SB 365 Expands Predatory Payday Loans

CRL Bill Analysis

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April 6, 2018

SB 365[1] Authorizes Long-Term Predatory Payday and Car Title Loans

In Louisiana, payday and car title lenders drain $251 million in fees each year from the state's residents due to triple-digit interest rate loans.[2] This fee drain is due to the fact that payday and car title lenders' business model is based on repeat reborrowing. In Louisiana, 87% of loans are taken out within 14 days of a previous loan being repaid.[3]

SB 365 expands the state's predatory lending problem by allowing payday and car title lenders to make larger and longer loans and codifies four core features of predatory payday and car title lending**.** If this bill passes, payday and car title lenders will still be able to legally trap Louisiana borrowers in a long-term cycle of debt, but lenders will have the ability to choose how they trap Louisianans – with short-term and/or long-term debt trap products.

As explained here, the impact of SB 395 is a legalized long-term debt trap for borrowers and puts payday lenders first in line for repayment on payday – ahead of other Louisiana businesses whom borrowers otherwise patronize to meet their basic needs, such as rent, groceries, child care, and medical bills. As payday loans increase a borrower's likelihood for bankruptcy, it also means some businesses and creditors may never be repaid at all, while payday lenders will have reaped hundreds of millions of dollars in interest and fees.

Predatory Features of Long-Term Payday Loans	SB 365 Provisions Codifying These Predatory Features
Triple-digit interest rates	SB 365 legalizes interest rates over 160% APR for loans lasting up to 1 year.
Larger loan amount	SB 365 allows lenders to make loans from $500 to $875, on top of the $350 loans already allowed.
No affordability assessment	SB 365 includes no requirements that the loan is affordable in light of a borrower's income and expenses.
Allows lenders to take bank account access or title to people's property, such as cars	SB 365 codifies the use of the post-dated check or electronic access to a borrower's bank account or using the vehicle title as security for the loan.

The bill provisions codifying these abusive features, as well as why the bill's other provisions are ineffective at mitigating these product flaws, are discussed below.

1. SB 365 legalizes triple-digit interest rates for longer-term payday and car title loans.
See § 1374(A), as amended

SB 365 creates a new predatory loan product exclusively for payday and car title lenders to charge annual interest rates over 160%. This bill would not replace the current payday and car title product but add an additional one – a longer and deeper debt trap. The bill would also create a carve out exclusively for businesses licensed as payday lenders from Louisiana's current law on installment lending, even though at least one payday lender already uses that law to make triple-digit interest rate loans.[4]

The annual percentage rate (APR) is an accepted, and legally required standard used to compare cost of credit. The federal Truth in Lending Act (TILA) mandates disclosure of accurate APR for small loan products, including payday loans. The charges authorized by SB 365 means that a ***typical $500 loan lasting 12 months can carry $540 in fees, resulting in 163% APR.***

Specifically, SB 365, as amended, authorizes the following charge on a long-term payday or car title loan: a monthly service charge of 9% of the original loan amount. Below are APRs authorized by SB 365, all of which are far in excess of the state's existing limits for installment loans.

Example 1: $500, 6-month loan

Loan Amount	$500
Fees	$270
Monthly Payment	$128
Total Payback Amount	$770
APR	167%

Example 2: $875, 12-month loan

Loan Amount	$875
Fees	$945
Monthly Payment	$152
Total Payback Amount	$1,820
APR	163%

Under current Louisiana law, such loan terms are illegal. SB 365, however, will codify these abusive practices for a unique subset of lenders (the same ones already allowed to make predatory short-term loans), leaving the state powerless to foster a level playing field for all small loan lenders.

2. SB 365 legalizes larger loan amounts.
See § 1373(A)(2), as amended

SB 365 allows payday and car title lenders to make triple-digit interest rate loans in amounts ranging from $500 to $875, in addition to the $350 loans lenders are already authorized to make. Larger dollar amounts means greater fees for lenders, and a deeper debt trap for borrowers. For example, on a $875 loan lasting 12 months, a lender will collect more in fees than what they lend.

