head." She earned a mere $18,000-$19,000 a year, yet managers at FastBucks only asked for her pay stubs and bank statements rather than her expenses or other outstanding loans. Endow testified that eventually she had several outstanding loans and would use the proceeds of one to pay off the others. "I was starting to get stressed and

overwhelmed," she said, becoming tearful again on the witness stand. "What am I going to do? How am I going to make it? Is it ever possible to get out of this?" Nevertheless, Endow managed to pay back her loans without going into default until her last loan.
Source: *New Mexico Attorney General v. FastBucks*, 2012
(1, 2)

44. After Joe received a payday loan, he became unemployed. He owed CashNet one more payment of $332.22, so he explained the situation to a representative of the company. They said that they understood. He then received a call at his parents' home, stating that a collection agency needed to speak to him concerning check fraud. CashNet had sold his account to a third party without telling him, and the collection agency attempted to charge a bank account that had been closed. Although he had previously told CashNet he closed that bank account and would need to pay with a new debit card, the collections agency accused him of committing check fraud. The accusation of check fraud has caused unnecessary tension and stress between Joe and his parents.
Source: Alabama Attorney General's Office, 2011
(2, 3)

45. After receiving a $250 payday loan from EZ Money, Terri was contacted by the company at her place of employment. Despite the fact that she informed EZ Money she could not receive personal correspondence at work, the company sent a letter to her job informing her that she had an outstanding balance on her loan. The letter even included the name of Terri's supervisor, which Terri interpreted as a threat to contact her employer.
Source: Alabama Office of the Attorney General, Consumer Affairs Section, 2010
(2, 3)

46. Robyn received a payday loan from National Credit Consultants three years ago. After making three sizeable payments to the company, Robyn asked to have her due date pushed back just one day. The company refused, threatened to have her arrested, and insinuated that they would contact her place of employment. Robyn has been brought to tears several times and feels sick from the stress of the 4-5 calls she receives from National Credit Consultants each time a payment is due.
Source: Florida Attorney General's Office, 2011
(2, 3)

47. Justin received a payday loan for $450 from CashNet USA. Shortly thereafter, he noticed there was an additional $250 deposit in his bank account. He discovered that the credit was for a loan that he never applied for. He called the company and was told that CashNetUSA created a new loan on top of the one he already had because he had "shown interest." The company told him he should have declined the loan within three days if he did not want it, which he was unable to do because he had been out of town with no access to internet to check his bank account. Justin's bank account has been debited repeatedly for payments for the two loans; as a result, he has accrued $450 in bank overdraft fees and his bank has restricted the use of his debit card.
Source: Florida Attorney General's Office, 2008
(2)

48. A San Antonio family requested assistance from their church in developing a household budget and becoming financially independent. In the course of developing a budget, the church deacon

discovered that the family would be able to live within their means except for one item of debt that was dragging them down: a $700 payday loan they had taken out roughly four months earlier to help with a rent payment on their home. The terms of the loan: $200 every two weeks was automatically deducted from the husband's bank account and timed with the deposit of his paycheck. This $200 did not reduce the original amount of the loan. It merely allowed for the $700 principal to roll-over until the next pay-period. In the course of the four months the family had maintained this loan, they had rolled the principal over nine times—at a cost of $1,800. Now, as they approached the church again for help, they needed help to pay their rent or face eviction.
Source: http://www.christianitytoday.com/local-church/2016/july/texas-pastor-payday-loan-reform-isnt-distraction-its-christ.html
(1, 2, 3)

49. Dodie received a $500 payday loan from National Payday. The company now says that she owes over $1,200 on the loan but will not explain the extra fees. National Payday has called her employer, her family, and her husband's employer and has threatened to file criminal charges against Dodie. Her mother had a heart attack after one of the company's harassing phone calls. Dodie informed National Payday that she has filed bankruptcy, but the calls continue.
Source: Florida Attorney General's Office, 2006
(2, 3)

50. Over a 17-month time period, Lisa, a single mom living in North Carolina, received 35 payday loans from Urgent Money Service – roughly one loan every two weeks. She spent over $1200 in fees for a $255 cash loan that kept rolling over because she could never repay the loan within the two-week period. Each time, she would write a check for $300 and receive $255 back in cash. Urgent Money Service never took into account Lisa's income and expenses. Each of her biweekly paychecks amounted to only $600, so she was left with only $300 for her other bills and expenses until her next paycheck. The debt trap cycle continued as she couldn't afford to pay back the loan and couldn't stretch her remaining $300 to cover all her bills without obtaining yet another loan. The only way she could stop the withdrawals from her bank account was to close her account. It took her two years to finally pay off the $255 loan.
Source: Commerce Committee meeting testimony, North Carolina General Assembly, 6/17/2003
(1, 2)

51. Lenny, who made about $600 a week, went to Advance America thinking a payday loan would help him catch up on an overdue bill. Over a year later, he had renewed his Advance America loan every two weeks, fallen deeper into debt, and taken a second payday loan to stay afloat. Lenny lost his apartment and ended up in a homeless shelter. While he lived there, Advance America continued to flip his loan, charging $20 per $100 every two weeks, 521% APR.
Source: *Caught in the Trap: The real story from payday lending borrowers* – CRL Issue Brief, June 2010
(1, 2, 3)

52. Mr. & Mrs. Anderson were unable to cure the default on their home loan because of their payday loans. A construction worker, Mr. Anderson had taken out payday loans from Advance America to help them through a bout of bad weather that slowed his work. They paid $200 every two weeks in fees to Advance America, for loans in both his and her names. This debt disqualified the couple for their loan modification.

Source: *Caught in the Trap: The real story from payday lending borrowers* – CRL Issue Brief, June 2010
(3)

53. Jason, a military service member who worked on a nuclear submarine in Kings Bay, Georgia, borrowed $300 from Advance America to make ends meet after being in a car accident. He soon found himself taking out loans from other payday lenders as he fell further and further behind. "In five months, I spent about $7,000 in interest, and didn't even pay on the principal $1,900. I was having marital problems because of money and didn't know what to do for Christmas for my kid," Jason told an AP reporter. The base emergency relief office finally helped Jason by paying off his triple-digit payday loans, some as high as 780% APR, and letting him repay the charity's interest-free loan over 18 months.
Source: *Caught in the Trap: The real story from payday lending borrowers* – CRL Issue Brief, June 2010
(1, 3)

54. Clarissa and her 15-year-old son put in more sweat equity hours than required on their Habitat for Humanity house, in joyful anticipation of living in their own home. Clarissa worked full time, but received no child support and struggled to manage her expenses, sometimes taking on a second job. When the company she worked for shut down, Clarissa borrowed from Advance America and Nationwide. Eventually, when she couldn't repay one of her loans, the payday company deposited the check they were holding as collateral. The check bounced and both her bank and the payday lender charged her additional fees for insufficient funds.
Source: *Caught in the Trap: The real story from payday lending borrowers* – CRL Issue Brief, June 2010
(2, 3)

55. Anita went to an Advance America store in hopes of finding a solution to a common problem -- how to delight her grandkids on Christmas. Unable to repay the loan, she had to renew her loan with Advance America every payday, paying $45 to keep the same $300 loan outstanding. She went to a second payday lender, Check 'n Go, to help repay Advance America. Anita could not afford the $820 it would take to pay off the two loans in full and get out of the trap. After just four months, she had paid almost $1,000 in fees, and still owed the $820. "I got a promotion and a raise, but I never saw any of that money," said Anita. She finally went to her church to get help paying the rent, and to a consumer credit counseling agency to get help negotiating a repayment plan. It took her nine more months to complete these payments.
Source: *Caught in the Trap: The real story from payday lending borrowers* – CRL Issue Brief, June 2010
(1, 2, 3)

56. Danny, a forklift operator from Kannapolis, was making $9.00 per hour. He got behind on his bills after being hospitalized from a heart attack and stroke. He went to his first payday lender in March 2000 and borrowed $300 for a 7-day term. This was about the same as his weekly pay, so he could not afford to pay back the loan, and got caught in the debt trap. Over the course of two years, Danny used eight different lenders including Advance America, Advance Internet, Check into Cash, and First Southern Cash Advance. He paid more than $5,000 in fees over the next two years, with over 170 check stubs for payments to these payday lenders.

Source: *Caught in the Trap: The real story from payday lending borrowers* – CRL Issue Brief, June 2010
(1, 2)

57. Stephanie paid her first payday loan back the first time when it was due on payday, but a few days later came up short again, so she took out another loan. "I was paying the fees, but still coming up short on bills. So I got a loan from another lender just to pay the fees on my other loans. I ended up with several loans from different payday lenders, struggling to pay the interest every two weeks so I wouldn't default, because if I did they would have passed my check to the bank." Stephanie had loans with Advance America, Check Into Cash, Check 'n Go and several others. Eventually she was paying $800 every month just in interest fees, without paying down any principal. "The payday lenders were not willing to work with me, even after I talked to them about my situation following the advice of my credit counselor," she said. One payday lender threatened to send her check to the magistrate's office, and to take her to court for writing a bad check.
Source: *Caught in the Trap: The real story from payday lending borrowers* – CRL Issue Brief, June 2010
(2)

58. Betty, a senior in Durham, took out a small $100 payday loan. She had no other debt at the time. When this loan came due a month later, she borrowed from a second payday lender to repay the first. And, then she did this four more times. Each time, it was slightly less expensive to flip a loan than to pay the bounced check fees if she defaulted. With six loans, she was paying over half of her $564 monthly Social Security income in payday fees, never paying down a penny of principal on these loans. She lost her phone and got one-time emergency help from social services to avoid eviction. We suspect Betty was later evicted when we could no longer reach her at her apartment.
Source: CRL Issue Brief: *Why We Must Keep Payday Lenders Out of NC: North Carolinians Caught in the Debt Trap*, April 2016
(2, 3, SL)

59. With retirement and disability income, Mary, a 62-year-old African American mother and grandmother, brought in about $1,000 per month. She took out her first payday loan because she needed "a little extra" money to go out of town. Like many borrowers, she had to take out a second loan to pay off the first. She ended up with loans from four payday lenders. "When I get a little extra money, I'm going to pay them off and I'm through with them," said Mary. "It's a rip off. There's nothing cute about it. I'm supposed to get some money, but I lose money." The fees Mary paid to keep from defaulting on her payday loans added up to over 40 percent of her monthly income.
Source: CRL Issue Brief: *Why We Must Keep Payday Lenders Out of NC: North Carolinians Caught in the Debt Trap*, April 2016
(2)

60. After her husband was laid off, Pamela borrowed $500 from a payday lender. But the Phoenix, Arizona, woman found that she, like many other borrowers, could not manage to repay the $588 she owed ($500 plus $88 in fees) when it was due in two weeks. She went to a second lender to pay the first, and a third to pay the second, getting in deeper until she had five loans of $500. She was paying $880 every month in payday fees, never paying down the principal owed.

By June of 2004, she had paid $10,560 in interest on these five loans. She was afraid of going to jail if she stopped paying the fees, and had no idea how to get out of the trap.
Source: CRL website: *The Victims of Payday Lending*.
http://www.responsiblelending.org/issues/victims-payday.
(1, 2)

61. Kym, a single mother working as a temp in the Triangle area, took out a payday loan when a friend told her about how she could borrow money until her next payday. She quickly fell into the debt trap, and had to pay a high fee every payday to renew the loan and avoid default. When she had trouble keeping up this cycle, she took out a second loan to pay fees on the first. She paid on both loans for about a year, finally convincing one of the lenders to let her pay off the loan in increments. It took Kym another eight months to shake free from the debt trap.
Source: CRL website: *The Victims of Payday Lending*.
http://www.responsiblelending.org/issues/victims-payday.
(1, 2)

62. As a grad student in North Carolina's Triangle area, Allen found it very difficult to pay off the four payday loans he had accumulated. When he did manage to pay off one or two of the loans, he soon found himself strapped for cash and forced to renew the loan. Allen finally sought help from a credit counselor. He sent letters to the payday lenders asking for a payment plan he could afford. But instead of helping him work out payments, one of the lenders deposited his check upon receiving his letter, and it bounced twice before he could cancel the check. Two other lenders were internet-based companies who automatically drafted his checking account. He had to close his account to stop them. When one of these lenders received Allen's payment plan letter, they called and threatened to send a sheriff to his house and serve him court papers. Allen now realizes he has technically repaid the debt several times over in rollover fees.
Source: CRL website: *The Victims of Payday Lending*.
http://www.responsiblelending.org/issues/victims-payday.
(2)

63. Rhonda and her two daughters experienced a financial crisis last summer that sent Rhonda looking for help from payday lenders. She found not the help she needed, but disaster. Rhonda fell into the payday lending debt trap - the terms of the loans she took out required her to either pay them off in less than two weeks or have $90 fees automatically debited from her bank account repeatedly. Those loans, at triple-digit APR, have cost her much more than the exorbitant fees. Her family's finances are in ruins and she is planning to file bankruptcy.
Source: CRL website: *The Victims of Payday Lending*.
http://www.responsiblelending.org/issues/victims-payday.
(1, 2, 3)

64. Like many borrowers, Janis went to one payday lender to get help paying the fees of another. She ended up borrowing from three different lenders. Since she could not pay the loans in installments, she paid the repeat fees until she got her tax returns. When she couldn't keep up with the fees one lender demanded, they called and left her a message saying that they would take her to court if her account was short. It was several months before Janis found her way out of the trap, and she needed help from social services during this time, once to pay her rent and twice to pay her light bill.

Source: CRL website: *The Victims of Payday Lending*.
http://www.responsiblelending.org/issues/victims-payday.
(1, 2, 3)

65. Sandy's first payday loan was for $100, with an $18 fee. She worked down the street from the payday shop, and since she was short on cash, she called to see what she needed to get a loan. All she needed was a source of income and a banking account, so she walked into the shop, and walked out 15 minutes later with the loan. Sandy got caught up in the payday lending debt trap, taking out multiple loans to pay the fees on each one as they became due. At one point, she was paying $300 every two weeks for four different loans. Over a six-month period, this added up to $3,600, but she was in the trap much longer, paying off one loan, then another, until she lost her job and could no longer keep up with the fees. She filed bankruptcy.
Source: CRL website: *The Victims of Payday Lending*.
http://www.responsiblelending.org/issues/victims-payday.
(1, 2, 3, SL)

66. Betty, a senior citizen in Durham, North Carolina, paid over half of her $564 monthly Social Security income in payday fees, never paying down her loans. She lost her phone and needed emergency help from social services to avoid eviction.
Source: CRL website: The Victims of Payday Lending.
http://www.responsiblelending.org/issues/victims-payday.
(2, 3)

67. Mr. R utilized payday loans for temporary help when he struggled to pay his bills. He ended up taking out at least 24 loans over the course of four years, becoming trapped in the payday debt cycle. His final loan was from a tribal payday lender who took $250 out of his bank account every two weeks. Only $50 of the payment applied to the principal of the loan, with the remaining $200 going towards fees. Eventually Mr. R was forced to close his credit union account, and even though he had repaid the principal several times over, he was harassed with round-the-clock phone calls from the payday lender.
Source: Brief of *Amici Curae* Nine Advocacy Organizations in Support of Defendants-Appellees Urging Confirmance, *The Otoe-Missouria Tribe of Indians v. New York State Department of Financial Services*, No. 13-3769 (2nd Cir. Nov. 13, 2013).
(1, 2)

68. Patricia paid half of her income every pay period to internet payday lenders. She obtained five internet payday loans, including one from a tribal lender, with a total of $2,000 to help pay her bills after incurring unanticipated medical expenses. The APRs on the loans ranged from 620% to 990%. The lenders took close to $600—half of her income—from her bank account every two weeks. After she had repaid more than the principal amounts of the loans, she closed her bank account to stop the lenders' debits.
Source: Brief of *Amici Curae* Nine Advocacy Organizations in Support of Defendants-Appellees Urging Confirmance, *The Otoe-Missouria Tribe of Indians v. New York State Department of Financial Services*, No. 13-3769 (2nd Cir. Nov. 13, 2013).
(1, 2)

69. Ms. B is a 71-year-old whose only income is her Social Security benefits and her pension. In November 2012, she received payday loans from three different lenders to help pay her bills.

Immediately, she struggled with the payments, which caused her to fall further behind on her rent and other bills. As a result, she took out another payday loan in January 2013. Fortunately, she was able to stop the lenders' withdrawals by closing her bank account, but they continue to harass her by phone and email, even threatening to sue her on the illegal loans.
Source: Brief of *Amici Curae* Nine Advocacy Organizations in Support of Defendants-Appellees Urging Confirmance, *The Otoe-Missouria Tribe of Indians v. New York State Department of Financial Services*, No. 13-3769 (2nd Cir. Nov. 13, 2013).
(2, 3)

70. Ivy, a retail worker from Brooklyn, took out six internet payday loans carrying APRs as high as 782%, to help pay her bills. The payday lenders continuously drained her bank account, often triggering overdraft fees. In a two-month period, the lenders tried to debit her account 55 times, and she was charged $1,500 in overdraft fees as a result. Because she was unable to pay the overdraft fees, her bank closed her account and reported her to ChexSystems, a consumer reporting agency, to prevent her from opening accounts at other banks.
Source: Brief of *Amici Curae* Nine Advocacy Organizations in Support of Defendants-Appellees Urging Confirmance, *The Otoe-Missouria Tribe of Indians v. New York State Department of Financial Services*, No. 13-3769 (2nd Cir. Nov. 13, 2013).
(1, 2, 3)

71. Subrina's exempt child support funds were seized by her bank after she took out three internet payday loans to help pay her bills. The lenders withdrew as much as $168 in fees from her bank account biweekly, while her bank charged her $800 in overdraft fees as a result of the repeated debits. Further, the bank illegally seized more than $600 in child support funds to cover the fees. The payday lenders refused to stop debiting her account. The bank eventually closed the account, but repeatedly called her to pay the overdraft fees and reported her to ChexSystems, a consumer reporting agency, to prevent her from opening accounts at other banks.
Source: Brief of *Amici Curae* Nine Advocacy Organizations in Support of Defendants-Appellees Urging Confirmance, *The Otoe-Missouria Tribe of Indians v. New York State Department of Financial Services*, No. 13-3769 (2nd Cir. Nov. 13, 2013).
(2, 3)

72. Cynthia, a New York City employee and single mother, borrowed eight payday loans over the course of several months when she fell behind on her rent. Soon, her entire paycheck was swallowed by the lenders. One company that debited money from her account never even made her a loan, but simply obtained personal and financial information from another lender and began electronically debiting her account. Cynthia's bank charged her $1,390 in overdraft fees, seized $721 in child support funds, closed her account, and reported her to ChexSystems so that she could not open an account at another bank. Two years later, debt collectors continue to harass Cynthia to repay the illegal loans.
Source: Brief of *Amici Curae* Nine Advocacy Organizations in Support of Defendants-Appellees Urging Confirmance, *The Otoe-Missouria Tribe of Indians v. New York State Department of Financial Services*, No. 13-3769 (2nd Cir. Nov. 13, 2013).
(2, 3)

73. Yesenia's mother was diagnosed with breast cancer and could no longer work, so Yesenia borrowed $510 (two loans of $255 each) to help pay the rent. She was trapped in a cycle of debt for 5 months, where she paid $90 every two weeks in fees alone. When she became late on a

payment to the payday lenders, they debited her bank account for the full amount of the loan, wiping out all of her funds and causing her to incur overdraft fees. A non-profit charity called Season of Sharing helped her pay one month's rent and she was finally able to pay back the loans. She paid $900 in fees to borrow $510.
Source: http://www.responsiblelending.org/issues/payday-loans-california-video
(2, 3)

74. George, an elderly man living in California, borrowed $1,020 (4 payday loans of $255 each). He was stuck in a debt trap for three years and paid $180 in fees every two weeks. Dolores Street Community Services helped him find his way out of the debt trap. He paid $12,960 in fees to borrow $1,020.
Source: http://www.responsiblelending.org/issues/payday-loans-california-video
(1, 2)

75. Michael borrowed approximately $1,530 (six payday loans of about $255). He has been stuck in the debt trap for more than two years and pays $270 per month in fees alone. Michael's monthly fees take a quarter of his Social Security benefits. He is working with a non-profit organization called Community Housing Works to help him get out of the debt trap. So far, he has paid more than $6,000 in fees to borrow $1,530.
Source: http://www.responsiblelending.org/issues/payday-loans-california-video
(1, 2)

76. Kimberly borrowed $1,550 from three different payday loan companies: one store front, one online, and one bank payday loan. She was stuck in a cycle of debt for nearly six months. She stopped paying her electric bill, went without power, and stopped buying groceries until she was able to pay back all her loans. She paid more than $2,800 to borrow $1,550.
Source: http://www.responsiblelending.org/issues/payday-loans-california-video
(1, 2, 3)

77. In June 2014, Dina took out a $4,570 installment loan from NetCredit. She was behind on her mortgage payments and other household bills and thought the loan could help her get back on track. The interest rate was advertised as 5% but in fact the loan carried an APR of 64%. The loan contract requires her to pay $135 every two weeks for three years, which means she will have paid more than $10,530 to borrow $4,560. Because she is paying $270 per month, she is having a hard time making her mortgage payments. Since obtaining the loan, Dina has been late on her mortgage every month and her credit score has dropped to 590. Instead of helping her get out of financial distress, the loan has put her in an even worse situation.
Source: CFPB complaint, NetCredit loan contract
(1, 2, 3, LT)

