

222 South First Street, Suite 305  
Louisville, KY 40202

October 5, 2016

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

Re: Comments on proposed rulemaking on payday, vehicle title, and certain high-cost installment loans

Docket number CFPB-2016-0025 or RIN 3170-AA40

Dear Director Cordray,

We are groups that are concerned about payday lending in Kentucky. Many of us have worked together to end the payday loan debt trap by advocating for state legislative proposals to limit the interest rate on payday loans to 36% APR. We support the Consumer Financial Protection Bureau's (CFPB) efforts to end the payday loan debt trap and ensure that credit options are safe and affordable.

We are filing this comment in response to the CFPB's proposed rule on payday, vehicle title, and certain high cost installment loans. Thank you for the opportunity to comment on this important subject. The rule is a critical first step in stopping the harms of unaffordable loans, but the rule must be strengthened to ensure it stops the debt trap once and for all.

The signee groups to this letter are diverse. They include advocates for seniors and the homeless, faith based bodies, legal aid, domestic violence and other service providers, as well as groups engaged in community and economic development. We have in common our work to improve the lives of Kentucky residents across a broad spectrum of issues. All of us have seen and experienced the pain and financial harm that is caused every day by payday lending in Kentucky.

### **Payday Lending in Kentucky**

In Kentucky, the debt trap payday loans cause is left largely unchecked. On a \$300, two-week payday loan, payday lenders typically charge 460% APR.<sup>1</sup> Annually, these high cost lenders drain over \$117 million in payday fees, a significant loss both to borrowers

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<sup>1</sup> Center for Responsible Lending, Map of U.S. Payday Loan Interest Rates, 2016, <http://www.responsiblelending.org/research-publication/map-us-payday-interest-rates>

and to the overall state economy.<sup>2</sup> A large proportion of borrowers are continuously caught up in the payday debt trap:

- 78% of loans are reborrowed on the same day that a previous loan is repaid
- 90% are reborrowed within 60 days of repayment of the previous loan.<sup>3</sup>

Fully 95% of loans in 2015 were generated by borrowers taking out 4 or more loans. The average borrower in Kentucky takes out 10.6 loans in a year. In 2015, nearly 6,100 Kentuckians were trapped in 30 or more payday loans.

Because there is no cooling-off period, and borrowers can take out two loans at a time, an individual could actually take out 52 loans in one year.

The current state of affairs is particularly detrimental to Kentucky's 303,167 veterans and its communities of color, populations which the payday lenders target and exploit. Payday lenders' ability to seize money directly out of borrowers' bank accounts means that people are left with little choice but to reborrow, becoming more deeply mired in a cycle of debt. The CFPB's rule would help these borrowers by beginning to rein in predatory lending practices.

While Kentucky enacted a database in 2010 to enforce the current limit of two loans up to \$500 at a time, the database does not limit the number of loans over time. The debt trap continues. Further, in recent years, the payday industry has been promoting a high cost unsecured installment loan product that could keep individuals in debt for 1 to 2 years at 276% interest.

It appears unlikely that the Kentucky Department for Financial Institutions, the state regulatory agency, will step up its regulation and enforcement of the industry. DFI has the authority to fine payday lenders up to \$5,000 per day for each violation, but lenders pay an average of only \$1,380 per violation. DFI can also suspend or revoke a license, but it has only done this a handful of times, never to a major lender. In essence, DFI penalties are a modest cost of doing business that the industry is willing to pay to continue forcing borrowers into the debt trap.

### **Analysis of the CFPB Payday Lending Rule**

The core principle of the CFPB's proposal is the right approach – requiring lenders to ensure that a loan is affordable without having to re-borrow or default on other expenses. This approach is critically important to stopping the debt trap, and we strongly support it. The ability to repay standard, which considers a potential borrower's income and

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<sup>2</sup> Center for Responsible Lending, "Payday and Car Title Lenders Drain \$8 Billion in Fees Every Year", 2016, <http://www.responsiblelending.org/research-publication/payday-and-car-title-lenders-drain-8-billion-fees-every-year>

<sup>3</sup> Table 21, page 108, CFPB SUPPLEMENTAL FINDINGS ON PAYDAY, PAYDAY INSTALLMENT, AND VEHICLE TITLE LOANS, AND DEPOSIT ADVANCE PRODUCTS, [http://files.consumerfinance.gov/f/documents/Supplemental\\_Report\\_060116.pdf](http://files.consumerfinance.gov/f/documents/Supplemental_Report_060116.pdf)

expenses, is a long-standing principle of responsible lending that is ignored by payday lenders and other abusive small dollar lenders.