These high fees that are tied to the larger loan amounts are what make the loan payments unaffordable for borrowers, with a significant portion of the borrower's pay check going directly to the payday lender, leaving them with an insufficient amount of money to pay other bills or basic living expenses. Even in a state such as Colorado that limits the size of long-term payday loans to $500 with rates averaging 129% APR, there is significant evidence of borrower distress, as nearly one in four borrowers defaults on the payday loans.[5]

3. SB 365 contains no assessment of affordability.

SB 365 authorizes payday and car title lenders to make loans that last from 3 months to 12 months, in addition to the short-term predatory loan product already allowed in the state. Long-term payday and car title loans are no improvement over short-term loans – it is the same game with a different name. Despite allowing lenders to make triple-digit interest rate loans that take access to a borrower's bank account for up to a year, the bill provides no requirements that the lenders assess a borrower's ability to repay in light of income and expenses.

The high rates of default for high-cost installment loans show clearly that the loans are unaffordable. One online lender that offers high-cost installment loans, Elevate, reported charge-off debt amounting to 52% of their domestic revenues in both 2016 and 2017.[6] Repeat borrowing is another indicator of the debt trap business model. The Colorado Attorney General's Consumer Credit Office found that customers of long-term payday loans spend up to 194 days of the year in debt, and that almost one-quarter of loans defaulted in 2016.[7] Similarly, data from the CFPB show that 32% of car title installment loans and 20% of storefront payday installment loans end in default.[8] These defaults create devastating consequences for borrowers, such as bank penalty fees, nonsufficient fund fees (NSF) by the payday lenders, marred credit scores, and abusive debt collection, while lenders have a business model that profits even when these loans go bad.

4. SB 365 allows direct access to a borrower's bank account or property, including cars.
See § 1373(B)

Payday lenders usually require loans to be repaid through the use of a post-dated check or authorization to electronically debit a bank account as security for the loans, an abusive feature of payday loans. SB 365 permits such bank account access. Direct access to a borrower's checking account essentially gives the payday lender an automatic claim to the borrower's future income. This feature forces a borrower to repay the payday loan first before all other debts and basic living expenses. Thus, payday lenders stand ahead of borrowers' other obligations they may have to other Louisiana businesses, such as rent, medical bills, or utilities.

SB 365 also allows lenders to take a borrower's car title or other personal property as collateral for the loan. These additional forms of security will allow lenders to coerce repayment or to continue to trap borrowers in an unaffordable cycle of debt, even in the face of financial difficulties in repaying the loan.

Research suggests that direct access to a borrower's bank account may actually increase involuntary bank fees. When a borrower eventually defaults on the payday loan–after paying hundreds of dollars in fees and interest that the payday lender never applies to reduce the loan principal–she becomes subject to overdraft fees charged by the banks *and* the insufficient fund fees charged by the payday lender.

The CFPB 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 as NSF or overdraft fee.[9] These borrowers paid an average of $185 in such fees, while 10% paid at least $432.[10] It further found that 36% of borrowers with a bounced payday payment later had their checking accounts closed involuntarily by the bank.[11] The CFPB notes that other borrowers close their accounts themselves as it seems the only way to stop the payday lender's collection attempts. Moreover, a report from Harvard Business School researchers finds that payday lending can increase the odds that households will repeatedly overdraft and ultimately have their banks close their checking accounts.[12]

Similarly, car title lenders use the threat of repossession to ensure that borrowers repay their loans. Repossession poses a real threat to employment and causes additional fees to be added to the balance of the loan. Paying back the loan is the top financial priority of borrowers, as the consequences of not doing so can be immediate and severe. Repossession is not an infrequent occurrence; for example, in Virginia, a state that allows long-term car title loans, lenders seized nearly 20,000 cars in a single year.[13]

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. On nearly a third (32%) of these loans, the principal and interest were not 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.[14]

SB 365 Will Not Stop the Harms Caused by Long-Term Payday Loans

Attempting to disguise the predatory terms of the products it seeks to legalize, SB 365 proposes a number of provisions typically touted as "best practices." However, the so-called borrower protections included in SB 365 have failed to protect borrowers in every state they have been tried. Below is a detailed explanation, but in sum, they are ineffective because they do not address any of the core abusive aspects of the payday product as previously described.

- <u>Monthly payment amount limits based on borrower's gross monthly income</u> *§1373(A)(4)*. SB 365 allows lenders to make long-term loans for which the payments account for a significant portion – 20% – of a borrower's gross monthly income.

  This provision does nothing to actually ensure that monthly payments are affordable. Most importantly, it fails to account for the borrower's other obligations, like rent or mortgage payments, car payments, medical bills, or other loans. By not taking these other obligations into account, SB 365 merely adds another trap to keep borrowers deeply in debt.