78. In May 2013, National Financial, LLC loaned $200 to Gloria James, a resident of Wilmington, Delaware. James worked in the housekeeping department at a hotel, earning $11.83 per hour. As a part-time employee, her hours varied. On average, after taxes, James took home approximately $1,100 per month. National described the loan product as a "Flex Pay Loan." In substance, it was a one-year, non-amortizing, unsecured cash advance. The terms of the loan called for James to make twenty-six, bi-weekly, interest-only payments of $60, followed by a twenty-seventh payment comprising both interest of $60 and the original principal of $200. The total repayments added up to $1,820, including $1,620 in fees. According to the loan document

that National provided to James, the APR for the loan was 838.45%. Before this loan, James had obtained five prior loans from National. For her first loan from National, James borrowed $100 on September 1, 2011. She repaid a total of $205 by making five payments over the course of two months. For her second loan, James borrowed $100 on August 22, 2012. She again repaid a total of $205, this time by making four payments over the course of two months. For her third loan, James borrowed $150 on October 31, 2012, less than two weeks after repaying her second loan. She repaid a total of $252 by making three payments over the course of two months. For her fourth loan, James borrowed $100 on December 20, 2012, one week after repaying her third loan. She repaid it the next day by making a single payment of $102. The prompt repayment suggests that James refinanced her loan through another provider. For her fifth loan, James borrowed $200 on December 27, 2012, less than one week after repaying her fourth loan. James failed to make the second payment, failed to make the fourth payment, and finally repaid the loan two months later. Her repayments totaled $393. Despite James' difficulty in repaying her fifth loan, National sent her text messages soliciting her interest in another loan. A text message on March 29, 2013, stated, "Loan Til [sic] Payday welcomes you with open arms. If you ever need a loan again we want to be your source! :)" A text message on April 5, 2013, stated, "Loan Til [sic] Payday misses you! Call NOW and receive $20 off your first payment."
Source: *James v. National Financial, LLC*, 132 A.3d 799, 805 (Del. Ch. 2016)
(1, 2, LT, SL)

79. Realizing that her next payday was two weeks away, Leticia Ortega worried about how she was going to get enough cash to pay overdue telephone and electric bills. Then Ortega, a cashier in San Antonio, Texas, spotted an advertisement by National Money Service in a local weekly newspaper. National Money Service charged her a $90 interest fee for a $300 loan, due by her next payday. This fee amounts to an APR of 780%. When the loan's due date arrived, Ortega did not have sufficient cash to repay the entire loan. Consequently, for almost a year, National Money Service debited Ortega's bank account every two weeks in the amount of $90 as interest to "roll over" the loan. Because none of the $90 interest payments counted as principal, Ortega still owed National Money Service $300 even though she had paid $1,800 in interest charges.
Source: Creola Johnson, *Payday Loans: Shrewd Business or Predatory Lending?*, 87 Minn. L. Rev. 1, 2–3 (2002)
(1, 2)

80. When her job sorting jeans at a garment factory didn't pay the bills, 47-year-old Patricia Turner went to E-Z Check Cashing of Cookeville, Tennessee. E-Z loaned her $300 for 30 days, and Turner secured the loan by writing a check for $405, $105 of which was for interest and "Other Charges." The APR on this loan was over 400%. At the end of the 30-day period, Turner was unable to repay the loan. She did not have enough money in the bank to cover the check or enough cash to pay the debt outright. She could have defaulted, but instead she chose to extend the loan by paying a cash extension fee of $105. After she extended the loan eight times, paying $840 over an eight-month period without reducing the principal of the loan, she was unable to pay either the balance of the loan or an additional extension fee. With full knowledge that there were insufficient funds in her account to cover it, E-Z then deposited Turner's eight-month-old check into its account. When the check bounced, Turner was forced to declare bankruptcy.
Source: Charles A. Bruch, *Taking the Pay Out of Payday Loans: Putting an End to the Usurious and Unconscionable Interest Rates Charged by Payday Lenders*, 69 U. Cin. L. Rev. 1257 (2001)
(1, 2, 3)

81. On a monthly basis from March 2005 through November 2007, Wilma A. Ruby entered into a total of 33 payday-loan agreements with Cashnet, Inc., d/b/a Cash Advance Centers. The amount of each loan increased over time, starting at $200 and reaching $500. Typically, Wilma would pay $575.00 in cash to Cashnet and would immediately enter into another payday loan agreement with Cashnet for $500. Wilma was to repay the $500.00 plus a 15% finance charge of $75.00 (for a total of $575.00) to Cashnet one month later. On the due date, Wilma would again pay $575.00 in cash to Cashnet and immediately enter into another loan with the company. This cycle continued until November 2, 2007, when Ruby entered into her final payday-loan agreement with Cashnet for $500. She could not repay this loan. With a fixed income of only $624.00 per month, Ruby could not afford to repay in full her loan with Cashnet and meet her monthly expenses. Thus, each time she repaid in full one loan, she immediately had to obtain another, usually for the same or a greater amount.
    Source: *Ruby v. Cashnet, Inc.*, 281 Va. 604, 607, 708 S.E.2d 871 (2011)
    (1, 2, SL)

82. On December 14, 2010, Timothy Williams obtained a short-term personal loan from Valued Services. The loan was for $550, and was due to be repaid approximately one month later. The APR was listed at 385.28%, with a total finance charge of $156.75. On January 10, 2011, the day the December loan was due, Williams obtained another loan from Valued Services to repay the December loan. The January loan was for $706, with APR of 246.51%, and a total finance charge of $1,241.40. It required Williams to repay the loan in 12 monthly payments, beginning February 9, 2011. Valued Services made high-interest loans to Williams despite the fact that Valued Services' files showed Williams' sole source of income was a monthly social security payment of $1,147. It also showed that in November 2010, Williams had an ending checking account balance of $8.32.
    Source: Williams v. Valued Servs. of Wisconsin LLC, No. 2012AP2115, 2013 WL 4016941 (Wis. Ct. App. Aug. 8, 2013)
    (1, 2, LT)

83. In March 2012, Rodella Smith obtained a loan for $5,000 from Western Sky Financial. The loan was subject to an APR of 116.73%, and the repayment term was set for a period of about seven years, resulting in a total payment of $41,172.61. She made payments of $480 for over two years, paying Western Sky approximately $13,000 in total—more than double the original loan amount. She then refused to make any more payments, and that's when the company began calling Smith's work and home phone numbers and emailing her, demanding ongoing payments and threatening to report Smith to credit reporting companies. The company has also called Smith's granddaughter four times accusing her of owing a debt and requesting Smith's contact information. Smith has suffered emotional and mental pain and anguish and damage to her credit as the result of reporting a debt that she does not owe.
    Source: Civil Action Complaint, *Smith v. Western Sky Financial, LLC*, 168 F. Supp. 3d 778 (E.D. Pa. 2016), *appeal dismissed* (Apr. 19, 2016)
    (1, 2, 3, LT)

84. In June 2008, Dominginho Powell obtained a car title loan from The Payday Loan Store of Illinois (PLS) using his 1972 Oldsmobile as collateral. He had been having financial difficulties and needed a loan to make ends meet. The loan was for $2,265 with an APR of 300% and called for two installments: one payment of $558.49 in July and a balloon payment of $2,842 in August.

The finance charge was listed as $1,135.60. PLS knew that Dominginho would not be able to make the balloon payment at the time of the loan but entered into the transaction anyway. When he went in to make the first payment in July, he was told that he had to refinance the loan. He went back to PLS in August to make his second payment, and PLS took a payment for the old loan and told Dominginho that he was required to refinance the remaining balance of $2,263, which was not yet due. PLS flipped his loan seven more times, each with terms more unfavorable than the last. Dominginho was told this is the "way loans work." When he was told he had to refinance for the seventh time, Dominginho realized that he had paid almost $5,000 in finance charges for a loan that was supposed to cost $1,135. He still owes $2,235—almost the original principal amount of the loan.
Source: Complaint, *Powell v. The Payday Loan Store of Illinois, Inc.*, No. 09 C 4146, 2010 WL 3893894, (N.D. Ill. Sept. 28, 2010)
(1, 2, CT)

85. Peter Alfeche entered into 23 payday loans with CashNet over a 10-month period, paying the company approximately $2,000 in fees. Being short on money an unable to meet all of his monthly expenses, Peter first obtained a loan from Cash America in November 2006. He agreed to borrow $250 for nine days for a fee of $62.50, representing an APR of 1,013.89%. Many of his subsequent 22 loans were obtained to pay off previous loans, as he often lacked enough money on the due date to pay off the loan and still pay his recurring expenses. Once Peter had established a personal account with CashNet, he also received email invitations to take out more payday loans from other internet payday lenders. Over the 10-month period in which Peter received the 23 loans from CashNet, he also obtained additional payday loans from some of these other lenders. In addition to paying $2,000 in fees to the payday lenders, he incurred hundreds of dollars per month in overdraft charges from his bank.
Source: Class Action Complaint, *Alfeche v. Cash America International, Inc.*, No. CIV.A. 09-0953, 2011 WL 3565078 (E.D. Pa. Aug. 12, 2011)
(1, 2)

86. Cynthia Williams and her husband were facing financial difficulties, so she decided to apply for and received a payday loan of $500 with an APR of 430% from Advance America. Over the next year, she was trapped in a cycle of debt with the company. Although the payday loans consumed over half of her monthly income, Advance America never considered Cynthia's ability to repay. As a result, she fell behind in her mortgage payments. Cynthia and her husband were only able to save their home with the help of a nonprofit foreclosure prevention group by taking on second jobs and increasing their workload by 70 hours per week.
Source: Plaintiffs' Second Amended Complaint*, Williams v. Advance Am., Cash Advance Centers of Missouri, Inc.*, No. 07-04187-CV-C-NKL, 2007 WL 3326899 (W.D. Mo. Nov. 6, 2007)
(1, 2, 3)

87. In order to evade the Arizona's voter mandate sunset of payday loans, the Ohio-based payday lender CheckSmart started making an open-end line of credit linked to a prepaid card in the months preceding the sunset's effect (and after CheckSmart unsuccessfully tried to push legislation in 2010 to repeal the voter's mandate). While this product is no longer on the market, because it was shut down via regulatory action as an evasion of consumer protections, here is what happened to one Arizona borrower: A 71 year old gentlemen was given one of these open-end line of credit loans by CheckSmart one month before the payday loan sunset in 2010. He was told by CheckSmart that it was his only option. His only income was a monthly

Social Security check of $2,350. The line of credit was for approximately half of this amount: $1,402. The fees then were structured as the following – 36% annual percent interest rate, but a "convenience transfer fee" that were far in excess of the actual interest. Because it was an open-end line of credit, the contract only states a 36% APR, despite all of the additional fees that would add up to an effective triple-digit APR.
Source: Contract on file with CRL
(1, LT, OE)

88. Check Into Cash, a Tennessee-based payday lender, makes open-end lines of credit to borrowers in Virginia. According to a legal services attorney in Virginia, here is one client's story: One woman, now aged 63 and whose source of income is comprised of disability plus a small pension, took out an open-end line of credit from Check into Cash in 2011. She is still paying it off today. She has paid over $3,000 in fees and interest alone on what has been less than $1,000 of credit over that time. This same borrower has another open-end line of credit from California-based payday lender– Allied Cash Advance. With this loan she has paid over $1,100 in fees after being stuck for more than a year in a $360 loan. As further evidence of payday lenders' disregard for the affordability of these loans, this same borrower is stuck also payday and car title loan as well. Because the monthly fees consume such a large amount of her monthly income, she forgoes purchases of the food and medicine she needs.
(1, 3, CT, LT, OE)

89. Single mother Malia Andrews lives in Tennessee, and obtained an open-end line of credit with a 279% APR. When she was short on cash, she took out one of these loans. Although it was touted as a better alternative to payday loans, it was not any better for Andrews. "I just about had a complete meltdown in the car," Andrews recalled, describing the moment she realized it would take years to pay off her flex loan. While approximately $300 of her monthly payment went to interest and fees, only about $20 actually paid down the principal of the loan. If she'd known how much the loan would end up costing her, she never would have taken it out.
Source: http://www.newschannel5.com/news/newschannel-5-investigates/consumer-alert/critics-call-279-loan-a-debt-trap-for-poor
(1, LT, OE)

90. Military veteran Joshua Hause had two existing loans for $925 that he said more than doubled after they were converted to a flex loan, an open-end line of credit carrying a 279% APR. Suddenly, his loan payment was over $2,000 when his original loan principal was less than half that amount. Due to the exorbitant interest and fees, Hause keeps getting farther behind. "If they're going to continue to get higher payments each month, I'll never get out of that hole," he lamented.
Source: http://www.newschannel5.com/news/newschannel-5-investigates/consumer-alert/critics-call-279-loan-a-debt-trap-for-poor
(1, LT, OE)

91. Jennifer Williams of Clarksdale, MS, teaches at a high school but remains in a debt trap due to payday lenders. She at one point owed thousands to nine different payday lenders in three separate towns. What started as a $100 loan when she had just began teaching in 2006 and needed a small amount of money due to her credit cards defaulting in college, had accrued to $4,000 in debt by 2009. She says, "It takes a toll on you, mentally. Those places are the devil. Once you get wrapped into it, it's hard to get out". After her son was born in 2011, she decided

to enroll in a 5-week financial boot camp, which was sponsored by the community bank, Southern Bancorp. As a result of completing the boot camp, she qualified for a savings account, as well as an affordable loan, with which she could refinance her debt. Credit counselor Charlestien Harris from Southern Bancorp states that Jennifer's situation is not uncommon.
Source: http://www.csmonitor.com/Business/2016/0903/Payday-loans-a-scourge-but-still-a-need
(2, SL)

92. Don Miller of HopeLink, a center that assists low-income families and people in Nevada, says that most seniors who he works with are living on $700-900 per month for utilities and rent. Some may take out $150 in payday loans to afford food in a crisis, not realizing that it will take them at least a year or two to pay off. Miller states that many of the seniors go into debt, with at least half of them having taken out payday loans. He also states that they often default on their loans and receive an influx of phone calls from the lenders, who usually threaten to send a lawyer to their homes.
Source: http://www.reviewjournal.com/view/seniors-often-pay-hefty-price-relying-payday-loan
(2, SL)

93. A man confided in pastor Wes Helm about his financial hardship with payday loans. Helm looked through the man's budget and discovered one major monthly expense: a payday loan fee three times more than the loan itself. When the church conducted a further investigation, they found that dozens other families at the church had been victimized by payday lenders as well, sometimes even losing their vehicles and homes.
Source: http://www.npr.org/2016/06/16/481558398/with-payday-loans-burying-borrowers-community-tries-alternatives
(2, 3)

94. Candice Byrd was a payday loan borrower in 2011, when she took out a $500 loan for a car payment. She was working in sales at the time. It was due in six weeks; however, three weeks after she took out the loan, she was advised to take out a new loan. She was told, "You're a good customer. This would be helpful for you." That second loan spurred a two-year cycle of paying off her debt. She eventually lost her car and apartment. She now only pays in cash. She said, "These places want you to keep borrowing. They don't want you to climb out of the hole."
Source: http://www.nytimes.com/2016/06/02/business/dealbook/payday-borrowings-debt-spiral-to-be-curtailed.html?
(2, 3, LT)

95. J.F. from Fresno, California, stated, "About two years ago I used a payday loan to assist with monthly expenses. I thought it would be easy to pay off but then I noticed I could not afford to pay the loan without securing another! The lenders provide little to no other option to pay back the loan which lets you know they aren't concerned with helping you get through the hard spot they are more concerned with keeping you in the endless cycle to pad their pockets! Payday loans are BAD business!!!"
Source: Collected by the California Reinvestment Coalition and quote reprinted verbatim from https://calreinvest.wordpress.com/2016/06/01/california-payday-loan-consumers-share-their-experiences/
(1)

96. S.F. from Oakland, California, shared, “In 2006 I was working full-time but when my boyfriend moved out I had to pay the entire rent myself and had trouble making ends meet. I started to use the payday loans and soon found myself in an endless cycle of debt, having to pay off two or more in cash every two weeks in order to get two more to cover my bills. The loan rates were outrageous and some of these franchises require you pay in cash instead of depositing your personal check. It took me a couple of years to get out of this cycle of debt and it kills me to think of all the money I lost on fees over those years. I will never use those services again. These companies are absolutely predatory and should be fully regulated and restricted since they profit from the people who can least spare the financial fleecing. Thank you."
Source: Collected by the California Reinvestment Coalition and quote reprinted verbatim from https://calreinvest.wordpress.com/2016/06/01/california-payday-loan-consumers-share-their-experiences/
(1, 2)

97. J.J. from Lamont, California, stated that he had "[n]o work, needed money to keep afloat and the lender made it too easy to get loan, a car title loan and it has been a nightmare, do yourself a big favor don’t ever get a title loan!"
Source: Collected by the California Reinvestment Coalition and quote reprinted verbatim from https://calreinvest.wordpress.com/2016/06/01/california-payday-loan-consumers-share-their-experiences/
(CT)

98. M. from San Diego, California, lamented, “I have been caught up in payday loan for over a year now it’s taking all of my money and I don’t know how to get out help."
Source: Collected by the California Reinvestment Coalition and quote reprinted verbatim from https://calreinvest.wordpress.com/2016/06/01/california-payday-loan-consumers-share-their-experiences/
(1)

99. D. D. from Los Angeles shared his story, explaining, “I was in a difficult financial time in my business and needed a $2,500 loan to cover my rent that was due. I had exhausted all my other options and wasn’t expecting any checks for a few weeks. I own my car and decided to go to Loanmart to get a loan. I called them up, told them what I needed and what kind of car they had. They approved me for $3,000, even though I asked them for only $2,500. Considering I was desperate for money, I went ahead with it, not knowing about the interest cap over $2,500. Which I am sure they were well aware of and is why they urged me to get a higher loan. So, after 2 years of paying, I have now given them over $4,500, that’s $1,500 more than the original loan. They say I still owe them $3,000. For a total of $7,500 due on a $3000 loan. It’s highway robbery. These people are awful, they harass me all the time, lie to me about payment due dates and even on one occasion sent me to collections on a missed payment even though I had already paid it for that month from their 3rd party payment site (moneygram). I went and checked and the payment never went through. Which is very suspicious. Now they are threatening to repo my vehicle. I don’t know what to do, this whole experience has been horrible. I am self-employed and struggle enough getting by. I hope someone can sue them for these shady business practices. I will be more than happy to testify against them.”
Source: Collected by the California Reinvestment Coalition and quote reprinted verbatim from https://calreinvest.wordpress.com/2016/06/01/california-payday-loan-consumers-share-their-experiences/

(2, CT)

100. An anonymous borrower reported the following story to the Pew Charitable Trusts, who shared the story with the LA Wave: “I had to come up with money [when] my husband was out of work, and I actually was up to $900 [in storefront payday loan debt]. … My entire check was gone the next two weeks, so that’s when I went to the online ones. … And then after I did the online ones, and got in that loop, and got stuck in there, I went back to the store again, and, yeah, it got bad. And my [checking] account ended up pretty negative. I had to close it out totally.”
Source: http://wavenewspapers.com/payday-lenders-may-face-new-regulations/
(1, 3)

101. Raymond Chaney, now 66, is a veteran who became homeless after he took out a payday loan and spiraled into the debt trap. He needed $400 to repair his broken-down car. Soon enough, he owed mounds of money on several loans to many different lenders. He also owed overdraft fees to banks while paying rent. The payday lenders had full access to his account and eventually took all of his Social Security money. Chaney lost his apartment as a result. The $400 loan led to $3,000 in additional loans, which later accumulated to $12,000 of debt. “I’m not dumb, but I did a dumb thing,” he said. He now lives in a rescue mission located in Boise, and is working with the Idaho Consumer Finance Bureau to pay off his debt. His advice to anyone considering taking out a payday loan is as follows: “I had a friend who had back surgery, and it was so painful...If the choice is between back surgery and dying, consider dying. Well, I give people the same advice about payday loans. If the alternative to a payday loan is dying, think long and hard about dying.”
Source: http://www.nbcnews.com/feature/in-plain-sight/drug-payday-loan-users-hooked-quick-cash-cycle-v18088751
(2, 3)

102. Ann Baddour, Director of Fair Financial Services Project, spoke on behalf of an anonymous borrower at the United Way Leadership Breakfast. She said that the senior citizen, who was living on Social Security, had taken an auto title loan at a value of $2,000 three years prior. She still owed the lender $1,900 after paying off $9,200 on the $2,000 loan.
Source: http://www.tdtnews.com/news/article_fa7d0ea0-7f8f-11e6-9006-afc9a2e7f963.html
(2, CT)

103. As reported by the American Forces Press Service, one military borrower took out a $300 loan when he was desperate for money to help him afford expenses necessary for his three children. He got trapped into the cycle of jumping from lender to lender in order to afford the original loan. The $300 loan soon cost him $15,000.
Source: http://www.military.com/money/personal-finance/credit-debt-management/pay-day-loans-big-business-for-them-headache-for-you.html
(2)

104. Joylynn M. Jossel from Columbus, OH, took out a loan of a couple hundred dollars. She could not pay off the first loan, so she took out a new loan from another payday lender, eventually owing money to four different lenders. Soon she was paying $1,800 each month on payday loans alone. At one point, she had to let a $600 loan she had taken out bounce to avoid dire circumstances. “It was either that or not pay my rent that month,” she says. “It was horrifying. They tell you any and everything to get you to come in and pay for the check that didn't clear.