We feel strongly that the ability to repay requirement should apply to *all* short-term and long-term high cost loans. There is no valid reason why high cost lenders should get a pass on such a critical responsible lending norm.

We believe there are weaknesses in the proposed ability to repay test that need to be remedied. The proposal does not go far enough to ensure that borrowers will be able to pay their expenses and have enough money to live on after making the loan payment. The rule should not allow a lender to simply forecast a borrower's living expenses based on a percent of income or other factors. Lenders should be required to review a borrower's basic living expenses and avoid over-reliance on back-end measures like default and reborrowing rates. Nor should the ability to repay be determined by the lender's rates of delinquency, default and reborrowing.

The rule allows lenders to make some loans without determining ability to repay if the loans meet certain alternative requirements designed to limit the length of indebtedness (referred to here as exception loans). We feel strongly that both the ability to repay standard and the limits on the length of indebtedness should apply to all lenders.

In any case, some of the exception rules are too generous to the lender. In particular, allowing up to 6 short-term loans without any ability to repay test is too many. The rules should also prevent unaffordable short-term debt from becoming long-term debt. In particular, the CFPB rule should adopt the FDIC standard of 90 days maximum indebtedness per year to *all* short-term loans, not just exception loans.

Also, we hope that the CFPB will change the cooling off period back to 60 days, as it was in the original draft proposal. Still, we acknowledge that the cooling off periods in the rule could significantly reduce payday lending volume and the debt trap in Kentucky. In particular, creating a limit of 3 short term loans, each one for a declining amount, followed by a mandatory 30 day cooling off period, would break the cycle of debt, at least for a time.

With regard to longer-term debt, we are encouraged by the models set out in the rule for long term loans that may be excepted from the ability to repay requirement. In particular, the NCUA's payday alternative loan is a good model which we would like to encourage lenders to use, as it would limit interest to 28% plus a small application fee up to \$20. We also support excluding long-term loans with fee inclusive interest up to 36% interest from the ability to repay requirements, although the permitted \$50 origination fee is too high. The \$20 fee permitted in the NCUA model should apply to these loans as well.

We encourage the CFPB to include in the rule loans that are not secured by an individual's bank account or car. In Kentucky, the proposed flex loan from last year would have created an open-ended unsecured loan with interest up to 276%. That type of

loan, if passed, would be totally exempt from the CFPB rule as proposed. *All* high cost loans, whether secured or unsecured, should be covered by the rule.

In addition, we encourage the CFPB to include within the scope of the rule loans that are secured later than 72 hours after they are finalized. At a minimum, *all* high-cost loans secured by a bank account or a vehicle should be covered by the rule. Exceptions open a large loophole for unaffordable loans that, like payday loans, force individuals to reborrow to avoid repossession or garnishment.

The payment collection practices in the rule are very positive. It would be very helpful to consumers to have a few days' notice before a lender attempts to collect from a bank account, in order to avoid overdraft and insufficient fee charges. We also appreciate the requirement that the lender obtain a new authorization from the consumer after two failed attempts to collect from the borrower's bank account.

## **Conclusion**

We applaud the CFPB for studying the serious issue of the debt trap caused by high cost lending, and appreciate the time and effort that went into creating this rule. We are very pleased that the rule adopts the basic premise and requirement that loans be affordable and that the lender ensure that the borrower has the ability to repay. While the rule needs strengthening, even in its current form it has the potential to significantly reduce the debt trap in Kentucky. Even if lenders mostly bypass the ability to repay rules for the alternative requirements, the limitations on the number of loans or days of indebtedness, the cooling off periods, the exemption for loans below 36% and added protections for borrowers' bank accounts are positive steps.

While there are many positive elements to the rule, unless the CFPB strengthens it, the rule will fall short of its stated purpose of ending the debt trap. This could end up making things worse for consumers by implicitly endorsing lending practices that lead to the debt trap.

To recap, the rule needs to be strengthened by requiring lenders to determine ability to repay in *all* loans. The lender should be required to review the borrower's actual income and expenses. The rule should protect against loan flipping by requiring a 60 day cooling off period between all short-term loans. The FDIC standard of 90 days indebtedness in any 12 month period should apply to all loans. Only long-term loans that limit interest to 36% should be exempted from the rule. Unsecured high cost installment loans should be covered by the rule.

Thank you for this opportunity to comment. We appreciate the work that you have done so far to protect consumers and hope that this rule will become as strong as possible in order to truly end the debt trap. For further information on these comments, please contact Anne Marie Regan at Kentucky Equal Justice Center. Ms. Regan can be reached at 502-333-6012 or at [amregan@kyequaljustice.org](mailto:amregan@kyequaljustice.org).

Sincerely,

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