Data from the CPFB show that for 12-month, fully amortizing payday installment loans, over 60% default with the payments account for 15% to 20% of a borrower's monthly income. The default rate is even as high as 40% when the payment accounts for 5% of a borrower's monthly income.[15]

- Limit on the number of outstanding loans *§ 1374(B)(1)*. SB 365 allows borrowers to enter up to two loans consecutively, with the second loan being unsecured. Around the country, however, these types of limitations are notorious for loopholes.

  Because of the length of the loans, a lender could presumably follow the law to the letter while still keeping the borrower in debt for two full years. One $875 loan lasting 12 months could be immediately followed by a $875 loan lasting another 12 months. In this scenario, the borrower would pay back more than the money they were lent, despite the fact that the lender would be repaid by the sixth month of each loan.

  Finally, SB 365 creates a new loan in addition to those already marketed in Louisiana. There is nothing to prevent lenders from loaning borrowers both an installment loan lasting three months to one year and traditional payday or car title loans. The limit on outstanding loans is not a limit at all. It is a loophole, plain and simple.

- Extended repayment plans *§ 1374(B)(2)(a)*. SB 365 gives the borrower the right to an extended repayment plan, at no additional cost to the borrower. These repayment plans are often promoted by the payday lending industry as an alternative to real reform. However, data from states that offer these plans show that consumers rarely take advantage of them. Florida provides a recent example. In 2016, fewer than one half of one percent of borrowers were placed into the repayment plans offered by payday lenders.[16] In Louisiana, the extended repayment plan is similarly ineffective at stopping the payday and car title loan debt trap, as evidenced by the fact that the typical payday loan borrower is stuck in 10 loans per year.

  The repayment plan itself could become another debt trap, because there is nothing in the plan to require that a borrower is near the end of their loan term when moving into the repayment plan. Therefore, a borrower in a six-month payday loan could be placed in the "extended" repayment at month two – giving them just 60 days to pay in full a loan that had 120 days left to pay. That's not a payment plan – it's an acceleration.

  Even if long-term payday loans borrowers were to be placed into the proper payment plan, however, the proposed four payments in 60 days is hardly sufficient to give a borrower the time to recover from the financial shock of a high cost loan. Especially considering a borrower's other financial obligations – which are not taken into account when reviewing the affordability of the loan – it is unlikely that an additional 60 days will be sufficient to help a borrower recover financially.

- One-month "cooling off" period *§ 1374(B)(1)*. SB 365 allows lenders to loan a borrower one secured or unsecured loan, followed by one consecutive unsecured loan, then requires a "cooling off" period before the next payday loan can be made.

This provision is a sham. There is nothing to stop a lender from loaning a borrower a payday or car title loan that currently exist in Louisiana during the 30-day window. Even if it was a true 30-day break, it would not be a meaningful protection against the harms of the debt trap. The 30-day window is not even triggered until a borrower is sunk into two consecutive loans at triple-digit interest. The 30-day window is not enough time to recover from the financial devastation of two unaffordable triple-digit interest rate loans.

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. 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.[17] In addition, data from other states show that lenders make new loans as soon as the cooling off windows expire.[18]

Data from around the country show that many payday loan borrowers become trapped in this cycle of borrowing and reborrowing. In Florida, for example, 83% of borrowers have seven or more loans a year – despite the industry's claims that Florida has a model law for payday consumers.[19] Indeed, this is by design. In 2007, the then-CEO of Cash America admitted "the theory in the [payday loan] business is you've got to get the customer in, work to turn him into a repetitive customer, long- term customer, because that's really where the profitability is."[20]

- Database *Amendment No. 10, to be inserted at §1374 (B)(1).* Amendment 10 to SB 365 proposes to enforce these provisions via a third party, private database. Databases do not stop the debt trap, both because the provisions of the law itself are ineffective and because database manipulation is a real and proven tactic of payday lenders.

  A database is only as effective as the provisions it is intended to enforce and, as discussed above, the consumer protection provisions contemplated by SB 365 do very little to actually keep lenders from trapping borrowers in debt. For example, in Florida, which has a database, 83% of payday loans go to borrowers stuck in seven or more loans a year, and this has been true every year for more than a decade.[21]

  Further, an investigation in Kentucky found that payday lenders often manipulate that state's database, created in 2010, to circumvent the law. The investigation found that clerks at Cash Express, a proponent of SB 365, "type the wrong Social Security number or other inaccurate personal information about their customers into a statewide payday loan database, or they wrongly report unpaid loans as 'closed' in the database, all of which lets customers borrow more money than state law permits."[22]

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[1] SB 365 was amended in the Senate Committee on Commerce, Consumer Protection and International Affairs on April 4, 2018. The bill passed that committee on the same day. This analysis reflects the amended version of the bill.
[2] Diane Standaert and Delvin Davis, "Payday and Car Title Lenders Drain $8 Billion in Fees Every Year," Center for Responsible Lending (2017), http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_statebystate_fee_drain_may2016_0.pdf.