They'll tell you, 'You're a criminal, you wrote a bad check. That's against the law, it's a felony, you're going to jail.' They call all of your references and your job. It's horrifying. I felt so suffocated. It felt as if I was in this black hole that I just couldn't get out of." Soon enough, the other three loans bounced as well, as she had to afford basic living expenses as well. She faced embarrassment at work when the lender called her at work and the receptionist would say who the caller was in front of the office before turning the call over to Joylynn. "Every time the phone rang, I'd jump like I was the next one in a horror movie to be taken out. I'd fear they'd come to my house because I'd known them to go to people's houses before. I felt guilty just putting gas in my tank. I felt guilty buying food. I felt as though any money I got should be going to the payday lenders and collection agencies to get them off my back." Eventually, she was able to repay her loans after winning a civil lawsuit not affiliated with her payday loans.
Source: http://www.aol.com/article/2010/11/02/payday-loans-how-one-woman-got-caught-in-a-vicious-cycle/19674757/
(2, 3)

105. Donald Garrett got behind on his bills, so he took out a $100 loan from Advance Till Payday and repaid them $200. "And I said, 'I appreciate you loaning me the $100. I'm sorry that I was in this bind but you helped me and I appreciate it and you won't see me anymore.' And I thought that was the end of it." Later on, he was receiving a dialysis treatment when he received another phone call from the company. "And he told me that I had a balance of $260 outstanding because of the $80 a month membership fee. Where did that come from? Nobody mentioned that when they gave me the $100."
Source: http://wvtf.org/post/federal-lawsuit-reveals-dark-underworld-payday-loans-virginia#stream/0
(2, SL)

106. Roger Tillman, 64, took out a $500 payday loan from The Money Center when he was tight on cash and needed to pay his bills. He was earning $9.00 an hour working as a late-night security guard. The Money Center's website states that they charge an APR of 650%, amounting to about $150 in interest and fees on a 2-week loan. He could not pay the loan back before the first two weeks, and renewed it as the costs accrued. He took a loan out from another payday store, falling into a debt trap. He soon lost his job. He tried to contact The Money Store two days later, and got no response. The manager finally reached out to Tillman. He recalls of the manager, "His statement was that 'I hope you don't get stopped by the police, because I'm filing a theft by check charge against you.' I didn't say anything. I was floored, because I was expecting to work out a payment plan." The Money Center filed a criminal complaint against him in November of 2009. The district attorney told Tillman that he must pay Marpast of Texas, the company through which The Money Center operates, $1,020 within 10 days, in addition to lawyers' fees of $140 and $90 in merchant fees. Otherwise, he would face 2 to 20 years in jail and would be fined as much as $10,000. This shocked him, leaving him scared - too scared to even attend his daughter's graduation from Lackland Air Force Base in San Antonio, fearing that there could be a warrant out to arrest him. "I'm innocent here," he said, "other than losing my job and an inability to pay. I tried to get on a payment plan. If my intention was to duck and dodge, why would I even call them?" He continued to avoid his jail by writing letters to the DA, the state Office of the Consumer Credit Commissioner, and Marpast. He mentioned that the Texas Office of Credit Commissioner submitted his debt to the DA for "collection purposes".
Source: https://www.texasobserver.org/cash-fast-how-taking-out-a-payday-loan-could-land-you-in-jail/

(2, 3)

107. Christina McHam took out a $200 loan from Cash Biz, near Houston, but was unable to repay it. She was arrested in November 2012 and charged an additional $305 for court costs and other fines. She "paid off" her debt with one night in jail.
Source: https://www.texasobserver.org/cash-fast-how-taking-out-a-payday-loan-could-land-you-in-jail/
(2, 3, SL)

108. An anonymous man, a veteran who had served in the military for 23 years, was being charged by the Potter County Attorney for a payday loan he could not repay. His wife wrote to the state Office of Consumer Credit Commissioner, “My husband is a good man! He has never done anything wrong, he fought for this country for 23 years … and now the Potty [sic] County Attorney wants to prosecute him for a payday loan.”
Source: https://www.texasobserver.org/cash-fast-how-taking-out-a-payday-loan-could-land-you-in-jail/
(2, 3)

109. An anonymous borrower repaid $800 on his $400 payday loan after 70 days. However, he was still in dire need of money, and took out another $500 loan the following day. Again, the next day he took out a $1,000 loan, as he was still struggling to afford his basic living expenses. He paid $2,051 back on that loan 70 days later. He took out another $1,000 loan, and a $600 loan from another store. By this time, he had paid $3,000 interest on these loans, in addition to the $2,500 principal amount.
Source: http://www.standard.net/Guest-Commentary/2016/08/07/paydaylenders-Ponzischeme-fraud-loans-column-Winward
(1, 2)

110. “Perry Green, 30, took out a $300 payday loan that soon cost him $1,000 in interest and other fees. By taking out this one loan, he fell into a three-year debt trap. He took out multiple loans after the initial $300 loan. Originally, he needed the loan to afford his rent, thinking a payday loan was the only option.”
Source: http://www.miunited.org/payday-loans-target-those-with-no-cash/
(1, 2)

111. Leonard Abbot, a 53-year-old security officer at the Department of Public Safety at the Texas State Capitol, had been warned of the dangers of payday loans. But after he owed some unexpected medical bills, he felt his only choice was to take out a $500 loan from a payday store. He says, “One thing that I didn’t realize is, it doesn’t matter how many payday loans you have, you still qualify for more.” He adds, “I’ve always been against those things, the payday loans. I knew about them ahead of time and I knew it’s easy to get caught up in their trap, but again, at the time I just felt like I didn’t have any other alternative options.” By May 2016, he had taken out four different payday loans totaling $2,500 and costing him $450 per month. He eventually converted his loans through the Predatory Loan Conversion Program, led by the Society of St. Vincent de Paul in Austin. “My favorite part about working at the Capitol is seeing the representatives coming in, and also just to see Texas law working at its best,” he said. “I am hoping and will be praying that they will look at legislation to regulate this.”

Source: https://www.texastribune.org/2016/06/18/federal-rules-could-tame-wild-west-texas-payday-le/
(2)

112. An anonymous veteran reported, “I took out a loan for thirty-four hundred bucks. I was gonna pay it back as soon as I got my paycheck. But when I realized I’d have to take out another loan to pay my living expenses, I let it ride. Even though I was paying more than $700 a month on the loan, with the high interest rate, it took forever to pay it off, and I ended up having to pay nearly double what I had borrowed.” He got caught in a debt trap for several years, taking out new loans to pay off previous loans.
Source: http://www.vietnow.com/veteran-buyout-plans-and-other-bad-ideas/
(1, 2)

113. Jon Gomez of Hialeah, FL, received a $400 payday loan at a Money Superstore location, due in 14 days and a $41 service charge. "I paid back the $441, but the next day, I took out another $400 payday loan because I needed the money," Gomez told VICE. "I was in this vicious cycle for three months." Eventually, he didn't have enough money to cover one of his payday loan checks, and it bounced.
Source: http://www.vice.com/read/inside-the-battle-over-floridas-racially-charged-payday-loan-racket
(1, 2)

114. “In 2014, hunger drove Michelle Warne, a retiree in Green Bay, Wisconsin, to take out a loan from a local Check ‘n Go. ‘I had no food in the house at all,’ she said. ‘I just couldn’t take any more.’ It took her two years to pay off that loan. Then she took out a second loan, which she has not paid off completely. Caught in a debt trap, she borrowed another $401, plus $338 to pay off the outstanding balance. According to her truth-in-lending statement, paying off this $740 will cost Warne $983 in interest and fees over 18 months. Warne’s APR on her so-called installment loan was 143%. ‘We need better laws,’ said Warne, 73. ‘Because when they have something like this, they will take advantage of anybody who is poor.’ Warne never applied for a standard personal loan from a bank or credit union, which offer loans at a fraction of the interest rate she paid. She was positive a bank would not lend to her, she said, because her only income is her Social Security retirement. For now, Warne said she has no way to pay off her loan. She has made one payment of $101, but does not know how she will pay off the remainder of her debt, which with principal, interest, and fees will cost her $1,723. Warne’s only income is a monthly $763 Social Security check. Warne said she would “never” borrow from a payday lender again, adding, “I wish I would have read the fine print.”
Source: http://wisconsinwatch.org/2016/06/no-relief-from-wisconsins-565-percent-payday-loan-interest-under-new-rules/
(2, LT)

115. Ronnette Souza-Kaawa, 46, lives in Waianae, HI and works in administrative services at an elementary school. Her family faced financial difficulty when her teenage daughter had a baby, so she simply went down the road to Easy Cash Solutions to take out a payday loan. Souza-Kaawa says she has taken out roughly a dozen payday loans in the past two years, ranging from $150 to $400. She says she’d always strive to pay them off before her next paycheck, but wasn’t always able to do so. “If I borrowed a high (amount), I’d pay some off and re-borrow only a little,” she says. Today, Souza-Kaawa owes roughly $1,470 from two recent loans. She is learning

budgeting and financial management strategies from a nonprofit called Hawaiian Community Assets. Today, Souza-Kaawa views payday lenders as a last-ditch option for many families. “It’s there when you need it,” she says, adding that thanks to financial counseling, she’s become savvy to what she now describes as their “hideous” interest rates. “If don’t need it, don’t take out a loan,” she says. “Don’t go borrowing $500, just because you can."
Source: http://www.hawaiibusiness.com/payday-lenders/
(1, 2, SL)

116. Toniette Brown from Alabama needed her first payday loan to afford prescription medicine for her daughter. Working as a part-time librarian, she did not have health insurance coverage to cover her family, or even herself. The payday lender gave her a $275 loan without any credit check. When she couldn't repay her loan by the next payday two weeks later, she took out another. This accrued to 12 loans across 4 different lenders, both in Alabama and online. She frequently had 3 to 5 loans at once. She was eventually in $4,288.96 worth of debt. "I couldn't pay them because I was already living on an income that was paycheck to paycheck," she said. When the interest and fees began to grow several times the amount of the original loan, she sought help from Gateway Financial Freedom and landed a full-time job. She has since almost fully paid back her loans, interest and fees, and says that she will never make the same mistake again
Source: http://www.al.com/news/index.ssf/2015/03/lifeline_or_financial_anchor_u.html
(1, 2)

117. Yolanda Roth, of Robbinsdale, Minnesota, took out a payday loan when she lost her job. She had to accept a lower-paying job and needed some extra money to afford her rent. “My check wasn’t quite enough to pay it off and still live, and I ended up racking up a lot of debt because of fees and so on,” Roth said. “I eventually paid it off, but it took a very long time.” Her original loan was for a couple hundred dollars, but ended up costing her a total of $1,500 over the next six months. She describes this experience as "very unpleasant" and "extraordinarily stressful." However, she understands that there is risk associated with taking out these types of loans. “I felt like I understood what was expected and I could definitely do it,” she said. “I was just in a desperate situation, or what I thought was a desperate situation.”
Source: http://post.mnsun.com/2015/10/12/faith-leaders-protest-payday-loan-practices-in-robbinsdale/
(1, 2)

118. Reverend Stevie Wakes, a Baptist minister in Kansas City, Kansas, received a payday loan of $500 that he thought he could pay back in two weeks. "We thought it was short-term," he said. He thought he would get a higher-paying job soon enough, but wasn't able to. He kept returning to the store to take out more loans every two weeks, and four months later had accumulated $1,250 in debt. He says that he renewed his loans about ten times, with an APR of about 450%. As soon as he realized how quickly his debt he was racking up, he managed to save the money to pay off his debt. “I’d like to see them cap the rate so that no one has to experience that kind of robbery, which is why I support the campaign [for a 36% interest rate cap] 100 percent," he says of payday lenders. "It's a debt trap."
Source: http://www.kansascity.com/news/local/article300576/Alternative-arises-as-payday-loan-industry-comes-under-scrutiny.html
(1, 2)

119. “Michael” of Verona, WI, had taken out payday loans from a dozen stores. He began taking out payday loans after a company mailed him an offer to take out a loan for no charge, directly after he had repaid his car title loan. Soon enough, his debt grew as he continued to take out loans to repay previous ones. He says he felt like a "gerbil on a treadmill". The payday lenders began aggressively calling his personal references, which he provided when he applied for the loans, causing him even deeper feelings of shame and desperation. "It got to be where I felt like my hair was on fire," he says. He eventually declared bankruptcy, halting the fees on the loans.
Source: http://host.madison.com/ct/news/local/govt_and_politics/wisconsin-is-one-of-few-states-with-no-ceiling-on/article_4e3585bc-cda8-5be9-8bf0-7d6b6a02dfdf.html
(1, 2, 3, CT)

120. Janet is a part-time security officer. She took out a $300 payday loan to afford diabetes medicine, as well as her rent. She found herself in a debt cycle. She recalls, "I called and tried to set up a repayment plan with them. I was not aware that I could do that and when I found out that I could, I did talk with them. And the amount that they said I owe is $425, and they said that I could repay in 2 payments which was over $200. I asked them if they could stretch it out 2 more payments; something that would be a lot smaller. The lady told me that they could only stretch it out 4 for 4 payments, which a little over $100 per payment, which is a payment I still cannot afford to pay at this time." She was still in debt 6 weeks later. "It's very frustrating because it's like I'm more on interest than the actual loan itself... it's like I'm actually paying double."
Source: Texas Fair Lending Alliance, https://www.youtube.com/watch?v=HCOwaudHr3g
(1, 2)

121. Trudy Robideau from California received an $800 loan from a payday loan store. She wasn't able to repay her loan right away, and renewed it for a fee. "Ka-ching," Robideau said. "You're hooked. You can feel the hook right in your mouth. And you don't know it at the time, but it gets deeper and deeper." She soon turned to other payday lenders, racking up fees totaling thousands of dollars. "I was having to get one to pay another," she said. "It's a real nightmare."
Source: http://www.npr.org/2015/03/26/395421117/payday-loans-and-endless-cycles-of-debt-targeted-by-federal-watchdog
(1, 2)

122. Elise Robillard, a teacher and single mother, said she fell into a cycle several years ago of taking short-term, high-interest loans that ultimately played a role in her decision to file for bankruptcy. “I spent the better part of 15 years stuck in a cycle of debt because of the initial payday loan that I took out,” Robillard said.
Source: http://www.koat.com/news/nm-supreme-court-exorbitant-payday-loans-violate-state-law/26688316
(2, 3)

123. In 2008, Joy Young and her newly immigrated husband were making only $30,000, in Woonsocket, RI. She and her husband stretched their income to cover their living expenses and their monthly payments on a home equity loan that paid for house repairs and a used vehicle. She received $450 from Advance America, which had to be paid back in two weeks, plus a fee of $45. Two weeks later, she paid her $495 debt, but was forced to borrow again to meet her

monthly expenses. She was now caught in the debt trap, borrowing a third and fourth loan. Every two weeks, Young spent two hours on a Friday afternoon waiting in line to pay off her loans and borrow again. Advance America pocketed $360 in fees each month from her alone. “Every time I got another loan, I thought it would help me in the short term,” Young says. “But there was no way out. I felt like I was in prison. Any time I would talk about my story I would start to cry. It has been a horrible, horrible last few years.” She was weeks away from foreclosure when she received a loan from Capital Good Fund, a microfinance institution that began extending small loans at 30% interest for a twelve-month term. She was able to pay off three of her payday loans with their help and is slowly paying off the fourth.
Source: http://www.rimonthly.com/Rhode-Island-Monthly/October-2014/Reporter-Breaking-the-Payday-Loan-Cycle/
(1, 2, 3)

124. Christina Sarno in Warren, OH borrowed just $200 from a payday lender, but she quickly realized she could not pay back the principal or the interest. “After receiving constant calls and having the store manager show up at my house to try to collect the money I owed, I gave up. At this point I had developed a lot of interest on the loan and owed more than I could possibly pay back on my income,” she said during a meeting at the Warren YWCA. She lost her car, but the Beatitude House of Warren helped her with housing and education to avoid falling into the payday lending trap again.
Source: Reprinted verbatim from http://www.vindy.com/news/2016/jun/28/women-tell-of-troubles-with-payday-lendi/
(2, 3, SL)

125. Tiffany Richardson, a resident of Houston, Texas, received a $5,000 car title loan, using the title to the 2005 Nissan Altima she bought for her mother as collateral. She fell behind on repaying the loan. She took out another car title loan for $2,400 using her 1999 Toyota 4Runner as collateral this time. The amount she owed skyrocketed to several times the original principal amount. “You’re like a hamster on a wheel,” Ms. Richardson, 43, said of repaying her ballooning debt, adding that she was “looking out the window every night” to make sure her cars had not been repossessed. One night, however, Ms. Richardson woke to see both cars being towed away.
Source: http://www.nytimes.com/2014/08/24/us/thousands-in-texas-lose-cars-amid-calls-for-loan-restrictions.html?_r=0
(1, 2, 3, CT)

126. Maranda Brooks, a records coordinator at a Cleveland college in OH, took out a $500 loan to help pay an electricity bill. Two weeks later, the full amount of the loan plus a $50 fee were deducted from her usual $800 paycheck. To cover expenses for herself and her four children, she took out another loan, falling into a debt trap that lasted almost a year. “It was a nightmare of going around and around,” said Brooks.
Source: http://www.chicagotribune.com/chi-payday-loans-rules-20150202-story.html
(1, 2)

127. According to her social worker, Sandra, is an illiterate 33-year old single mother in Missouri with a third-grade education. Sandra received a payday loans from King of Kash. Her only income was her Social Security disability check. Sandra took out a loan for $300 at an APR of 342%, which cost her $1,080 to pay off.

Source: https://www.youtube.com/watch?v=2enmyz-7CQo
(2, LT)

128. After his daughter returned from serving in Iraq and asked for financial help to relocate her family, Preston White, 63, took out a title loan on his pickup truck from a store in Killeen, Texas. The 30-day, $4,000 loan carried a 375% APR. White had already spent his life savings on paying for treatment for his wife's pancreatic cancer and soon realized that his fixed income left him only enough money to cover the fees, not the principal. He recognized the cycle of debt: "In four months, I could have paid more than what I went to the store for in the first place, and still owe the original loan amount," he said. "Never in my wildest imagination did I think that such a loan product could even exist. You assume the system will have usury laws and protect you from such things…Everybody's got to make a profit but there should be no place for usury in the 21st century." He was ultimately able to retire the debt by taking out a loan at 16% APR through a credit union.
Source: Gogoi, P. (2010). "Costly cash: How a retiree wound up with a 375% loan." *Daily Finance.* Available at http://aol.it/16TVtof (viewed 5/24/13).
(1, 2, CT)

129. Alicia and Clinton Lummus of Conyers, Georgia, took out a $525 car title loan after injuries forced them both to stop working. Over eight months, they made payments totaling $1,056—more than twice the amount borrowed—but ultimately fell behind on payments. The lender repossessed the vehicle, worth $14,000—and was able to keep any excess money from the sale of the vehicle, since Georgia law allows the lender to do so.
Source: Kirchhoff, S. (2006). "Some consumers run into big problems with auto title lending." *USA Today*. Available at http://usat.ly/124EbDR (viewed 5/25/13).
(2, CT)

130. Shanell White of Elk Grove, California, needed money to pay for rent after her expenses increased when she began to care for her neice. She took out a $3,900 installment title loan using her car—worth $12,000—as collateral. After having paid nearly $10,500 over three years, she was told she still owed the full principal that she had borrowed. The lender repossessed and sold the car yet still sent her a bill for the loan after. "To me, it's just modern-day loan sharking. People are being taken advantage of," she concluded.
Source: Said, Carolyn. (2013). "'Car-title loans' a road to deep debt: Legislators weight capping high-interest 'car-title loans.''' *San Francisco Chronicle*. Available at http://bit.ly/ZgEx6D (viewed 5/30/13).
(1, 2, CT)

131. Sean received a $1,500 car title loan, which he renewed over 40 times—paying over $11,500 in interest—before receiving help from family to pay off the principal. He said, "I was too embarrassed to ask my parents for the initial loan money, [but] ended up borrowing money from them to make some of the payments and ultimately had to ask them to pay off the whole loan, after losing tons of money along the way."
Source: Martin, N. & Adams, O. (2012). "Grand theft auto: Repossession and demographic realities in title lending." *Missouri Law Review*. Available at http://bit.ly/Z12wSX.
(1, 2, CT)

132. Caroline O'Connor, a 30-year-old hospital lab technician, was in need of $1,000 to cover her rent and electricity bills. When she saw a television commercial advertising how to get cash from your car in the form of a short-term loan, she believed she had found relief. The loan carried a 171% APR. Two years of being stuck in the debt cycle, the lender seized her car. ""These companies put people in a hole that they can't get out of," Ms. O'Connor said.
Source: http://dealbook.nytimes.com/2014/12/25/dipping-into-auto-equity-devastates-many-borrowers/
(2, CT)

133. Ken Chicosky, a 39-year-old Army veteran, received a $4,000 car title loan from Cash America, a in his Austin, Texas, neighborhood. The loan came with an APR of 98.3%. He says he knew the loan was a bad decision when he received his first bill detailing that he would have to pay a total of $9,346 on the $4,000 loan over 24 months. Even though the City of Austin limits loan terms to three months, according to the New York Times investigation, Cash America made the 24-month loan term by having Mr. Chicosky filled out the paper work and pick up his loan check from a store in a nearby town. Chicosky, a college student, said the loan has sunk his credit score and he uses some of his financial aid money to pay his title-loan bill.
Source: http://dealbook.nytimes.com/2014/12/25/dipping-into-auto-equity-devastates-many-borrowers/
(2, CT)

134. Derek Drewery was caught in the debt trap beginning in 1996, when he was stationed at Wright-Patterson Air Force Base in Ohio. He received a payday loan of a few hundred dollars at a payday lender near the base. When he returned to the store to repay the loan, he realized that with interest and fees, he owed a lot more than he had borrowed. "I had to borrow again to pay that back, and had to borrow again to pay that back," Drewery says of getting trapped in the debt cycle. "I got into the real churning situation to borrow this week to pay for last week." To help pay off the loan, Drewery cut back on food, even sharing his last box of Cheerios with his Jack Russell terrier until his father found out and sent him grocery store gift cards. He now works as an electrician and is the pastor of a church which has joined a coalition of Christians to oppose predatory lending.
Source: http://www.nytimes.com/2016/06/11/us/full-faith-and-credit-christian-groups-unite-against-predatory-lending.html
(1, 2, 3)

135. Mr. Sanchez, a veteran who served in Iraq as an infantryman in 2004, returned home to his wife and two daughters but suffers from Post-Traumatic Stress Disorder. When he needed a bit more cash to make ends meet, he took out a car title loan to pay for his family's monthly bills. He had already taken out a $2,500 car title loan earlier in the year, paying $350 per month on the loan. After 10 months of paying a total of $3,500 in fees, he could no longer afford the loan and sold his family's second vehicle in order to continue paying on the original title loan. Unfortunately, a few months later the Sanchez family was in a similar situation, unable to make the regular monthly payment of $350 in interest-only payments while still owing the original $2,500 principal. He couldn't lose his second car to the predatory lenders as it was the only way his wife could get to her job. Desperate for a solution, Mr. Sanchez turned to Helping Hands Ministry, a Texas social service organization that provides opportunities for financial empowerment to veterans and working class families. The organization was able to help the Sanchez family pay off their debt.

Source: https://medium.com/@stoppaydaypreds/payday-lenders-target-veterans-fcfe91b92c86#.wl764nkqu
(1, 2, CT)

136. Susan Fronczak, a 60-year-old woman from Florence, Arizona, secured a $2,000 car title loan using her 2007 Nissan as collateral. Fronczak had six months to pay off the loan, at an APR of 182%. Her loan contract provided for 11 interest-only payments followed by a balloon payment of $2,100, for a total repayment amount of $3,860. By month five, she had paid pack $1,920 and the lender said she still owed the full $2,000. When Fronczak could no longer afford the monthly interest-only payments, her car was repossessed. Getting it back cost her $1, 100. Fronczak continued to struggle after refinancing the loan, and it is estimated that she had paid close to $5,000 on the $2,000 loan by the time she got help. Not only had she paid over double the original loan amount, but she was still facing threats of repossession from the lender. The company returned Fronczak's car title and released her from the debt only after she filed a complaint with the Consumer Financial Protection Bureau.
Source: http://www.azcentral.com/story/news/local/mesa/2014/06/20/auto-title-lenders-give-additional-high-risk-option/11061451/
(2, 3, CT, LT)

137. Elaine is 74 years old and lives independently in a small, one-bedroom apartment. She receives social security and a small monthly pension totaling $1,278. She was struggling with her bills. Elaine came to one of the Catholic Charities of Northeastern Kansas' Emergency Assistance Center (EAC) for help with an electric bill. During her meeting she shared that she had payday loans totaling $1,725. She had these payday loans for years and, unfortunately, her low income just would not cover the loans to be paid off while still trying to take care of her daily living expenses and housing. Because of the high rate, Elaine was paying $275 per month just in interest on all of her payday loans. Elaine shared that she had not told her grown children because she was ashamed to let them know she had gotten into this situation in the first place. Catholic Charities was able to assist Elaine through its Kansas Loan Pool Project (KLPP). By converting her high-interest payday loan into a new, low-interest fixed loan, Elaine now has a manageable payment with an actual payoff date. Elaine participates in monthly financial coaching through the KLPP program. Her bills are now up to date and she has set some realistic financial goals. Elaine has newfound hope through the help of Catholic Charities and the KLPP program. "It's a relief to know that I now have enough money to pay my bills AND go to the grocery store." Elaine shared.
Source: Catholic Charities of Northeastern Kansas
(1)

138. Tiemeyer White, a 33-year-old Navy veteran from Texas, full-time electrical engineering college student, and father, took out a car title loan more than a year ago. When the federal government shut down due to a budget impasse in October 2013, White didn't get his Post-9/11 benefits or work-study pay for his Department of Veterans Affairs job for almost two months. As a result, he fell behind on his bills, and the car title lender began calling him several times a day both at work and at home, demanding loan payments. "I tell them, I understand you're doing your job, but I also understand that your job – you make your living off of making my life worse," White says. "That's how I felt that moment." Two weeks later, his 2003 Dodge pickup truck was repossessed from his school's parking lot.

Source: https://www.nerdwallet.com/blog/banking/banking-news/car-title-payday-loans-trap-unwary-veterans/
(2, CT, LT)

139. Homeless veteran Mel Hair hitchhiked to Sioux Falls, South Dakota, from Minnesota a few years ago. He stayed at a shelter to get back on his feet. When Hair and his girlfriend were able to get their own apartment, he received a car title loan for $200. One title loan turned into three loans amounting to more than $2,000. He has been making monthly payments of $430 per month for the past two years.
Source: http://www.keloland.com/news/article/featured-stories/the-high-price-for-small-loans-
(1, 2, CT, SL)

140. Kim Brust of South Dakota started taking out payday loans three years ago. At the time, her social security and disability checks were not enough to cover her monthly expenses for the children and other family members who had moved in with her. She fell into a cycle of debt, taking out a total of eight loans from four different lenders in Sioux Falls. The interest rates range from 247 percent to as much as 608 percent over the course of a year. "I fell into that same trap and I know better. I'm not stupid, but I was stressing about money. I was wondering sometimes where the next meal was coming from," Brust said. "It just sneaks up on you and one day I just laid out all the papers and I go, 'Oh, my Lord what have I done.'"
Source: http://www.keloland.com/news/article/featured-stories/the-high-price-for-small-loans-
(1, 2)

141. Eddie Dorman of Duval County, Florida, has been caught in a vicious debt trap for years. He uses one payday loan to pay for another, and is currently fighting with a car title loan company in Gainesville that is trying to repossess his truck. "I would never do it again, if I ever get out from under this one." Dorman said. "Everyone has problems. I got behind on a payment, the next thing you know there is a wrecker in the front yard at 3 in the morning." With his truck title loan, the company made him take out a $700 insurance policy to cover the company. “It covers them and yet it does not cover you,” Dorman explained.
Source: http://www.news4jax.com/news/borrower-beware-title-payday-lenders-are-back
(1, 2, CT)

142. Lara was a young mother who stayed home to raise three children while her military husband worked full time. She worked jobs when she could, but the family still found themselves strapped for cash. They reluctantly took out a payday loan of $200 to manage the bills until their next paycheck. When payday arrived, the lender wanted $300. They paid the $300 but came up short on their next payment, so they took out another loan and quickly found themselves caught in the debt trap. “I kid you not, we did that dance for close to six months,” Lara said. “It was horrible. Just unbelievably horrible.” Ultimately, Lara had to beg her parents to help get them out of the cycle, but she knows not everyone has a safety net to fall back on.
Source: http://www.tcdailyplanet.net/new-guidelines-nonprofits-help-curtail-predatory-payday-loans-in-minnesota/
(2, SL)

143. Gordon Martinez: "About 8 years ago, I was struggling financially. I had a family and was starting out a new job in sales, transitioning from being a band director. I used my most prized possession, a tuba valued at $8,000, as a security against a $500 pawn loan to help make ends

meet. I made payments faithfully every 2 weeks, fighting Friday rush hour traffic, trying to stay afloat. I could only ever cover interest fees, none of my payments hit the principal. In the midst of making those payments, I took out another loan from another payday storefront, and even went online to several payday loan [stores] trying to cover my bills. Avoiding pending eviction and keeping my family's finances afloat, I felt hopeless, and that I was failing to uphold my responsibilities. I was trying to do what was best for my family, only to be taken deeper and deeper into a financial mess created by products that were advertised to help. Ultimately, all of the loans and fees took too much of my paycheck and I couldn't keep up. I defaulted on the loans. We lost our residence, I lost my prized tuba, and the strain led to the loss of my marriage, destroying our family. I found myself answering an online ad to rent a couch in a one room studio apartment with all of my worldly possessions housed in two plastic storage tubs. I have never felt so low in my life. I felt isolated, ashamed and lonely. I did what I had to do to survive, but I never imagined I would hit such a low. Thankfully, in the midst of this, I found my church and they helped me get back on my feet. I started sharing my story and exposing what I feel are predatory lending practices that run counter to our faith. I felt powerless while I was trapped in payday loans, but now I work with Faith in Texas to help organize other borrowers to help them so that what happened to me, doesn't happen to them. And to advocate for an end to the debt trap I found myself in. My experience is not uncommon. In a recent Faith for Just Lending survey with Clergy and Congregations, 86% said payday loan products were more harmful than helpful. Common themes raised in interviews with Congregations included a cycle of debt, and loss of a major asset such as a home, family, stress and shame. All of which I lived."
Source: https://vimeo.com/167331364
(1, 2, 3)

144. Diana LaCroix, a 63-year-old widow living off of her husband's Social Security survivor's benefits, received a $300 payday loan. It took her three or four months to pay off the small $300 loan. Then, she found herself caught in the debt trap, borrowing $50, $75, or $100 at a time. She is still borrowing money to make up for the loan payments that are eating into her fixed monthly budget, explaining, "I'll probably have to borrow a little more next month to get caught up on bills."
Source: http://www.omaha.com/money/days-of-the-payday-loan-could-be-numbered-with-new/article_0565b988-8356-5fb5-acf9-d3a076e250a0.html
(2)

145. John Miller, an attorney in Missouri, tells the story of his friend who had been struggling financially and turned to a payday loan store as a last resort before taking his own life.
Source: https://www.youtube.com/watch?v=t2-UlIrs95A
(3)

146. Richard Kitterman, a retired Master Sergeant and former Chief of Consumer Affairs Office, tells the story of a solider: "I remember one particular story, I'll never forget it. She was a young soldier, and she was a good solider. She was a single mother, she was doing her best to meet her obligations to the Army, and to raise her child. But she was facing in some cases, some nearly insurmountable obstacles: she had to have daycare, she had to have babysitting for her kids when she worked late. And she found herself getting her first payday loan and then another, and then another... and it got down to where on payday, her entire check disappeared. It was gone to pay back payday loans. And so her payday was spent standing in line at several different payday

loan offices to get new loans or to renew existing loans. And each time paying healthy loan fees to get that money. And she eventually…and she was a responsible solider. Most of the soldiers that get involved in this are really good, decent soldiers, good people who want to pay their bills, understand their obligations, but they just have more month left at the end of a paycheck. So they just see this as a quick fix; something they only have to do once, and that was the case with this young lady. She just got in over her head. And I remember after she got straightened out and things were going good and she continued to work to pay off those loans, even though she could have walked away and there wasn't really much the payday lender could have done, but that's not the kind of person she was. And I remember her telling me, 'Sergeant Kitterman, I felt like I was in a black hole. Every morning I woke up, every night I went to sleep, I was sick to my stomach over what am I going to do? How am I going to work this out?'"
Source: https://vimeo.com/143323466
(1, 2)

147. Paula, who lives in Texas with her husband and 3 children, took out some payday loans through lenders on the Internet after her husband lost his job. After he started working again, they were never able to get out of the debt trap due to excessive rollover fees. At one point, $800 a month of the family's money was going towards payday loans.
Source: Fact Sheet: *The Victims of Payday Lending*,
http://www.responsiblelending.org/issues/victims-payday
(2)

148. Tennessee resident Natalie has paid over $4,000 in fees for $800 worth of loans. Each time that she thinks she is has paid down the principal, the lender informs her of more fees that have been piled onto her already steep debt. Additional fees are added every time that she pays late.
Source: Fact Sheet: *The Victims of Payday Lending*,
http://www.responsiblelending.org/issues/victims-payday
(1, 2)

149. Maria took out one payday loan three years ago. Now, she is struggling to handle five payday loans and is over $3,000 in debt. Most of her budget goes to paying fees to rollover her loans, leaving little money for her to live on the rest of the month. She cannot afford to pay them off.
Source: Fact Sheet: *The Victims of Payday Lending*,
http://www.responsiblelending.org/issues/victims-payday
(1, 2)

150. According to a 2013 *New York Times* investigation, "Johanna Pimentel said she and both of her brothers had taken out multiple title loans. They are everywhere, like liquor stores," she said. Ms. Pimentel, 32, had moved her family out of Ferguson, Mo., to a higher-priced suburb of St. Louis that promised better schools. But after a divorce, her former husband moved out, and she had trouble paying her rent. Ms. Pimentel took out a $3,461 title loan using her 2002 Suburban as collateral. After falling behind, she woke up one morning last March to find that the car had been repossessed. Without it, she could not continue to run her day care business."
Source: http://dealbook.nytimes.com/2014/12/25/dipping-into-auto-equity-devastates-many-borrowers/

(2, CT)

151. Knoye Jackson of Goodyear, Arizona received a $700 car title loan, which then ballooned to $7,000 in three years due to the high interest rate and additional fees. The $80 Jackson was paying each week was only paying the interest she was accruing—none of it went toward paying down the principal. Ultimately, Jackson's car was repossessed and she filed for bankruptcy. She wishes she had just called the utility company she owed money to and arranged a payment plan directly with them rather than taking out a loan. Of her experiences, Ms. Jackson says, "I think they trap you because they make it seem like, come and get this good money so you can get caught up on your bills, but you never get caught up. They're getting richer by charging you all of this money. We're getting poorer." Those loans don't bring you out of debt, they put you in debt.
Source: http://www.abc15.com/news/state/woman-caught-in-flex-loan-cycle-speaks-out
(1, 2, 3, LT)

152. A single mother in Georgia took out a $450 loan from Atlanta Title Loans to help make her utility payments. After making four monthly interest-only payments of $112.50, she was unable to keep up with the payments and found the firm had repossessed her car in the middle of the night. Without access to her vehicle, she could no longer get to work.
Source: http://usa.streetsblog.org/2010/11/10/driven-to-the-poorhouse-how-car-title-lenders-prey-on-americans/
(2, 3, CT)

153. Jamela Lott, a single mother of five, was falling behind on her rent and borrowed $900 from Loan Max in Akron, Ohio. She used her 2001 Oldsmobile as collateral for the loan. After paying $938 on the original $900 loan, she was unable to keep up. Lott was told she still owed more than $1,600 or had to face repossession of her car. Shortly thereafter, she and her children became homeless and entered the program of Family Promise of Summit County, which provides temporary shelter to homeless families and offers assistance. Harry McKeen, a local attorney, accepted Lott's case via Legal Aid, and settled with LoanMax to write off Lott's debt. Meanwhile, readers donated more than $1,160 to help Lott get into a rental house in West Akron.
Source: http://www.ohio.com/business/taking-action/akron-woman-works-through-financial-situation-involving-lender-1.470027
(2, 3, CT)

154. Norma Poalson, 68, of Akron, Ohio, took out a $600 car title loan from LoanMax for a now-deceased friend who needed money for a chair lift. When she fell behind on her payments, the company rolled over her loan for the same amount. Poalson says she has paid about $2,200 on the loan and still owes another $1,690 or faces repossession.
Source: http://www.ohio.com/business/taking-action/akron-woman-works-through-financial-situation-involving-lender-1.470027

155. Rasheeda Jackson of Akron, Ohio, took out a $600 car title loan. She fell behind on the payments, and her car was repossessed a few months later. To get her car back, Jackson had to pay $890, including $600 to a repossession company. The company charged her storage fees and tried to ask for money to get things out of her car if she didn't pay the full fees.
Source: http://www.ohio.com/business/taking-action/akron-woman-works-through-financial-situation-involving-lender-1.470027

156. Tony Williams of South Carolina was strapped for cash and took out a $715 car title loan. He says it was easy and he was desperate. “They just ask what your income is, and whatever you tell them is what they go by,” said Tony. However, there is a catch. The annual percentage rate on his loan is 360%. So, of the $715 dollars he and his wife borrowed, they'll end up paying back nearly four times that amount, unless they’re able to pay it off sooner. If they don't, their car gets repossessed. “It’s like you're caught in a revolving door and you can't get out,” said Tony. At Max Cash Title Loan in Spartanburg, the max APR was listed as up to 396%. At North American Title Loans, it was 372%.
Source: http://wspa.com/2014/05/01/driven-to-debt/
(2, CT)

157. Roger Irby of North Akron, Ohio, faced financial difficulty when he broke a bone in his neck which hindered his ability to work full time. He turned to Loan Max for a $500 car title loan, using his 13-year-old truck as collateral. Loan Max required him to pay the loan back in 30 days, along with $200 in interest. A month later, the only way he could pay the loan off in time and have enough money to pay his family’s bills was to take out another loan—this time, for $1,000. The loan is due in 30 days, plus $295 in interest. Irby has paid almost $500 to borrow $1,500 for two months. “They are modern day loan sharks,” Irby said. “Me and my wife are trying to pay this bill off and we don’t ever want to mess with them again. Ever.”
Source: http://www.ohio.com/news/local/need-emergency-cash-cuyahoga-falls-group-considering-an-alternative-to-payday-lenders-1.505993
(2, CT)

158. In July 2010, Army Staff Sergeant Jason Cox of Columbus, Georgia, faced a family emergency. He obtained a $3,000 loan with his car title as collateral from Alabama Title Loans in Phenix City, Alabama. The loan carried an APR of 146% and was required to be paid off in 30 days, or Cox would have to pay the interest portion and renew the loan to set the due date back another 30 days. Unable to pay what eventually grew to approximately $4,500, Cox paid between $330 and $417 each month. After nearly a year of monthly payments, Cox could no longer afford to pay the monthly fee, none of which went to pay down the principal of the loan. He stopped making payments and his vehicle was repossessed at his home on the Fort Benning military base. That’s when Cox felt something was amiss, and visited Columbus attorney Kyle Fischer of the law firm Day Crowley. As a former JAG lieutenant in the Army, Fischer knew many of the laws pertaining to military active duty personnel and soon realized that it appeared Cox’s loan was in violation of the 2007 Military Lending Act, implemented by Congress to protect active duty personnel from predatory lending. Barnes and Bevis agreed with Fischer, and in November, they filed a class-action lawsuit against Community Loans of America and Alabama Title Loans. “I definitely feel like I was taken advantage of,” said Cox, who has served three tours in Iraq during his 11 years of service and earned the Purple Heart for a foot injury he received during enemy gunfire. “I had no clue this law was in place, and nothing was explained to me.”
Source:
http://www.barneslawgroup.com/Portals/0/Veteran%20challenges%20title%20loan%20company%20in%20courtmdj.pdf
(2, 3, CT)

159. In 2012, Tammy in Colorado received a payday loan from Speedy Cash, after seeing a commercial and facing trouble paying rent. She now says, "I would be better off if I never had

one." She had a job and thought she could pay the loan back with no problem. She was approved for the loan in less than 10 minutes and given $500 based on her income. The fee did not seem too bad added on top of the $500 loan, and the payback terms seemed okay, until it was time to make her first installment payment. She was going to be $50 short. She called Speedy Cash to tell them to not send her check to the bank because the total amount was not in her account. She made the request for them not to send the check for another 7 days, but the check was sent anyway. She was charged an NSF Fee from Speedy Cash and a Retun Check Charge from the bank, and her bank account went into the negative. Tammy recounts, "This became my downward spiral. I then went to another payday lending company to obtain another loan and was granted." With the second payday loan, she paid the $125 installment plus $35 NSF from the first payday loan. She said, "However, the next payday from my job came around and I was still in the same position again. I was short now on both payday loans and I could not figure out how to settle it, then I got my third payday loan from another payday store. These loans happened all in a timeframe of less than 90 days. Then the awful phone calls began and I stated to dodge all the calls. Letters began and I did not try to address them because I knew that I am now unable to pay any of them due to the all the fees applied from all the payday lending sources. The end result to my story was that since I met payday lenders my life resulted in filing Chapter 7 bankruptcy. I lost my home, car and became homeless and also my credit was damaged. Even today through my email I am now getting threats to garnish my income, and now that I am disabled I cannot afford them to be able to do this to me. This is all because the first payday lender would not honor my request to hold off for a week so I could get the 50.00 and not have to seek other lenders to rob peter to pay Paul. Even today this is a nightmare!"
Source: Story on file with CRL
(2, 3)

Appendix B

Center for Responsible Lending's
Critiques of Selected Payday Lending Studies

This Appendix provides the Center for Responsible Lending's previously published responses to the following:

1. "Reframing the Debate about Payday Lending" by Robert DeYoung, Ronald J. Mann, Donald P. Morgan, and Michael R. Strain (2015)
2. "Do Defaults on Payday Loans Matter?" by Ronald J. Mann (2014)
3. "Payday Loan Rollovers and Consumer Welfare" by Jennifer Lewis Priestley (2014)
4. "Liar's Loan? Effects of Origination Channel and Information Falsification on Mortgage Delinquency" by the Columbia Business School (2006)
5. "Payday Holiday: How Households Fare After Payday Credit Bans" by Donald P. Morgan and Michael R. Strain (2008)
6. "Defining and Detecting Predatory Lending" by Donald P. Morgan, Federal Reserve Bank of NY (2007)

Center for Responsible Lending's Response to *Reframing the Debate about Payday Lending* by Liberty Street Economics

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The primary issue with payday lending, and the one from which most of its other harms flow, is the intentional structuring of the payday loan product as a debt trap for vulnerable borrowers. The Center for Responsible Lending (CRL) and many others have documented the built-in payday loan features that result in the rollover debt trap: lack of underwriting for ability to repay, high fees (typically 400% APR or higher), unaffordable principal payments, and first-in-line access to a borrower's checking account as collateral.[1] The authors of Liberty Street Economics' *Reframing the Debate about Payday Lending* utilize a straw man approach in attempting to refute consumer harm in payday lending.[2] This includes front and center attacks on a number of legitimate, but secondary objections to payday lending including excess profits, spiraling fees, neighborhood targeting, cognitive errors on the part of borrowers, and the like. Liberty Street's attacks are superficial and fail ultimately to robustly address any of the above listed objections. It's disappointing then, to wait until the very end of their piece for the "Reframing", only to find out that – "It's All about the Rollovers" – something that has been widely known for some time.[3] The authors have in fact reiterated rather than reframed the prime driver of consumer harm from the payday product, and that is the payday lenders' debt trap by design.