[3] Consumer Financial Protection Bureau, "Supplemental findings on payday, payday installment, and vehicle title loans, and deposit advance products" (2016) p. 108, https://files.consumerfinance.gov/f/documents/Supplemental_Report_060116.pdf.
[4] S.B. 365, § 1372(3) (2017) ("'Licensee' means any person who offers installment loans and is licensed pursuant to Chapter 2-A of Title 9 of the Louisiana Revised Statutes of 1950, comprised of R.S. 9:3578.1 through 3578.8."). ACE Cash Express makes loans from $400 to $700 that last 62 to 70 days with APRs over 150% under Louisiana's current installment loan law. *See* https://media.acecash.com/~/media/Files/Products/Installment/Store/Rates/LA_FeeSchedule.ashx.
[5] Ellen Harnick and Delvin Davis, "Payday Lenders Continue to Put Coloradoans into High-Cost Debt" (2018), http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-colorado-payday-highcost-feb2018_0.pdf.
[6] Elevate Credit, Inc., 10-K at 39 (filed March 9, 2018), https://www.sec.gov/Archives/edgar/data/1651094/000165109418000014/elevate10-kx2017.htm.
[7] Ellen Harnick and Delvin Davis, "Payday Lenders Continue to Put Coloradoans into High-Cost Debt" (2018), http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-colorado-payday-highcost-feb2018_0.pdf.
[8] Consumer Financial Protection Bureau, "Supplemental findings on payday, payday installment, and vehicle title loans, and deposit advance products" (2016) p. 22, https://files.consumerfinance.gov/f/documents/Supplemental_Report_060116.pdf.
[9] 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, Center for Responsible Lending et al. (2016), p. 20, http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_payday_comment_oct2016.pdf.
[10] Id.
[11] Id.
[12] Researchers from Harvard Business School analyzed involuntary bank account closures, which usually result from an account holder bouncing checks or overdrawing an account too many times. Using national data, the study found that payday loans are associated with an increase in closed bank accounts due to multiple overdrafts. Dennis Campbell, et al., *Bouncing Out of the Banking System: An Empirical Analysis of Involuntary Bank Account Closures* (Dec. 3, 2008), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1335873.
[13] Michael Pope, "As repossessions pile up, critics of car-title lenders call for change," *WAMU 88.5* (2015), https://wamu.org/story/15/10/08/as_repossessions_pile_up_critics_of_car_title_lenders_call_for_change/.
[14] 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, Center for Responsible Lending et al. (2016), p. 72, http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_payday_comment_oct2016.pdf.
[15] Consumer Financial Protection Bureau, "Supplemental findings on payday, payday installment, and vehicle title loans, and deposit advance products" ((2016) p. 25, https://files.consumerfinance.gov/f/documents/Supplemental_Report_060116.pdf.
[16] Brandon Coleman and Delvin Davis, "Perfect Storm: Payday Lenders Harm Florida Consumers Despite State Law" Center for Responsible Lending (2016), http://responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_perfect_storm_florida_mar2016_0.pdf.
[17] 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, Center for Responsible Lending et al. (2016) p. 13 http://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_payday_comment_oct2016.pdf.
[18] Leslie Parrish and Uriah King, "Phantom Demand: Short-term due date generates need for repeat payday loans, accounting for 76% of total volume" (2009), http://www.responsiblelending.org/payday-lending/research-analysis/phantom-demand-final.pdf.
[19] Brandon Coleman and Delvin Davis, "Perfect Storm: Payday Lenders Harm Florida Consumers Despite State Law" Center for Responsible Lending (2016), http://responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_perfect_storm_florida_mar2016_0.pdf.
[20] Id.
[21] Id.
[22] John Cheves, "Payday lenders cited hundreds of times, face few consequences in Kentucky*" Lexington Herald Leader* (2016) http://www.kentucky.com/news/politics-government/article88451342.html.