CRL and others have shown that repeat borrowing is central to the lender's business model, a fact that has been invariant since payday lending's founding and is irrespective of the form of lender ownership, storefront or online delivery, or the current borrower makeup of the lender's portfolio.[4] Our analysis of state regulatory data shows that 85% of payday loans go to borrowers with seven or more loans a year. [5] Similarly, the CFPB in its 2013 analysis of lender-provided payday loan data found that three-quarters of loan fees from their consumer sample came from borrowers with more than ten transactions in a one year period. [6] Most recently, in June 2016, new CFPB research examining millions of payday loan transactions found that approximately 60% of loans are taken out on the same day that the previous loan is repaid, and 85% within 60 days. This industry-wide average persists even when accounting for states with "rollover bans" that do not stop the harms of repeated back-to-back transactions.[7] Payday lending executives and allies have themselves acknowledged the importance of repeat borrowings, or rollovers, to the bottom line: "…. [T]he theory in the business is [that] you've got to get that customer in, work to turn him into a repetitive customer, long-term customer, because that's really where the profitability is"[8] and "in practice, consumers mostly either roll over or default; very few actually repay their loans in cash on the due date."[9].

The Liberty Street authors give a pass to the disingenuous claims of payday lending proponents that the payday loan is mostly used as a product to meet emergency financial needs, despite strong evidence to the contrary. Several studies have shown that the majority of borrowers take out payday loans to cover shortfalls in meeting everyday living expenses between paychecks.[10] This shortfall persists and results in an inability to repay the loan when due, hence, the near ubiquitous rollover. (The Liberty Street authors fail to note that only 15% of loans to new borrowers are repaid at the maturity of the first loan without re-borrowing before the next paycheck.[11])

What percentage of payday borrowers show evidence of long periods of indebtedness for a supposedly short term liquidity fix? The CFPB found the median number of days of indebtedness per borrower to be 199 over a twelve month period for its sample of approximately 15 million loans in 33 states.[12] Looking at the same data from another angle, 67% of borrowers took out seven or more loans in a year with the vast majority of these borrowers being flipped into a new loan immediately or within a few days of paying off the prior loans, racking up an additional fee each time. Seven loans taken in rapid succession, for what is essentially floating the same debt, will usually result in fees that exceed the amount of borrowed principal. So for example, a typical loan fee of $15 per $100 dollars, applied to a loan of $350 borrowed for a two week period and rolled over seven times, results in aggregate fees of $368.

It should be noted that a large percentage of borrowers experience far longer loan sequences than seven. The CFPB found that 34% of borrowers took out between 11 to 19 loans in a year, and an additional 14%, 20 or more loans. In this last category, approximately seven out of eight borrowers are unable to pay off their loan without re-borrowing before their next paycheck so that they would pay $1050 in fees for 20 loans floating the same debt of $350 under the terms of the first example above. It's notable that even NonPrime101, an entity that has close ties to payday lending service providers, recognizes that almost one-third of payday borrowers in their sample are stuck in the product for at least 3.5 years: "From the original 1000 [borrowers], 302 persisted for the entire 3.5 years." (p. 2)[13]

While Liberty Street reluctantly admits that there may be a problem with rollovers (although they understate the phenomenon's prevalence among borrowers), they posit that wholesale regulation should not proceed until additional study determines the extent of over-optimism in the borrowing population. Most research into such questions of cognitive errors in the finance arena occurs in highly controlled laboratory situations. This research has proven very difficult to translate into "the field" of actual payday lending behavior. Over-optimism is just one of the factors that researchers look at with respect to borrower behavior - others include strong responses to uninformative advertising, overestimation of search and switch costs and time-inconsistent preferences. [14] More than one of these factors are likely at play: borrowers clearly do not take out payday loans anticipating that they are going to lose their bank accounts, pay fees well in excess of the amount borrowed and then default, or be unable to pay for critical monthly expenses due to the immediate claim on their paycheck by payday lenders recouping fees and borrowings (all common outcomes).[15] Be that as it may, insights from the field of behavioral economics cannot be used to fix a fundamentally flawed product driven by unaffordability.

The Liberty Street authors sidestep an additional and related pernicious aspect of the payday debt trap - the lender's direct access to the checking accounts of borrowers for repayment. Both CRL and more recently the CFPB have shown that this access, combined with the lack of affordability of the loan relative to borrower's ability to repay, can result in numerous NSF and/or overdraft fees (typically $35 per event) when presentments are made by the lender. Our research of payday lending using state regulatory and checking account transaction data showed that nearly half of all borrowers experienced an NSF or overdraft fee in their checking account within two weeks of a payday transaction in the same account.[16] In the same vein, a CFPB report released in April of this year looked at payday lending activity (332 lenders) at the checking account level of almost 20,000 payday borrowers across a number of states.[17] They found that half of these borrowers were charged an average of $185 in bank penalties, usually NSF and/or overdraft fees, as a result of often repeated attempts to access borrowers' accounts for payment when bank balances were insufficient.

These devastating charges are not surprising given that the payday lender's business model is built on such outcomes. Indeed, this cascading, but less visible burden on a payday borrower's finances, is evidence that Liberty Street's focus was too narrow in their semantic quibble with the word "spiraling" as it relates to the accrual of contractual payday loan fees. For the many borrowers that experience bank checking account penalties, when added to the accumulating amount of contractual lender fees due to numerous loan rollovers, the net cash flow effect of the initial small dollar loan does indeed spiral out of control.

Finally, the Liberty Street authors are concerned that "economists do not agree" about the perils of payday lending as measured by such proxies as involuntary bank closure, complaints against lenders, difficulty paying bills and the like. We find that on balance the academic research strongly supports the premise of long-term harm to payday borrowers.[18] However, what is undisputed in all of the legitimate research, academic or otherwise, is the high percentage of loans that go to borrowers that become trapped in long term, sequential use of the loan product, often sending them on a downward trajectory towards insolvency. These consumers deserve strong federal and state protections and access to credit on fair terms. Their welfare shouldn't be held hostage to the proclivities of a small group of economists who would extend the research horizon indefinitely. Delay is clearly not in the best interests of current (and prospective) payday borrowers whose pockets are drained by the fees of payday lenders to the tune of $11.2 million every day. [19]

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[1] Susanna Montezemolo, *Payday Lending Abuses and Predatory Practices,* in *The State of Lending in America and its Impact on U.S. Households*, Center for Responsible Lending, September, 2013, available at http://responsiblelending.org/sites/default/files/uploads/10-payday-loans.pdf , also
The Pew Charitable Trusts, *How Borrowers Choose and Repay Payday Loans*, February 2013, available at http://www.pewtrusts.org/~/media/assets/2013/02/20/pew_choosing_borrowing_payday_feb2013-(1).pdf, also
Michael A. Stegman, 2007. "Payday Lending." *Journal of Economic Perspectives*, 21(1): 169-190, available at https://www.aeaweb.org/articles?id=10.1257/jep.21.1.169

[2] Liberty Street Economics, *Reframing the Debate about Payday Lending,* October 2015, available at http://libertystreeteconomics.newyorkfed.org/2015/10/reframing-the-debate-about-payday-lending.html

[3] From the 2006 Department of Defense *Report on Predatory Lending Practices*,

> "For example, when some states banned "rollovers," meaning the borrower could extend the loan for another fee without paying it back, payday lenders attempted to circumvent this reform by offering back-to-back transactions. The borrower paid off the loan and immediately opened a new one for the same amount. This had the same detrimental effect on the borrower, and also allowed the payday lender to call the transaction a "new" loan, even though they were handing back the same amount of money. Even when the transactions are separated by a couple of days or a week, the borrower is still caught in the cycle of debt. If they were using these loans as an occasional boost to get to the next payday, they would have only a few loans a year, with weeks or months between". (p. 47) available at http://www.dtic.mil/dtic/tr/fulltext/u2/a521462.pdf, also

Uriah King and Leslie Parrish, *Springing the Debt Trap: Rate Caps are Only Proven Payday Lending Reform,* Center for Responsible Lending, December, 2007, available at www.responsiblelending.org/payday-lending/research-analysis/springing-the-debt-trap.pdf

[4] Ibid, *Phantom Demand,* Center for Responsible Lending, July 2009, available at http://www.responsiblelending.org/payday-lending/research-analysis/phantom-demand-final.pdf

[5] Susanna Montezemolo, *Payday Lending Abuses and Predatory Practices,* in *The State of Lending in America and its Impact on U.S. Households*, Center for Responsible Lending, September, 2013, *available at http://responsiblelending.org/sites/default/files/uploads/10-payday-loans.pdf*
also,
Brandon Coleman and Delvin Davis, *Perfect Storm: Payday Lenders Harm Florida Consumers Despite State Law,* Center for Responsible Lending, March 2016, available at http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_perfect_storm_florida_mar2016_0.pdf

[6] CFPB, *Payday Loans and Deposit Advance Products*, April 2013, available at http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf

[7] Ibid, *Supplemental Findings on Payday, Payday Installment, and Vehicle Title Loans, and Deposit Advance Products,* June 2016, available at http://www.consumerfinance.gov/data-research/research-reports/supplemental-findings-payday-payday-installment-and-vehicle-title-loans-and-deposit-advance-products/

[8] Dan Feehan, former CEO of Cash America, remarks at Jeffries Financial Services Conference, 06/20/07.

[9] excerpt from email dated 2/14/2011 from Hilary B. Miller, chairman of the pro-payday lender group, Consumer Credit Research Foundation, available (see Exhibit D) at http://campaignforaccountability.org/cfa-report-reveals-payday-lenders-paid-for-at-least-one-favorable-academic-study/

[10] The Pew Charitable Trusts, *Who Borrows, Where they Borrow and Why*, July 2012, available at http://www.pewtrusts.org/~/media/legacy/uploadedfiles/pcs_assets/2012/pewpaydaylendingreportpdf.pdf, also FDIC*, Alternative Financial Services and Prepaid Cards Findings*, National Survey of Unbanked and Underbanked Households, 2011, available at https://www.economicinclusion.gov/surveys/2011household/afs-and-prepaid-cards-findings/

[11] CFPB, *CFPB Data Point: Payday Lending*, March 2014, available at http://files.consumerfinance.gov/f/201403_cfpb_report_payday-lending.pdf

[12] Ibid, *Payday Loans and Deposit Advance Products*, April 2013, available at http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf

[13] NonPrime101, *A Balanced View of Storefront Payday Borrowing Patterns, Report 7c,* March 2016, available at https://www.nonprime101.com/data-findings/

[14] Jonathan Zinman, *Consumer Credit: Too Much or Too Little (or Just Right)?* , February 2014, available at http://www.dartmouth.edu/~jzinman/Papers/CreditSupply_Zinman_JLS_2014.pdf

[15] Dennis Campbell, F. Asis Martinez-Jerez, and Peter Tufano, *Bouncing out of the Banking System: an Empirical Analysis of Involuntary Bank Account Closures,* Journal of Banking & Finance 36, no. 4 (April 2012), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1335873, also
Paige Marta Skiba and Jeremy Tobacman, *Payday Loans, Uncertainty, and Discounting: Explaining Patterns of Borrowing, Repayment, and Default*, Vanderbilt Law and Economics Research Paper No. 08-333, August 21, 2008, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1319751, also
Brian Meltzer, *The Real Cost of Credit Access: Evidence from the Payday Lending Market,* The Quarterly Journal of Economics 126,, no. 1 (2011), available at http://web.law.columbia.edu/sites/default/files/microsites/transactional-studies/files/13PDL_realcosts_melzer_qje_pub_0.pdf

[16] Susanna Montezemolo and Sarah Wolff, *Payday Mayday: Visible and Invisible Payday Lending Defaults,* The Center for Responsible Lending, March 2015, available at http://files.consumerfinance.gov/f/201403_cfpb_report_payday-lending.pdf

[17] CFPB, *Online Payday Loan Payments,* April 2016, available at http://files.consumerfinance.gov/f/201604_cfpb_online-payday-loan-payments.pdf

[18] Brian Meltzer, *The Real Cost of Credit Access: Evidence from the Payday Lending Market,* The Quarterly Journal of Economics 126,, no. 1 (2011), available at http://web.law.columbia.edu/sites/default/files/microsites/transactional-studies/files/13PDL_realcosts_melzer_qje_pub_0.pdf, also
Scott Carell and Jonathan Zinman, *In Harm's Way? Payday Loan Access and Military Personnel Performance,* Review of Financial Studies, 27, no. 9 (2014), 2805-2840, available at http://rfs.oxfordjournals.org/content/early/2014/06/19/rfs.hhu034.abstract , also
Paige Marta Skiba and Jeremy Tobacman, *Do Payday Loans Cause Bankruptcy*?, Vanderbilt Law and Economics Research Paper (2009, Paper No. 11-13) *available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1266215*
Dennis Campbell, F. Asis Martinez-Jerez, and Peter Tufano, *Bouncing out of the Banking System: an Empirical Analysis of Involuntary Bank Account Closures, Journal of Banking & Finance 36, no. 4 (April 2012), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1335873*

[19] Diane Standaert and Delvin Davis, *Payday and Car Title Lenders Drain $8 Billion in Fees Every Year,* The Center for Responsible Lending, May 2016, available at http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_statebystate_fee_drain_may2016_0.pdf

Research Comment On: "Do Defaults on Payday Loans Matter?"

By Debbie Gruenstein Bocian and M William Sermons *March 2014*

In "Do Defaults on Payday Loans Matter?" author Robert Mann uses a difference-in-difference regression-based analysis to analyze "harm" in the payday lending market. He finds little difference in changes in credit scores between payday defaulters and non-defaulters and uses this as evidence that payday loans do not cause harm. However, this study suffers from significant conceptual and technical flaws.

1) Credit score is a poor metric for analyzing the harm caused by payday lending.

- Credit scores, such as the VantageScore used in this paper, are poor metrics for measuring financial health for the payday population. Credit scores are designed to be used by financial institutions to predict the likelihood of default and, while they may be useful metrics of access credit, payday borrowers typically have stretched their credit to the limits—therefore, they have scores that are strongly skewed toward the lowest ranges of the credit score spectrum.[i] According to Mann, his sample of payday borrowers has an average score of 578 (compared to the overall VantageScore average of 736) and a standard deviation of 48. It is, therefore, unclear that measuring movement within this very low range credit scores gives any insight into the financial wellbeing of these borrowers.
- Payday lenders do not report to credit bureaus so there is no direct link between the performance of payday loans and credit scores. However, using credit score as the outcome variable leads to potential reverse causation because changes in borrowers' scores may impact other credit options which, in turn, may impact their ability to pay off payday loans. Such reverse causation may lead to unreliable coefficients and significance estimates.

2) Mann's hypothesis and model are incoherent.

- More importantly, Mann is testing an incoherent hypothesis. Any harm to credit scores would be caused, not by default, but by the financial drain resulting from paying the exorbitant fees charged by payday lenders. This harm would be incurred most acutely by the payday borrowers who pay multiple fees- these borrowers may or may not be the defaulters.
- Even if credit score is serving as a crude proxy for the financial distress caused by an inability to repay a payday loan, Mann's model is flawed because he assumes inability to repay always leads to default when, in fact, more often than not it leads to serial loan refinancing (i.e. "rollovers"). Mann justifies his model technique the following way:

> "Recent regulatory initiatives suggest an inclination to add an 'ability to pay' requirement to payday-loan underwriting standard that would be fundamentally inconsistent with the nature of the product. Because the

> premise of that regulation would be that borrowers suffer harm when they fail to repay such a loan, it is timely to examine the after-effects of such a default empirically."

However, because Mann's "difference-in-difference" analysis compares payday defaulters to all non-defaulters (including those who had to rollover their loans) both the treatment group and the control group include borrowers who were unable to pay off their loans.

Research Comment On: “Payday Loan Rollovers and Consumer Welfare”

By Debbie Gruenstein Bocian and M William Sermons *March 2014*

In “Payday Loan Rollovers and Consumer Welfare”, Jennifer Lewis Priestley analyzes proprietary payday loan data for borrowers who received payday loans from 2006-2009 in California, Florida, Kansas, Missouri, Oklahoma, Texas and Utah to estimate the impact of payday rollovers on consumer welfare (as measured by changes in Vantages Score). The author finds that payday borrowers who engage in protracted refinancing or “rollovers” have positive changes to their credit scores, relative to borrowers with shorter periods of payday borrowing. In addition, the author finds that borrowers in states with less restrictive payday loan laws have better credit score outcomes.

The payday loan industry and CFPB detractors are using the study to argue against the need for meaningful payday loan regulations. However, the study has serious limitations that opponents of payday loan reform do not acknowledge

1) Methodological Limitations

- *Omitted Variable Bias*: The study shows a significant relationship between change in credit score and number of rollovers is suggestive of a causal relationship between the two. However, there are likely other variables that are not controlled for that may account for the relationship. For example:
    - *Income/Employment shocks*: Borrowers who lose their jobs may not be approved for subsequent payday loan rollovers and those who suffer from other negative income shocks may default on their loans. Undoubtedly, these same borrowers will likely experience negative changes in their credits scores, compared to borrowers who do not lose their jobs. However, the study does not control for employment status or income of the borrower. As a result of omitting variables that are likely correlated both with the duration of payday borrowing and credit scores, there is a high chance of omitted variable bias.
    - *State-specific economic conditions:* In addition, the study attributes the state fixed effects on credit score changes to differences in state payday regulatory regimes when, in fact, there are many economic factors that could account for these differences (e.g. state unemployment levels, housing markets dynamics such as foreclosures and prices, etc).
- *Misspecification of Regression Models:* According to the study, VantageScore is “is based on multiple general factors regarding a consumer's credit-related behavior, including delinquencies, line utilization, balances, depth of credit,

recent credit and available credit." However, in most of the models, the independent variables indicating bankruptcy, percent of lines over 50% utilized, and balances are not statistically significant, suggesting that the regression is not specified correctly.

2) *Negligible Size of Impact*

- Even if methodology weren't limited in the ways outlined above, the magnitude of the impact of rollovers on credit score is miniscule. For every additional rollover, an average borrower achieves an increase of 0.1-0.2 in their scores. Put another way, for every 10 rollovers (at an estimated cost of $450), the average borrower would achieve an increase of 1-2 points in their VantageScore. Given that the average credit score for borrowers in the sample ranged from 579-588[1], the typical payday borrower would need an increase of 13-22 points just to move from the highest risk "F" category to the next highest risk "Non-Prime" category.[2] Therefore, any claim that sustained use of payday loans has a positive impact on consumer's welfare is hard to support by any reasonable cost-benefit analysis.

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[1] See Table 5.

[2] See Irby, Latoya. "VantageScore Credit Overview", available at http://credit.about.com/od/vantagescore/a/vantage-score-overview.htm

Research Comment: On "Liar's Loan? Effects of Origination Channel and Information Falsification on Mortgage Delinquency"

By Debbie Gruenstein Bocian and Keith S. Ernst
September 24, 2009

A working paper recently released by the Columbia Business School, "Liar's Loan? Effects of Origination Channel and Information Falsification on Mortgage Delinquency" [1] reported three main findings: **(1) mortgages originated through brokers are more likely to become delinquent than similar mortgages made through retail channels; (2) mortgages with low levels of income documentation are more likely to become delinquent than those with standard levels; and (3) African-American and Latino borrowers were more likely than non-Latino, white borrowers to become delinquent.** This report is consistent with the following well-established facts regarding loan delinquencies:

- **Loans originated by mortgage brokers perform worse than those originated by the bank's retail channel, even after controlling for borrower risk factors.** The authors find a large disparity between the delinquency rates of loans originated by brokers versus those originated directly through the bank's retail channel and cannot fully explain the disparity by differences in risk factors such as credit score and loan-to-value ratio, a finding that has been borne out by other research as well.[2] The authors' attribute this unexplained disparity to "manifestation of the misalignment of incentives for brokers who issue loans on the bank's behalf for commissions but do not bear the long-term consequences of low-quality loans." That is, the authors argue that because the financial compensation of brokers is largely based on origination volume, not loan performance, they are not as vested in assuring the long-term viability of the loans they originate. Of course, in virtually all brokered transactions, the responsibility for underwriting ultimately rests with the lender. The implication is that lenders have been less able—or less willing—to maintain standards in the broker channel.

- **Loans with low levels of documentation defaulted at higher rates than loans with full documentation**. The authors find that loans with low levels of documentation perform worse than those with full documentation and point to the poor predictive power of the low-documentation models as indications of inaccurate information on many low-documentation loans. The prevalence of low-doc loans, particularly in the subprime and Alt-A markets, along with their high default rates have been widely noted.[3] The authors

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[1] See Wei Jiang, Ashlyn Aiko Nelson and Edward Vytlacil. "Liar's Loan? Effects of Origination Channel and information Falsification on Mortgage Delinquency". Available at http://www.columbia.edu/~wj2006/liars_loan.pdf.

[2] See "Risky Borrowers or Risky Mortgages: Disaggregating Effects Using Propensity Score Models." Lei Ding, Roberto G. Quercia, Wei Li, Janneke Radcliffe. Available at http://www.ccc.unc.edu/documents/RiskyMortg_Final_Dec11.pdf

[3] See GAO's "Characteristics and Performance of Nonprime Mortgages", available at http://www.gao.gov/new.items/d09848r.pdf and the University of North Carolina's "The Impact of Predatory Loan

should take care, however, not to assume that it was the *borrowers* who lied on their loan applications. It is possible that loan originators falsified information without the borrowers' knowledge in order to over-qualify borrowers for loans. This is particularly likely for mortgage brokers, since broker compensation is dependent upon the volume and terms, but not the performance, of originated loans. Consequently, brokers have a financial incentive to originate as many loans as possible without due regard for borrowers' ability to repay. This incentive structure is also true, albeit to a lesser extent, for retail lenders who sell their loans on the secondary market. The higher default rate of low-documentation loans in both retail and broker channels, but with the disparity between low- and full-documentation loans larger in the broker channel, combined with the larger disparity between the full- and low-documentation models' predictive power in the broker channel, is consistent with a hypothesis of originators falsifying information on low-documentation loans.

- **African-American and Latino borrowers were more likely to struggle with their loans than white borrowers.** The study shows that African-American and Latino borrowers were more likely to be delinquent on their loans than white borrowers with similar characteristics. Because some readers may mistakenly conflate this finding with others in the paper, it is important to explicitly note that <u>the study does not find nor do the authors conclude that African Americans or Latinos were somehow more likely to misrepresent their income on mortgage applications</u>. And, while this paper does not find evidence of disparate loan pricing within fixed-rate products[4] or of steering to low-documentation products, it is nonetheless possible that differences in delinquency rates are due to minority borrowers being disproportionately steered into loan products with other risky features, particularly subprime products. For example**,** previous research has shown that borrowers in African-American and Latino neighborhoods were much more likely to receive subprime loans with prepayment penalties than borrowers with similar risk profiles in white neighborhoods.[5] Such evidence of racial and ethnic steering, combined with conclusions from a recent report published by the University of North Carolina[6] showing that receipt of risky loan products, especially subprime products, are strong determinants of loan defaults, suggests that the disparate delinquency rates in this study may reflect a targeting of dangerous products to minority borrowers.

Terms on Subprime Foreclosures: The Special Case of Prepayment Penalties and Balloon Payments", Roberto G. Quercia, Michael A. Stegman and Walter R. Davis, available at http://www.ccc.unc.edu/documents/foreclosurepaper.pdf.

[4] It is worth noting that other studies have, in fact, found that minorities receive higher-priced loans than similarly-qualified white borrowers. See"Race, Ethnicity and Subprime Loan Pricing." Debbie Gruenstein Bocian, Keith Ernst and Wei Li. Journal of Economics and Business, Vol. 60, Issues 1-2, January-February 2008, Pages 110-124.

[5] See "Borrowers in High Minority Areas More Likely to Receive Prepayment Penalties on Subprime Loans." Debbie Gruenstein Bocian and Richard Zhai, January 2005. Available athttp://www.responsiblelending.org/media-center/press-releases/archives/rr004-PPP_Minority_Neighborhoods-0105.pdf

[6] See "Risky Borrowers or Risky Mortgages: Disaggregating Effects Using Propensity Score Models." Lei Ding, Roberto G. Quercia, Wei Li, Janneke Radcliffe. Available at http://www.ccc.unc.edu/documents/RiskyMortg_Final_Dec11.pdf .

While the study will be a valuable contribution to the existing literature on loan delinquency, the authors should consider several adjustments as they move to a final analysis. First, the models would greatly benefit from the inclusion of controls for loan segment and product, especially subprime status and product features such as adjustable rates, negative amortization options, and interest-only periods. Second, while the authors control for origination year and cluster observations by MSA, they should consider explicitly controlling for MSA-level housing price changes, since the dynamics of housing price depreciation is a critical determinant of loan default. Third, debt-to-income can be included in the models as it is this ratio (and not income by itself) that is the traditional underwriting variable used by lenders. Fourth, even though the primary interest of the authors' is default and not prepayment, the authors should consider employing a competing-hazard model that jointly estimates the probability of prepayment and default to better isolate default risk.

CENTER FOR RESPONSIBLE LENDING

CRL Critique of "Payday Holiday: How Households Fare After Payday Credit Bans" by Donald P. Morgan and Michael R. Strain

Rev. January 2008

In a recent working paper, Donald Morgan, a researcher affiliated with the New York Federal Reserve and Michael Strain, a Cornell University graduate student, attempt to determine whether households in two states which have outlawed payday lending (North Carolina and Georgia) have fared better than households in states in which payday lending is still authorized. The authors analyze patterns of returned (bounced) checks, complaints filed with the Federal Trade Commission (FTC) against lenders and debt collectors, and federal bankruptcy filings, and conclude that "Georgians and North Carolinians do not seem better off since their states outlawed payday credit."

The authors contend that Georgia and North Carolina residents (1) had greater rates of returned checks than the national average; (2) complained more to the FTC about lenders and debt collectors; and (3) filed for Chapter 7 bankruptcy at rates greater than the national average.

However, Morgan and Strain's data and research methods are not adequate to support these findings or overall conclusion. The authors consistently intermingle data from Georgia and North Carolina—which outlaw payday lending—with data from states which allow it. They also ignore important data that does not support their arguments.

- The returned check data used to report increases for Georgia and North Carolina after payday lending was banned includes not only these two states, but also returned checks from Alabama, Louisiana, South Carolina, southern Mississippi, and Tennessee—states where payday lending is legal. The authors did not separate out Georgia and North Carolina-specific data from these others states which allow payday lending.

- The assertion that borrowers have no other alternative to payday loans than to bounce a check, is in direct conflict with academic and industry research showing a variety of less expensive alternatives for dealing with a financial shortfall.

- While FTC complaints increased after payday lending was banned in Georgia, the District of Columbia actually experienced the highest rate of complaints—a jurisdiction that—until 2008—had almost no limitations on payday lending.

- In analyzing variances in bankruptcy rates among states, the authors fail to account for several factors that greatly influence a person's chances of filing for bankruptcy protection, including health insurance coverage, foreclosures, divorce rates, and demographic factors such as income.

These and other flaws in this study's conclusions are discussed in more detail below.

Returned check data

The returned check data used to report increases for Georgia and North Carolina after payday lending was banned includes not only these two states, but also returned checks from Alabama, Louisiana, South Carolina, southern Mississippi, and Tennessee—states where payday lending is legal. The only point demonstrated by this data is a slightly higher number of returned checks for people living in the much of the southeastern region of the United States, relative to the national average.

In analyzing returned checks, the authors use data from the Federal Reserve's *regional* check processing centers (CPCs) as proxies for *state* credit markets. However, the regional CPCs in Atlanta and Charlotte handle checks for other states besides Georgia or North Carolina, including states that allow payday lending. For example, more than half of the checks processed at the Charlotte center come from South Carolina, home of Advance America's headquarters and over 1,000 payday lending storefronts.[1] Similarly, during the aftermath of Hurricane Katrina, checks from those areas affected began to be processed in the Atlanta center.[2] Atlanta's CPC also serve Alabama and Tennessee, additional states with payday lending locations. Because the CPC data includes returned checks for states that authorize payday lending, one cannot draw the conclusion that a payday lending ban results in higher rates of returned checks.

Atlanta check processing center processes returned checks from:		**Charlotte check processing center processes returned checks from:**	
Alabama, Louisiana, southern Mississippi, and Tennessee (payday lending legal)	Georgia (payday lending banned)	South Carolina (payday lending legal)	North Carolina (payday lending banned)

Even if we were to accept this data as a valid proxy for conditions in Georgia and North Carolina, the increased rate of returned checks is minuscule—in Atlanta's worst quarter after the payday ban, they had two-tenths of one percent more returned checks than the national average. In other quarters, they were actually below the national average. Charlotte's CPC has had fairly consistent above national average rates ranging from 0-0.4% throughout the study period, *before, during, and after* payday lending was legal in North Carolina.

Finally, the authors erroneously assume that bounced checks are the *only* substitute for a payday loan: "Of course, households in Georgia and North Carolina had only one choice once payday credit was banned. If we observe higher bounced checks afterwards, it tells us payday credit was the preferred choice..." But a recent study by the University of

North Carolina found that former payday borrowers use a host of options to cover financial shortfalls, such as working out delayed payments with creditors; borrowing from family, friends, or employers; dipping into savings; or delaying a purchase for a short period of time.[3] In addition, Pat Cirillo of Cypress Research, who frequently conducts borrower surveys for the industry, has found that over half of payday borrowers have a credit card that they could instead use for a financial shortfall.[4]

FTC complaint data

In analyzing complaints to the FTC, the authors find that people in Georgia complain more to the FTC than those in other states. However, this was the case before and after the payday lending was halted in 2004, with a steady upward trend beginning in at least 1997.[5] In addition, the authors find Georgia has the second highest rate per capita of FTC complaints per year, they note that the jurisdiction with the highest complaint rate was the District of Columbia. Yet during the time period for this research, the District of Columbia had some of the loosest restrictions on payday loans of any state. This appears to refute the authors' attempt to develop a cause/effect relationship between the absence of payday lending and FTC complaints.

Moreover, the authors admit that the rate of FTC complaints from households in North Carolina is *not* higher than complaint rates in other states. The data does show a steady *national* increase in FTC complaints for some time but especially since 2001. Many experts have attributed this to rise of identity theft; this is confirmed by the FTC as over 40 percent of all complaints involve challenging the actual validity of the debt. We are not aware of even a potentially plausible relationship between payday lending and identify theft.

What sorts of financial services state residents were using also affects the number of complaints logged by the FTC. For example, a consumer wishing to complain about high credit card fees would log their complaint with the FTC. However, a person wishing to complain about a 391% APR payday loan and payday lender debt collection tactics would likely direct their complaint to a state regulator.

Regardless, the authors' conclusion that a person taking out a payday loan "helps avoid…getting hassled at work by debt collectors" completely ignores the aggressive tactics used by payday lenders, including frequent phone calls to the borrower and their employer, family, and friends. In fact, the majority of complaints filed against payday lenders are regarding debt collection practices. [6]

Bankruptcy data

In analyzing variances in bankruptcy rates among states, the authors fail to account for several factors that greatly influence a person's chances of filing for bankruptcy protection, including health insurance coverage, foreclosures, divorce rates, demographic factors such as income. In fact, the *only* factor that the authors control for is unemployment rates.

By failing to account for many important factors, or to consider that changes to the bankruptcy code in 2005 coincide with the North Carolina and Georgia ban on payday loans, the authors are unable to show a clear pattern in bankruptcy filings versus payday lending activity. For example, the Georgia data shows a steady increase in bankruptcy filings starting in 1998, with a quick decrease when the new bankruptcy reform takes effect and then a continuing increase after that.

Finally, the data provided by the authors shows that North Carolina residents file for Chapter 7 bankruptcy at rates lower than the national average during periods both with and without payday lending.

Other industry and academic research paints a very different picture, with long-term payday borrowing leading to a high likelihood of default which could spur—rather than prevent—bankruptcy. Rather than a $300 two-week payday loan preventing bankruptcy, borrowers are typically trapped in a debt trap cycle for 18 months or more, with a third to half of all borrowers ultimately ending up in default.[7]

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[1] The Columbia, SC check processing center was closed in August 2004, with checks from that facility then processed at the Charlotte, NC CPC. For more details, see http://www.federalreserve.gov/boarddocs/press/bcreg/2004/200406222/attachment.pdf. The authors note that half of checks processed at the Charlotte CPC are from financial institutions in South Carolina.

[2] In 2005, the Birmingham, AL CPC was closed and checks from this region were processed at the Atlanta CPC. See http://www.federalreserve.gov/boarddocs/press/bcreg/2005/20050208/attachment.pdf. Also in 2005, the New Orleans, LA CPC was shut down and checks once coming into that facility began to be processed at the Atlanta CPC. Finally, in 2007, the Nashville, TN CPC was closed and checks from that region were routed to the Atlanta CPC as well. See http://www.federalreserve.gov/boarddocs/press/bcreg/2005/20051215/attachment.pdf for details on the closing of the New Orleans and Nashville CPCs. These and other consolidations of CPCs across the country have occurred because of the decline of paper check usage.

[3] *North Carolina Consumers After Payday Lending.* Center for Community Capital, November 2007. Available at http://www.ccc.unc.edu/documents/NC_After_Payday.pdf

[4] Pat Cirillo, in testimony to the Ohio House Committee on Financial Institutions, Real Estate and Securities, January 31, 2008.

[5] 1997 is the first year for which the authors provide data. It is unclear whether this trend began in 1997 or in years' prior.

[6] For examples of payday lenders' aggressive collection tactics, see Chris Flores, When Lenders Cross the Line, *Daily Press*, September 16, 2007.

7 In testimony to the Ohio House Committee on Financial Institutions, Real Estate and Securities, January 31, 2008, Pat Cirillo of Cypress Research noted that borrowers tend to remain in payday loans for 18 to 24 months. Using transaction data from one of the largest payday lenders in Texas, Paige Skiba and Jeremy Tobacman estimate default rates on payday loans per borrower. See *Do Payday Loans Cause Bankruptcy?* and *Payday Loans, Uncertainty, and Discounting: Explaining Patterns of Borrowing, Repayment, and Default*. Papers available at http://www.law.vanderbilt.edu/faculty/faculty-personal-sites/paige-skiba/index.aspx.

CRL REVIEW OF *DEFINING AND DETECTING PREDATORY LENDING*, BY DONALD P. MORGAN, FEDERAL RESERVE BANK OF NEW YORK, JANUARY 2007

January 23, 2007 (revised 2/14/07)

In a recent working paper, Donald Morgan, a researcher from the Federal Reserve Bank of New York, attempts to determine whether payday lending is predatory by comparing the welfare of households in states where payday lending is unlimited versus states where payday lending is not authorized. After a comparative analysis, Morgan concludes that "unlimited" payday lending enhances welfare. However,

MORGAN'S FINDINGS ARE FLAWED FOR THREE KEY REASONS:

- <u>The comparisons attempted between unlimited payday and non-authorizing states in 2001 are impossible because states did not have the tools to effectively regulate or restrict payday lending at that time. Example: Morgan considers North Carolina a non-authorizing state—however, it had at least 500 stores during the analysis period and was one of the most saturated states in the country.</u>

- <u>Key definitions utilized by the research are overly narrow or are contradicted by available data. Example: Morgan, in part, defines vulnerable households as those with unpredictable future income. However, an industry survey notes that households are nearly three times likely to borrower payday loans because of unexpected *expenses*.</u>

- <u>Morgan's finding that unlimited payday lending leads to lower prices is in conflict with other research. Example: Researchers from the FDIC, using a national, random sample, found that most payday companies charge the maximum rate permitted by state law.</u>

We discuss these points more fully below.

RESEARCH SUMMARY

In order to determine if payday lending is predatory, Morgan compares the welfare of households in states where payday lending is "unlimited" versus states where payday is not authorized. Morgan measures "welfare" in two ways: (1) household non-mortgage debt levels and (2) delinquent bill payments. Specifically, the study assumes the greater the level of debt and incidence of delinquency, the lower the household's welfare. Morgan concentrates on "risky" households, which he defines as those who believe they will face income uncertainty in the future and those with less than a college degree. The main data sources used for this survey is the Federal Reserve's 1995 and 2001 Survey of Consumer Finance, which gathers information on a little over 4,000 households' financial status.

Morgan finds that households in states where payday lending is unlimited enjoy a greater level of welfare than those in states where payday is not authorized. Therefore, he concludes that payday lending is not predatory.

The author also hypothesizes that payday lender competition, measured by payday loan shops per capita, decreases the costs of loans. Morgan compares fees reported in a 2001 survey with more recent state shop data and concludes that payday loans in states with higher payday stores per capita carry modestly lower costs.

The rationale and findings of this paper are flawed for the following reasons:

1. COMPARISONS BETWEEN "UNLIMITED" PAYDAY AND NON-AUTHORIZING STATES NOT POSSIBLE IN 2001 BECAUSE OF BANK AGENCY MODEL.

The crux of Morgan's findings rest on the comparison of states that had unlimited payday lending in 2001 to those that did not specifically authorize the product. Unfortunately, because of some mis-identifications of non-authorizing states and the "bank agency" model of payday lending prevalent across the country in 2001, this study—and its findings—are fundamentally flawed.

Morgan identifies 18 states that he determines not to allow payday. Indeed, some of these states expressly did not permit payday lending. Others had active payday stores operating and did not address these loans specifically in law. In all of these states, however, payday lending stores could still operate under a "bank agency" (sometimes called rent-a-bank or rent-a-charter) model, in which a payday lender partners with a federally-insured bank in order to export favorable lending laws from the bank's home state to consumers in states where lending is more restrictive.[1] These arrangements were commonplace in 2001 – one payday lending company alone had 431 shops in so-called non-authorizing states.[2] As a result, comparisons between unlimited payday lending states and those which did not specifically authorize payday (but in fact they were saturated with payday lending shops) are not possible. Notable examples are detailed in the Appendix.

2. QUESTIONABLE DEFINITIONS OF PREDATORY LENDING, RISKY HOUSEHOLDS, AND WELFARE.

Morgan's definition of predatory lending as a welfare-reducing event with negative impacts for families is certainly a reasonable approach for capturing this problem. Families preyed on by unscrupulous lenders could be said to have less overall welfare than families utilizing responsible credit products. However, his measurement of welfare is quite narrow, only taking into account a family's overall debt level and timeliness of bill payments. A more inclusive definition of predatory lending such as "the lack of a fair exchange of value or loan pricing that reaches beyond the risk that a borrower represents or other customary standards" as proposed by the FDIC could be part of a more suitable definition upon which to judge whether payday lending is predatory.[3]

Morgan also creates a "risky" household profile as a proxy for payday borrowers by using two variables: households who feel their future income may be uncertain and those without a college degree. While these households may indeed be more "at risk" than those with more income security and education, these proxies do not necessarily lead to a greater propensity to use payday loans. In fact, payday industry data shows that payday borrowers have similar education attainment levels as the overall population.[4] In addition, it is uncertainty of expenses (not income), which has been found to primarily drive payday consumption.[5] We posit that payday borrowers have relatively stable incomes, since the requirements for a payday loan include a bank account and a regular paycheck or other source of income.

In summary, while Morgan's attempts to define these murky topics are certainly commendable, the narrow interpretations of family welfare and likely payday borrowers make it impossible to draw broad conclusions regarding the impact of payday lending on the welfare of "risky" households. The author concedes this point in the Conclusion, in which he states, "…perhaps payday loans help risky households better manage their finances? It will take more data to confirm that particular conjecture…"[6]

3. PURPORTED LINK BETWEEN PAYDAY STORE SATURATION AND LOWER COSTS IN CONFLICT WITH REGULATOR DATA AND OTHER RESEARCH.

Morgan's finding that "payday loan rates and fees decline significantly as the number of payday lenders…increase" is contradicted by a number of other studies that strongly suggest state rate caps determine the typical payday loan fee. For example:

- In 2005 researchers affiliated with the Federal Deposit Insurance Corporation (FDIC) analyzed a random, national sample of 600 payday stores and found that payday lenders charged an effective annual percentage rate (APR) near the state statutory limit. These researchers concluded that "competition does not appear to affect fees charged in the way [one] normally thinks that competition will affect loan market interest rates."[7]

- Similarly, researchers at the University of North Carolina while reviewing regulator-collected data on NC-based payday firms noted in 2003 that a payday loan's APR is mostly a function of loan term because "most companies charge the maximum fees permitted by law."[8]

- In a 2004 analysis of Colorado payday lending data, Chessin found that a borrower's payday lending costs appear to be inelastic with 89.27 percent of all loans charging the state's maximum permissible rate. In fact, Chessin noted that despite an increase from 212 locations in 2000 to 616 locations at the end of 2004 (i.e. more stores per capita), the frequency of loans charged at the state limit *increased* albeit modestly from 89.27 percent in 2002 to 92.75 percent in 2004.[9]

One other issue with Morgan's analysis is his comparison of reported fees from 2001 with stores per capita from 2005. Given that the industry's regulatory landscape has changed rather dramatically since 2001 (as previously noted) and the total national number of payday loan shops has increased from some 10,000 in the beginning of 2001 to 23,000 shops thru 2005,[10] any comparison between fees charged in 2001 and storefront saturation in 2005 would likely be strained.

Appendix

Morgan identifies many states as not allowing payday lending in 2001 that were among the most payday saturated during that period. Each of the states listed below was categorized in *Defining and Detecting Predatory Lending* as a non-authorizing state.

- North Carolina was one of the most payday-saturated states in the nation at the time, with over 500 storefronts.[11] Even when the law authorizing payday lending expired at the end of August 2001, payday lending continued in the state unabated due to rent-a-bank charters. In 2005, an estimated 385 payday loan stores continued to operate in the state.[12] Not until a March 2006 Attorney General settlement agreement did payday lending effectively end in North Carolina.[13]

- Indiana was found to have a thriving $510 million a year payday loan industry operating within its borders in this time period, with an estimated 500 payday store locations throughout the state.[14]

- Arkansas passed a law authorizing payday lending in 1999. Despite a court challenge in 2001 because of the law's conflict with a state constitutional interest limitation of seventeen percent per annum, payday licenses were still granted and businesses continued to operate. In 2004, 275 payday stores were operating in Arkansas and these loans continue to be made in that state to this day.[15]

- Michigan's Attorney General reported about 650 payday lending storefronts in 2001.[16]

- In New York, the state regulator found thirty-two Internet payday lenders making payday loans to New Yorkers in 2000, many of which were partnered with County Bank, a Delaware state-chartered bank.[17] Attorney General Spitzer later sued and successfully shut down these arrangements along with the FDIC actions to halt these abuses of a bank charter.

- A 2001 survey found that payday loans were made by storefronts in Georgia and Virginia at triple-digit APRs through partnership with banks primarily located in Delaware.[18]

- In Pennsylvania, the Attorney General in 1999 stated his approval of payday stores operating there through the bank agency model despite being in excess of usury limits.[19]

- In West Virginia, First American Cash Advance opened it first stores in 2001 and quickly grew to 11 payday shops. Not until 2006 did the company suspend its operations in West Virginia.[20]

- Finally, legal challenges and regulatory interpretations enabled payday lending to continue in Alabama throughout 2001 despite loans exceeding the state's small loan interest rate cap.[21]

One of the largest payday lenders in the country—Advance America—has released its number of storefronts on a state-by-state basis for several consecutive years as part of its annual report. While this only documents one lender's market presence by state in 2001, it plainly demonstrates how states identified by Morgan as having not authorizing payday lending in fact had significant numbers of payday shops in operation during this time period.

State identified as "non-authorizing" in 2001 by Morgan	Advance America locations in 2001
Alabama	53
Arkansas	27
Georgia	67
Indiana	77
Michigan	27
North Carolina	124
Virginia	56

Just these seven "non-authorizing" states make up over a quarter of Advance America's total 1,558 locations in 2001.

[1] Further discussions of the bank agency model of payday lending can be found in *Rent-a-Bank Payday Lending: How Banks Help Payday Lenders Evade State Consumer Protections* (at http://www.consumerfed.org/pdfs/paydayreport.pdf) and, more recently, in *Georgia's Payday Loan Law: A Model for Preventing Payday Lending* (at http://www.responsiblelending.org/issues/payday/policy/page.jsp?itemID=29472890).
[2] Appendix table from Advance America's annual reports. On file with author.
[3] FDIC Financial Institution Letter. Supervisory Policy on Predatory Lending, January 22, 2007. Available at http://www.fdic.gov/news/news/financial/2007/fil07006.html.
[4] The Community Financial Services Association released an *Analysis of the Payday Advance Industry* in 2001, which found that 27% of payday borrowers had at least some college and 11% held a college degree. In comparison, they report that 28% of the total adult population had at least some college and 13% held a college degree. A 2002 IO Data survey of 2,600 payday borrowers found that 34% had at least some college and 21% held at least a college degree.
[5] See findings from a 2002 IO Data survey of 2,600 payday borrowers commissioned by the Community Financial Services Association of America (CFSA), which found that 52% of borrowers took out a payday loan because of an unexpected expense and 10% because of an expected expense, compared to 18% that had a temporary reduction in income.
[6] *Defining and Detecting Predatory Lending*, page 22.
[7] From *Payday Lending: Do the Costs Justify the Price*, Mark Flannery and Katherine Samolyk, pg 9-10. June 2005
[8] From *Payday Lending: A Business Model that Encourages Chronic Borrowing*. Michael Stegman and Robert Faris, pg 23. Economic Development Quarterly, March 2003

[9] From *Borrowing Peter to Pay Paul: A Statistical Analysis of Colorado's Deferred Deposit Loan Act*, 400; 408-409. Denver University Law Review, Vol. 83, Iss. 2

[10] Stephens Inc. *Presentation at CFSA Conference*, March 2, 2006; Stephens Inc. *Update on the Payday Loan Industry: Observations on Recent Industry Developments*, September 26, 2003.

[11] From *Rent-a-Bank Payday Lending: How Banks Help Payday Lenders Evade State Consumer Protections*, Consumer Federation of America and the U.S. Public Interest Research Group, November 2001. Available at http://www.consumerfed.org/pdfs/paydayreport.pdf.

[12] From *Race Matters: The Concentration of Payday Lenders in African-American Neighborhoods in North Carolina*, Center for Responsible Lending, March 2005. Available at http://www.responsiblelending.org/issues/payday/reports/page.jsp?itemID=28012448.

[13] *Payday Lending on the way out in NC,* press release by North Carolina Attorney General, March 1, 2006. Available at http://www.ncdoj.com/DocumentStreamerClient?directory=PressReleases/&file=paydaylenders3.06.pdf

[14] From *Race Matters: The Concentration of Payday Lenders in African-American Neighborhoods in North Carolina*, Center for Responsible Lending, March 2005. Available at http://www.responsiblelending.org/issues/payday/reports/page.jsp?itemID=28012448.

[15] Payday Lenders in Arkansas: The Regulated and the Unregulated, Arkansans Against Abusive Payday Lending, February 2006. Available at http://www.stoppaydaypredators.org/pdfs/news%20articles/06_0200_Payday_U_Study.pdf.

[16] Gregg Krupa, *The Detroit News*, "Payday Loans Trap Borrowers," August 19, 2001.

[17] From *Internet Payday Lending : How High-Priced Lenders Use the Internet to Mire Borrowers in Debt and Evade State Consumer Protections*, Consumer Federation of America, November 2004. Available at http://www.consumerfed.org/pdfs/Internet_Payday_Lending113004.pdf.

[18] From *Rent-a-Bank Payday Lending: How Banks Help Payday Lenders Evade State Consumer Protections*, Consumer Federation of America and the U.S. Public Interest Research Group, November 2001. Available at http://www.consumerfed.org/pdfs/paydayreport.pdf.

[19] From *Show Me the Money! A Survey of Payday Lenders and Review of Payday Lender Lobbying in State Legislatures*, Consumer Federation of American and the U.S. Public Interest Research Group, February 2000. http://www.uspirg.org/uploads/0J/JI/0JJIxjolTQlIpsOOhaP_dg/showmethemoneyfinal.PDF.

[20] Greg Hohmann, *Charleston Daily Mail*, "State's only payday lender leaves the area," October 27, 2006 at http://www.pliwatch.org/news_article_061027A.html

[21] From *Show Me the Money! A Survey of Payday Lenders and Review of Payday Lender Lobbying in State Legislatures*, Consumer Federation of American and the U.S. Public Interest Research Group, February 2000.

Appendix C

Summary of Research on Payday and Car Title Lending, 1998-present, by
Center for Responsible Lending
Consumer Federation of America
National Consumer Law Center

A. Center for Responsible Lending

1. Quantifying the Economic Cost of Predatory Payday Lending (Keith Ernst, John Farris and Uriah King, Dec 2003)
    - 91% of all payday loans are made to borrowers with five or more payday loans per year;
    - Two in three borrowers (66%) incur five or more payday loans per year, while nearly one in three (31%) receive twelve or more loans per year;
    - Borrowers, on average, receive 8 to 13 payday loans per year; and
    - 5 million payday borrowers are caught in this debt trap each year.

2. Race Matters: The Concentration of Payday Lenders in African-American Neighborhoods in North Carolina (Uriah King, Wei Li, Delvin Davis and Keith Ernst, Mar 2005)
    - African-American neighborhoods have three times as many stores per capita as white neighborhoods. This disparity increases as the proportion of African-Americans in a neighborhood increases.
    - This three-fold disparity remains unchanged even when we control for the neighborhood characteristics of income, homeownership, poverty, unemployment rate, urban location, age, education, share of households with children, and gender.

3. Car Title Lending Driving Borrowers to Financial Ruin (Amy Quester, CRL; Jean Ann Fox, CFA, Apr 2005)
    - General description of the car title lending model, recommending the following:
        i. Establishing fair and affordable loan terms.
        ii. Protecting borrowers after default.
        iii. Closing loopholes to ensure consistent regulation.
        iv. Monitoring lenders through licensing, bonding, reporting, and examination requirements.
        v. Ensuring borrowers can exercise their rights.

4. Payday Lenders Target the Military (Ozlem Tanik, Sep 2005)
    - Active-duty military personnel are three times more likely than civilians to have taken out a payday loan.
    - One in five active-duty military personnel were payday borrowers last year.
    - Predatory payday lending costs military families over $80 million in abusive fees every year.

5. Financial Quicksand: Payday lending sinks borrowers in debt with $4.2 billion in predatory fees every year (Uriah King, Leslie Parrish and Ozlem Tanik, Nov 2006)
    - Ninety percent (90%) of payday lending revenues are based on fees stripped from trapped borrowers, virtually unchanged from our 2003 findings. The typical payday borrower pays back $793 for a $325 loan.
    - Predatory payday lending now costs American families $4.2 billion per year in excessive fees.
    - States that ban payday lending save their citizens an estimated $1.4 billion in predatory payday lending fees every year.

6. Springing the Debt Trap: Rate caps are only proven payday lending reform (Uriah King and Leslie Parrish, Dec 2007)
    - The debt trap of payday lending persists even in states that have attempted to reform the practice. In these states, 90 percent of payday lending business is generated by trapped borrowers with five or more loans per year. More evidence that the debt trap persists:
        i. Over 60 percent of loans go to borrowers with 12 or more transactions per year;
        ii. 24 percent of loans go to borrowers with 21 or more transactions per year;
        iii. One of every seven Colorado borrowers have been in payday debt every day of the past six months;
        iv. Nearly 90 percent of repeat payday loans are made shortly after a previous loan was paid off. 4 Springing the Debt Trap: Rate caps are only proven payday lending reform
    - As implemented in any state, none of these restrictions have stopped payday lending from trapping borrowers in long-term debt:
        i. Renewal bans/cooling-off periods
        ii. Limits on number of loans outstanding at any one time
        iii. Payment plans
        iv. Loan amount caps based on a borrower's income
        v. Databases which enforce ineffective provisions
        vi. Regulations that narrowly target payday loans
    - Those states which enforce a comprehensive interest rate cap at or around 36 percent for small loans have solved their debt trap problem; realizing a savings of $1.5 billion for their citizens while preserving a more responsible small loan market.

7. High-Cost Payday Lending Traps Arizona Borrowers (Leslie Parrish, Sep 2008)
    - Over 700 payday lenders charging up to 459% annual percentage rate (APR) for a two-week loan are located throughout Arizona; with the highest concentrations per capita in Pinal, Mohave, and Maricopa Counties.
    - A typical Arizona borrower pays an estimated $516 in fees for a $325 payday loan and still owes the $325 in principal. Overall, payday lending costs Arizona families nearly $149 million each year. Payday lending drains $91 million and $23 million from Maricopa and Pima County households, respectively.

8. Wealth-stripping payday loans trouble communities of color (Aracely Panameno and Keith Corbett, Oct 2008)

- People of color have less wealth than their white counterparts, making them more vulnerable to predatory lending. This, in turn, threatens to further widen the wealth gap.
- Research from several states suggests that people of color are disproportionately impacted by 400 percent APR payday lending. An examination of payday lending storefront locations in Maricopa and Pima Counties—in which over three-quarters of Arizona payday lenders are located—reveals a pattern of these stores clustering in communities of color.

9. Predatory Profiling: The Role of Race and Ethnicity in the Location of Payday Lenders in California (Wei Li, Leslie Parrish, Keith Ernst, and Delvin Davis, Mar 2009)
    - Payday lenders are nearly eight times as concentrated in neighborhoods with the largest shares of African Americans and Latinos as compared to white neighborhoods, draining nearly $247 million in fees per year from these communities.
    - Even after controlling for income and a variety of other factors, payday lenders are 2.4 times more concentrated in African American and Latino communities. On average, controlling for a variety of relevant factors, the nearest payday lender is almost twice as close to the center of an African American or Latino neighborhood as a largely white neighborhood.
    - Race and ethnicity play a far less prominent role in the location of mainstream financial institutions, such as bank branches. While race and ethnicity account for over half of the variation in payday lender location explained by neighborhood factors, they explain only one percent of the variation in bank branch locations.

10. Phantom Demand: Short-term Due Date Generates Need for Repeats Payday Loans (Leslie Parrish and Uriah King, Jul 2009)
    - The great majority of payday loans are originated shortly after a previous loan is paid back, with half of new loans opened at the borrower's first opportunity, and 87 percent opened within two weeks.
    - Borrower churn inflates payday loan volume by over $20 billion each year, with three of every four loans generated by the debt trap.
    - This churning of loans to borrowers each pay period costs these households $3.5 billion in extra fees each year.

11. High-Cost Payday Lending Traps Mississippi Borrowers (Jennifer Johnson, Jul 2010)
    - Over 900 payday lenders charging up to 572% annual percentage rate (APR) for a two-week loan are located throughout Mississippi; with the highest concentrations per household in Tunica, Attala, and Leake Counties.
    - A typical Mississippi borrower pays an estimated $691 in fees for a $350 payday loan and still owes the $350 in principal. Overall, payday lending costs Mississippi families over $270 million each year. Payday lending drains $2.2 million and $3.9 million from Tunica and Attala County households, respectively.

12. Payday Lenders Pose as Brokers to Evade Interest Rate Caps: The next chapter in payday lender subterfuge (Diane Standaert and Sara Weed, Jul 2010)
    - Payday lenders repeatedly attempt to dodge reforms
    - Payday loans brokered through credit repair laws perpetuate the debt trap

13. Payday Loans, Inc.: Short on Credit, Long on Debt (Uriah King and Leslie Parrish, Mar 2011)
    - The typical payday borrower remains in payday loan debt for much of the year, and many borrowers remain indebted in payday loans for extended periods of time.
        i. In their first year of payday loan use, borrowers are indebted an average of 212 days. Over the full two-year period, borrowers are indebted a total of 372 days on average.
    - Payday borrowers' loans increase in size and frequency as they continue to borrow.
        i. Those payday borrowers who continue to take out loans over a two year period have 12 payday transactions in their second year of borrowing, up from 9 transactions in the first year.
    - A significant share of borrowers become late or default on their payday loan, triggering more fees and placing their bank account at risk.
        i. Over the first two years of payday loan use, 44 percent of borrowers will experience a "return event" or default in which they are cannot service their payday loan debt in a timely manner.

14. Big Bank Payday Loans: High-interest loans through checking accounts keep customers in long-term debt (Rebecca Borne, Joshua Frank, Peter Smith and Ellen Schloemer, Jul 2011)
    - Bank payday loans are very expensive, carrying an annual percentage rate (APR) of 365 percent based on the typical loan term of 10 days.
    - "Short-term" bank payday loans often lead to a cycle of long-term indebtedness—on average, bank payday borrowers are in debt for 175 days per year (twice as long as the maximum length of time the FDIC has advised).
    - Nearly one-quarter of all bank payday borrowers are Social Security recipients, who are 2.6 times as likely to have used a bank payday loan as bank customers as a whole.

15. Driven to Disaster: Car-Title Lending and Its Impact on Consumers (Delvin Davis and Uriah King, CRL; Jean Ann Fox and Tom Feltner, CFA, Feb 2013)
    - • Approximately 7,730 car-title lenders operate in at least 21 states costing borrowers $3.6 billion each year in interest on $1.6 billion in loans.
    - The average car-title borrower renews their loan eight times, paying $2,142 in interest for $951 in credit.
    - Car-title loans' annualized percentage rates (APR) are especially excessive considering the value of the collateral and the relatively low amount of the loan. In our borrower-level data set, the median loan-to-value ratio was 26 percent, yet the APR was 300 percent.
    - One in six borrowers in our data set also faced repossession, with repossession fees averaging half of the borrower's outstanding loan balance.

16. Triple-Digit Danger: Bank Payday Lending Persists (Rebecca Borné and Peter Smith, Mar 2013)
    - Bank payday loans carry an annual percentage rate (APR) that averages 225 to 300 percent.
    - The median bank payday borrower took out 13.5 loans in 2011 and spent at least part of six months during the year in bank payday debt. Over a third of borrowers took out more than 20 loans, bringing the mean number of loans per borrower to 19.

- Bank payday borrowers are two times more likely to incur overdraft fees than bank customers as a whole.
- Over one-quarter of all bank payday borrowers are Social Security recipients.

17. State of Lending: Car-Title Lending (Susanna Montezemolo, Jul 2013)
    - Balloon payment car title loans lead to repeat borrowing, enforced by the threat of repossession.
        i. The typical TitleMax loan is refinanced 8 times.
    - Borrowers who take out the typical nine title loans in a year pay back over three times the amount borrowed: $3,391 in payments for a $1,042 loan.
    - Car-title lenders originate an estimated 2.0 million car-title loans each year worth $1.9 billion in annual loan dollar volume, not including churn. Borrowers pay $4.3 billion in fees alone on these loans.

18. State of Lending: Payday Lending (Susanna Montezemolo, Sep 2013)
    - Loan churn in states with no restrictions on payday lending costs borrowers at least $2.6 billion in excess fees annually.
    - 16,341 payday stores are located in states without substantive restrictions on payday lending, with total loan dollar volume (including churn) of $19.9 billion and total fees collected of $3.4 billion.
    - The evidence shows that the majority of payday borrowers are trying to address budget gaps caused by recurring, everyday expenses; they are not trying to address the occasional emergencies payday lenders claim are the key reasons borrowers to take out loans.
    - 85% of loans go to borrowers with seven or more loans in a year, more than the maximum level of indebtedness recommended by the FDIC.

19. State of Lending: Bank Payday Lending (Rebecca Borne and Peter Smith, Sep 2013)
    - Bank payday costs and loan term translate to an annual percentage rate (APR) ranging from 225% to 300%.
    - The median bank payday borrower took out 13.5 loans in 2011 and was in bank payday loan debt at least part of six months annually. The mean number of loans was 19.
    - 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.
    - Banks that permit installment repayment plans make these plans difficult to qualify for or obtain.
    - Banks' cooling-off periods allow borrowers to become mired in a cycle of debt before the cooling-off period is triggered.
    - More than one-quarter of bank payday borrowers are Social Security recipients.

20. Car Title Lending: Disregard for Borrowers' Ability to Repay (May 2014)
    - Car title advertisements emphasize their lack of underwriting standards.
    - Car title lending leads to repeat refinancing and repossessions.

21. Analysis: New State Data Show California Payday Lenders Continue to Rely on Trapping Borrowers in Debt (Paul Leonard and Graciela Aponte, Oct 2014)

- Payday lenders rely on borrowers who get stuck in a cycle of repeat borrowing.
    i. 76% percent of all payday loan fees are due to borrowers stuck in 7 or more payday loans per year.
    ii. 60% of payday loan fees are from borrowers with 10 or more loans in a year.
- The long-term debt trap is the most typical borrower experience.
    i. Borrowers taking out 7 or more loans per year accounted for 45% of borrowers.
    ii. The "10 or more" loan category was the single largest, accounting for 29% of all borrowers. Conservatively, borrowers in this category received an average of 13 loans annually, or more than one loan per month.
- The debt trap in California is growing deeper: The number of borrowers with 10 or more loans in 2013 increased by 11 percent over 2012, even as the total number of payday loans declined slightly over the same period.
- Payday loans that are used only occasionally – as they are advertised – account for only a small portion of payday lending business.
    i. Only 4 percent of all payday loan activity in 2013 was from borrowers with just one loan in 2013. These borrowers accounted for 22% of all borrowers.
    ii. Only 15 percent of all payday loan activity in 2013 was from borrowers with 4 or fewer loans.

22. Payday Mayday: Visible and Invisible Payday Lending Defaults (Susanna Montezemolo and Sarah Wolff, Mar 2015)
    - Nearly half of all payday borrowers defaulted within two years of their first loan.
    - Of borrowers who defaulted, nearly half did so within the first two payday loans.
    - Default does not necessarily signal the end of payday borrowing, with many defaulters going on to repay their loan and even borrow (and possibly default) again at a later date.
    - Nearly one in five borrowers had a loan charged off by the lender.
    - One-third of payday borrowers experienced at least one invisible default in which their account was overdrawn on the same day that they made a payment to a payday lender.
    - For payday borrowers, overdrafts and bounced transactions frequently occurred close in time to the use of payday loans. Nearly half of payday borrowers incurred an overdraft or NSF fee in the two weeks after a payday loan transaction, and 64% paid overdraft or NSF fees at some point.

23. Payday and Car Title Lenders' Migration to Unsafe Installment Loans (Diane Standaert and Peter Smith, Oct 2015)
    - Evidence of payday and car title lenders offering more installment loan products.
    - Installment loans show evidence of unaffordability: repeat borrowing, delinquencies, and defaults.

24. The Buckeye Burden: An Analysis of Payday and Car Title Lending in Ohio (Diane Standaert and Delvin Davis, Nov 2015)
    - There are 836 storefronts in Ohio that make payday or car title loans, the majority of which (59%) offer both forms of high-cost loans.
    - Payday and car title loans drain more than $502 million in predatory loan fees from Ohioans annually, twice as much as what payday loans drained in 2005.

- Larger, longer-term payday and car title loans with triple-digit interest rates further expose Ohioans to the harms of unaffordable loans secured by their bank accounts and cars.

25. Predatory Payday and Larger Installment Loans Overshadow Emerging Market for Smaller, Less Expensive Installment Loans in California (Paul Leonard, Dec 2015)
    - Payday lenders rely on borrowers who get stuck in a cycle of repeat borrowing. 76% percent of all payday loan fees are due to borrowers stuck in 7 or more payday loans per year. 60% of payday loan fees are from borrowers with 10 or more loans in a year.
    - Not only do these high-cost lenders charge triple-digit rates, but several of them report high charge-off rates.
    - Surge of small loans between $250 and $2,500 shows promising possibilities for California's small dollar loan pilot programs, increasing 116% from 2009 to 2014.

26. Perfect Storm: Payday Lenders Harm Florida Consumers Despite State Law (Brandon Coleman and Delvin Davis, Mar 2016)
    - Florida's payday loan law – passed in 2001 and sold as a measure to prevent the debt trap – fails to stop the wealth stripping effects of payday loans with APRs averaging 278%.
    - With more payday loan stores than Starbucks, payday lenders have stripped over $2.5 billion in fees from Floridians since 2005, with over $311 million collected last year alone.
    - Payday loans to trapped borrowers generate the majority of payday loan volume. Last year, over 83% Florida payday loans were to Floridians stuck in 7 or more loans.
    - The economic drain of payday lending is disproportionately concentrated in Florida's black and Latino communities, and has seen significant growth among senior citizens

27. Payday and Car Title Lenders Drain $8 Billion in Fees Every Year (Diane Standaert and Delvin Davis, May 2016)
    - Payday loans drain over $4.1 billion in fees a year from people in the 36 states that allow triple-digit interest rate payday loans.
    - Car title loans drain approximately $3.9 billion in fees annually from people in 23 states.

28. States without Payday and Car-title Lending Save $5 Billion in Fees Annually (Delvin Davis and Susan Lupton, Jun 2016)
    - Estimates that states without payday and car title have saved nearly $5 billion a year in fees annually – $2.2 billion from payday lending, plus another $2.8 from car title lending.

29. Shark-Free Waters: States are Better Off without Payday Lending (Robin Howarth, Delvin Davis and Sarah Wolff, Aug 2016)
    - State payday loan bans save consumers more than $2.2 billion annually in fees that would otherwise be paid to payday lenders.
    - Payday loan restrictions do not force consumers to use products that cause greater harm than payday loans. Borrowers in states without payday loans employ a variety of strategies to address a cash flow shortfall at a fraction of the cost of payday loans.

- In addition to protecting consumers from the high costs of payday loans, state payday lending restrictions also help borrowers by preventing the long-term harms associated with these loans. These harms include: increased difficulty paying bills, delayed medical spending, involuntary bank account closure, higher likelihood of filing for bankruptcy, and decreased job performance.
- Finally, there is broad public support for maintaining the rate caps in states that prevent the harms of the typical 400% payday loan, both from citizens at large and from former payday borrowers.

B. Consumer Federation of America

1. The Growth of Legal Loan Sharking: A Report on the Payday Loan Industry (Jean Ann Fox, Nov 1998)
    - Explains the different aspects of the payday loan industry, and the debt treadmill.
    - Recommends states enforce usury laws, forbid rollovers, and that Congress close any legal loopholes.

2. Safe Harbor for Usury: Recent Developments in Payday Lending (Jean Ann Fox, Sep 1999)
    - Overview of payday lending, and its growth on a state level, recommending:
        i. Congress should close the national bank exportation loophole and protect consumers.
        ii. States should maintain and enforce interest rate caps for small loans.
        iii. States should strengthen existing state payday loan laws.

3. Show Me The Money!: A Survey of Payday Lenders and Review of Payday Lender Lobbying in State Legislatures (Jean Ann Fox, CFA, and Edmund Mierzwinski, US PIRG, Feb 2000)
    - Payday loans are being made in states despite usury ceilings.
    - Payday lenders using national bank charters to avoid state regulation.
    - Stores did not quote APR on payday loans.
    - Payday lenders appear to exceed fee limits.
    - Danger of additional bounced check (NSF) fees.
    - Cost of loan often confused by fees based on total check or total loan.

4. Rent-A-Bank Payday Lending: How Banks Help Payday Lenders Evade State Consumer Protections (Jean Ann Fox, CFA, and Edmund Mierzwinski, US PIRG, Nov 2001)
    - Payday lending continues its rapid growth and expansion into more states.
    - State lawmakers and regulators are showing increasing resistance to legalizing triple digit interest loans based on checks held for future deposit.
    - The payday loan industry is attempting to avoid state consumer protection laws by partnering with banks, while states step up efforts to enforce state laws.
    - CFA and PIRG staff and volunteers surveyed 235 payday lenders doing business in 20 states and the District of Columbia. The survey included stores in six states that effectively prohibit payday lending through usury regulation (Category 1 states), in two states with no law (Category 2 states) and 12 states where payday lending is authorized and regulated (Category 3 states).

- Payday lenders surveyed charge consumers an average Annual Percentage Rate (APR) of 470% and an average fee of $18.28 to borrow $100 for two weeks. APRs ranged from 182%-910% and fees ranged between $10-$35 per $100 borrowed.
- Fifteen percent (15%) of payday lenders in states that cap fees quoted rates higher than allowed by law in that state and an additional 38% of payday lenders quoted rates exactly at the allowable APR.
- The most common APR found was 390% APR, imposed by 30% of all stores. The next most common APR found was 520%, imposed by 18% of all stores. An additional 21% of stores charged APRs clustered narrowly between 442-459%.
- One-third (33%) of all stores imposed APRs greater than 500%. The following chart shows the range of APRs found for the 233 of 235 stores where enough information was provided to calculate an APR.
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5. Unsafe and Unsound: Payday Lenders Hide Behind FDIC Bank Charters to Peddle Usury (Jean Ann Fox, Mar 2004)
    - Banks continue to play a major role in enabling payday loan chains to evade state usury, small loan and payday loan laws. Ten state-chartered FDIC supervised banks are the only financial institutions known to be partnering with pawn chains, check cashers, and payday lenders, following regulatory action by the Comptroller of the Currency, Office of Thrift Supervision, and Federal Reserve.
    - The Federal Deposit Insurance Corporation, the last bank regulator to issue payday loan enforcement guidelines for banks that partner with payday lenders, has taken no payday loan guideline enforcement action involving state-chartered FDIC supervised banks. Since the FDIC guidelines were issued in July 2003, three more FDIC regulated banks have entered into partnerships with payday lenders. The FDIC permitted a Federal Reserve-member bank to switch regulators in order to continue its lucrative payday loan business.
    - The payday loan industry's goal is safe harbor legislation in every state. Currently 33 states and the District of Columbia authorize payday loans by law or regulation, and two additional states have no usury limits for small loans by licensed lenders. Fifteen states prohibit payday lending through operation of usury or loan laws and a growing number of states prohibit retailers from brokering loans for out-of-state banks.
    - Payday lenders face growing resistance from state legislatures, especially in states where loans are not legal. In 2004 the Michigan Governor vetoed a safe harbor bill and Georgia legislators passed a tough anti-payday loan enforcement bill.
    - Industry analysts in early 2003 reported a 50 percent increase in the number of payday loan outlets as of since year-end 2000 and double the fee revenue. Growth in industry size is fed by additional states authorizing payday lending, expansion of lending into

states through rent-a-bank arrangements and other devices as well as repeat borrowing by current customers.

6. Internet Payday Lending: How High-Priced Lenders Use the Internet to Mire Borrowers in Debt and Evade State Consumer Protections (Jean Ann Fox and Anna Petrini, Nov 2004)
    - Payday lending has expanded from check cashing outlets, pawn shops and payday loan outlets to the Internet. Loans are marketed, delivered and collected online at rates and terms that mire cash-strapped consumers in repeat borrowing at extremely high costs. Finance charges are in the $25 (650% APR) to $30 (780% APR) per $100 borrowed range, with built in loan flipping in many contracts.
    - Web sites marketing and/or delivering small loans are growing rapidly, with numerous referral sites feeding applications to actual lenders. Lenders are hard to locate, identify or contact. Some are licensed in their home states, while others hide behind anonymous domain registrations or are located outside the United States.
    - Banks are involved in Internet payday loans through the Automated Clearing House System (ACH) used to electronically deliver loans to consumers' bank accounts and to withdraw payments. County Bank of Rehoboth Beach, DE, participates directly in Internet payday lending.
    - Internet payday lenders bypass state usury laws and consumer protections by locating in lax regulatory states and making loans without complying with licensing requirements or state protections in the borrower's home state. State regulators, notably in Kansas, New York and Colorado, are beginning to enforce state usury and small loan laws against lenders making loans online to state consumers.
    - Payday loan applications made online expose consumers to privacy and security risks as bank account numbers, Social Security numbers, and other personal financial information are transmitted to lenders, often over unsecure web links. Privacy policies do not protect privacy.
    - Federal electronic banking laws and industry self-regulatory rules for use of the Automated Clearing House (ACH) system do not adequately protect consumers who use electronic fund transfers to borrow and repay loans from bank accounts.

7. Car Title Lending Driving Borrowers to Financial Ruin (Amy Quester, CRL; Jean Ann Fox, CFA, Apr 2005)
    - General description of the car title lending model, recommending the following:
        i. Establishing fair and affordable loan terms.
        ii. Protecting borrowers after default.
        iii. Closing loopholes to ensure consistent regulation.
        iv. Monitoring lenders through licensing, bonding, reporting, and examination requirements.
        v. Ensuring borrowers can exercise their rights.

8. Driven into Debt: CFA Car Title Loan Store and Online Survey (Jean Ann Fox and Elizabeth Guy, Nov 2005)
    - Title loans are extremely expensive. Title loan stores charge a median 25 percent per month finance charge, which translates to 300 percent annual interest, plus additional fees averaging $25 per loan. Online title lenders quote rates of 24 to 651.79 percent APR

for loans fully secured by the title to the borrower's paid for car, but the low rate is charged by a lender that charges high fees for additional products.

- Title loans trap borrowers in perpetual debt. Lenders don't run credit checks or base loans on the borrower's ability to repay. Loans are generally due in one month, with interest only renewals available. Since most lenders hold a duplicate set of car keys, non-judicial repossession is easy.
- Title lenders structure their loans to evade state usury or small loan rate caps. In California and South Carolina, loans start at dollar amounts just above the cut-off for small loan rate caps. In Virginia, Iowa and Kansas, title loans are claimed to be open-ended credit to benefit from the deregulation of credit cards in those states. Title lenders making loans via the Internet export high cost loans to consumers in protected states by using dubious choice of law claims from states with no rate caps.
- Title loans are over-secured. Title lenders loan a fraction of the value of the car used to secure the loan, with the most frequent loan-to-value set at 50 to 55 percent of the car's value, a higher percentage than we expected. In Virginia, many title lenders will loan up to 100 percent of the value of the car.
- Information necessary to make an informed credit decision is hard to come by. Only four title loan websites disclosed an annual percentage rate prior to applications being submitted. Store personnel often quoted monthly finance charges as an interest rate instead of the federally required annual percentage rate. Store clerks gave confusing and contradictory cost information. Consumers were only able to obtain reliable pre-loan information in states that require licensees to post rates and fees or to provide brochures on consumer rights.
- Rate regulation is necessary to reduce the price of loans. Store surveys found the lowest rates in Arizona, where rates are capped at no more than 17 percent per month on loans up to $500, and at lower levels for larger loans. In states with high rate caps, title lenders with few exceptions charged the legal maximum. Rates were highest in states with no rate caps, such as Illinois, where the annualized rates ranged from 300 to 470 percent or New Hampshire where title loans cost 300 to 366.9 percent.
- Permissive state laws and lender exploitation of loopholes and gaps in protections leave vulnerable consumers exposed to high risk title loans. Title lending passes for pawn transactions in Georgia and Alabama as a result of court decisions that have not led to corrective state laws. Almost half the states permit predatory title lending, either through weak authorizing laws or failure to close loopholes.
- State laws set the stage for title loan debt traps by setting high maximum loan ceilings and permitting one-month balloon payments. For example, Tennessee and Mississippi permit loans as large as $2,500 to be due in 30 days. New Hampshire caps its title loans at $10,000 with no rate cap and permits 11 loan renewals with only five percent reductions in the original principle each time, resulting in a balloon payment at the end. Georgia sets a 30 day loan but fails to limit loan size.
- Internet title loans may deprive consumers of home state law protections. Some online lenders claim choice of law contract terms from states, such as New Mexico and Delaware, with lax credit laws. Consumers who live in states with protective credit and pawn laws are exposed to online title loan abuses.

9. Cashed Out: Consumers Pay Steep Premium to 'Bank' at Check Cashing Outlets (Jean Ann Fox and Patrick Woodall, Nov 2006)
    - Cost to Cash Benefit Checks Increased: In 2006, the 2.44 percent charged by average check cashing outlets to cash Social Security checks was 15.6 percent more expensive than the 2.11 percent charged a decade earlier. The 2006 rate was significantly (53 percent) higher than the 1.59 percent charged in 1987.2 On average, it costs $24.45 on average to cash a $1,002 Social Security check in 2006.
    - Cost to Cash Paychecks Grows: The cost to cash hand-written paper checks has grown steadily over the past two decades. In 2006, the 4.11 percent charge to cash a paper payroll check was 75.6 percent higher than the 2.34 percent charged in 1997 and 152.7 percent higher than the 1.62 percent charged to cash a paycheck in 1987. A blue-collar worker using check cashing outlets to cash their paycheck pays an average $19.66 every week to cash a $478.41 check.
    - Payday Loans at Check Cashing Outlets are Expensive: Two-thirds of check cashers in states that authorize them also make payday loans, cash loans based on the borrower's personal check held for future deposit by the lender. Typical loans are for over $300, due on the borrower's next payday, and cost $15 to $30 per $100 loaned or 390 to 780 percent annual percentage rate. Average payday loans at check cashing outlets were offered with more than 400 percent annual percentage rate. To qualify for a payday loan, a consumer only needs a bank account and a source of income.

10. CFA Survey of Online Payday Loan Websites (Jean Ann Fox and Catherine B. Bourke, Aug 2011)
    - Lenders require electronic access to borrowers' bank accounts. Instead of holding a paper check to secure payment of loans made at payday loan stores, Internet lenders gain authorization to electronically deposit loan proceeds and withdrawn payments directly from borrowers' bank accounts.
    - Borrowers complete online applications and provide Social Security numbers, bank account and bank routing numbers in online applications.
    - Surveyed loan size ranges from $100 to $1500, with payment/s due on the borrower's next payday with loan terms ranging from five to thirty days.
    - Typical cost of a $500 loan is $125 or 652% APR for a two-week loan. Surveyed loan cost ranged from a low of 378% in Kansas to 780% charged by six lenders.
    - The default payment plan for most sites is to pay the finance charge only, with no reduction in loan principal for several paydays. To initiate payment in full, a borrower has to notify the lender days before the due date to request the lender to withdraw the full amount.
    - While some lenders purport to be state-licensed and to comply with state rate caps and loan terms, many online lenders claim choice of law from states with no rate caps or from foreign countries. A growing number of online lenders claim to be exempt from state law enforcement due to tribal sovereign immunity.
    - Online lenders pay up to $110 for referrals of qualified loan applications from lead generators or affiliate marketers and some lenders encourage borrowing by offering discounts on the initial loan. Online lenders that make loans in states where licensed typically also link applicants to lead generators when applications come from states they do not serve.

11. [The Military Lending Act Five Years Later: Impact on Servicemembers, the High-Cost Small Dollar Loan Market, and the Campaign against Predatory Lending] (Jean Ann Fox, May 2012)
    - MLA largely successful in curbing abusive lending as defined by DOD.
    - Restrictive definitions of "consumer credit" in DOD rules left loopholes to be exploited.
    - Problematic credit products not included in covered credit definitions.
    - Bank credit products similar to payday lending excluded by DOD rule.
    - MLA ban on state discrimination against non-resident military borrowers not effective.
    - Enforcement tools need to be updated to uniformly deliver MLA protections.
    - Ban on securing loans with allotments does not apply to all forms of credit.
    - The MLA has had a major impact on the policy debate about predatory small dollar lending and was a major factor in the reversed trend in states legalizing payday loans.

12. [Driven to Disaster: Car-Title Lending and Its Impact on Consumers] (Delvin Davis and Uriah King, CRL; Jean Ann Fox and Tom Feltner, CFA, Feb 2013)
    - Approximately 7,730 car-title lenders operate in at least 21 states costing borrowers \$3.6 billion each year in interest on \$1.6 billion in loans.
    - The average car-title borrower renews their loan eight times, paying \$2,142 in interest for \$951 in credit.
    - Car-title loans' annualized percentage rates (APR) are especially excessive considering the value of the collateral and the relatively low amount of the loan. In our borrower-level data set, the median loan-to-value ratio was 26 percent, yet the APR was 300 percent.
    - One in six borrowers in our data set also faced repossession, with repossession fees averaging half of the borrower's outstanding loan balance.

13. [Wrong Way: Wrecked by Debt – Auto Title Lending in Arizona] (Jean Ann Fox, CFA, and Kelly Griffith, Southwest Center for Economic Integrity, Jan 2016)
    - One hundred companies operated 633 licensed title lender locations in Arizona mid-2015. This is a conservative count since we identified several unlicensed title lenders that have Electronic Lien and Title numbers to access records at the Arizona Motor Vehicle Department or that advertise in Arizona.
    - Arizona has the seventh most concentrated title loan market in the country, with one outlet for every 8,072 adults. The number of title loan outlets grew from just 159 locations for current companies in 2008 to over 630 in 2015 and now exceeds the number of payday lenders that surrendered their licenses in 2010.
    - Mapping of title lender locations in Phoenix and Tucson illustrate that title lenders are concentrated in vulnerable communities and overlap former payday lender outlets.
    - If Arizona is typical of the other 24 states where title lending operates legally, 190,000 to 285,000 Arizona consumers use title loans per year, or 4 to 5.5 percent of adults.
    - If Arizona is similar to Virginia, title lenders take in \$316.5 million in revenue per year.
    - Lenders make both title-secured loans to consumers who own their vehicles free and clear and "registration" loans to borrowers who do not hold clear titles. These loans have many similarities to now-defunct payday loans.
    - Risks to title loan borrowers include repossession of vehicles, deficiency judgments when sale of repossessed property does not cover the amount owed plus costs, and lawsuits when borrowers default and lenders sue instead of repossess vehicles.

- If Arizona repossession rates are similar to those reported by regulators in Virginia, it is likely that 25,320 borrowers lost their vehicles to repossession last year, based on 633 title loan locations in Arizona and 40 repossessions per store. Currently, the AZDFI does not report repossession data.
- Several lenders require borrowers to provide access to their bank accounts as back-up payment, a feature of payday lending.

C. National Consumer Law Center

1. Stopping the Payday Loan Trap: Alternatives that Work, Ones that Don't (Lauren Saunders, Leah Plunkett, Carolyn Carter, June 2010)
    - Several myths surround payday loan alternatives:
        i. *The myth that any alternative that is slightly cheaper than a traditional payday loan is a good alternative.* An affordable alternative must be just that: affordable.
        ii. *The myth that any loan that does not give the lender excessive profits is a responsible loan.* Loans should be judged by their impact on the borrower, not on the lender's bottom line.
        iii. *The myth that a payday loan alternative needs to look like a payday loan.* That claim is a self-serving justification for offering a loan with such a high fee structure and short repayment period that it is unaffordable.
        iv. *The myth that expensive loans must be tolerated because there is demand for them and we should not restrict access to credit.* Harmful forms of credit should be restricted.
    - To be truly affordable and avoid the pitfalls of traditional payday loans, an alternative product must:
        i. Have an annual percentage rate (APR), including fees, of 36% or less;
        ii. Have a term of at least 90 days, or one month per $100 borrowed;
        iii. Require multiple installment payments rather than a single balloon payment;
        iv. Not require that the borrower turn over a post-dated check or electronic access to a bank account.

2. Why 36%?: The History, Use, and Purpose of the 36% Interest Rate Cap (Lauren Saunders, Apr 2013)
    - History behind the 36% usury rate cap, and its impact on loan affordability.
    - Records states that cap payday loans at 36% or less.

3. Big Data A Big Disappointment For Scoring Consumer Credit Risk (Persis Yu and Jillian McLaughlan, March 2014)
    - Conducted survey of data brokers, finding concerning amounts of inaccuracies and incomplete information. This would impact assessments of income and credit based on this data.
    - We should consider big data brokers as subject to regulation under the Fair Credit Reporting Act.
    - Also, regulators should examine how the impacts of big data collection could disproportionately impact groups protected under the Equal Credit Opportunity Act.

4. [Payday Lender Prepaid Cards: Overdraft and Junk Fees Hit Cash-Strapped Families Coming and Going]() (Lauren Saunders, Jul 2015)
    - Payday lender prepaid cards allow payday lenders to take advance authorization to debit the card on the consumer's payday.
    - Payday lender prepaid cards can overdraft and charge overdraft fees.
    - NetSpend made $50 million or more in overdraft fees last year.
    - Payday lender prepaid cards have unusual fees triggered by payday loans. These fees are generally not found on mainstream prepaid cards:
        i. $1 to $14.95 for declined automated clearinghouse (ACH) payments.
        ii. $10 to $25 to stop recurring payments.
        iii. On one card, $4.95 for a successful payday loan payment.

5. [Installment Loans: Will States Protect Borrowers from a New Wave of Predatory Lending?]() (Lauren Saunders, Margot Saunders, Carolyn Carter and Andrew Pizor, Jul 2015)
    - For a $500 closed-end installment loan, with all fees included:
        i. In 19 states and the District of Columbia, the full APR is 16% to 36%,
        ii. 13 states allow interest and fees that can bring the full APR as high as 54%,
        iii. 10 states allow fees that can potentially bring the full APR for a $500 loan up to between 61% and 116%,
        iv. 4 states place no cap on the interest rate except that it cannot be unconscionable–so one-sided that it shocks the conscience, and
        v. 4 states have no rate cap or ban on unconscionability at all.
    - For a $2,000 closed-end installment loan:
        i. 31 states and the District of Columbia cap the full APR at 17% to 36%,
        ii. 6 states allow just a bit more (38% to 41%)
        iii. 2 states allow rates and fees that can bring the full APR as high as 82%,
        iv. 6 states place no cap on the interest rate except that it cannot be unconscionable,
        v. 5 states have no rate cap at all.
    - Of the 44 states whose non-bank lending statutes specifically allow open-end credit:
        i. 14 states fail to cap rates for a $500 cash advance and 16 fail to cap rates for a $2000 advance.
        ii. 14 states have rate caps but do not have unambiguous, airtight caps on the fees that lenders can impose for a $500 cash advance, and 13 fall into this category for a $2000 advance.
        iii. For a $500 cash advance, 7 states cap it between 39% and 54%, 4 cap it at 59% to 89%, and Tennessee caps it at 279%.
        iv. For a $2,000 cash advance, 11 states cap the full APR at 36% or less, 3 states cap it between 39% and 42%, and Tennessee caps it at 279%.

6. [Misaligned Incentives: Why High Rate Installment Lenders Want Borrowers Who Will Default]() (Lauren Saunders, Margot Saunders and Carolyn Carter, Jul 2016)
    - As long as the borrower pays long enough before defaulting, a high-rate installment loan will be profitable. If the borrower makes even half the payments on a longer term high-rate installment loan, the lender may receive sufficient cash flow to recover the amount loaned and another 50% or more, likely more than enough to turn a profit.

- A borrower who defaults later can be a more profitable customer than one who prepays the loan in full too early. Tighter underwriting can lead to borrowers who are able to repay early, generating less revenue than a consumer who struggles for months or years to make payments and then ultimately defaults.
- While the lender may have a successful experience, default causes a cascade of devastating consequences that are likely to plague the consumer for a lifetime.
- After 20 months of payments, less than halfway through the loan, the consumer has paid over $4,331 yet reduced the loan balance by only $391.