SOUTH CAROLINA appleseed LEGAL JUSTICE CENTER

October 1, 2016

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

Re: South Carolina Appleseed Legal 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,

South Carolina Appleseed files 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 submit comments on this important subject. The rule is a critical step in stopping the harms of unaffordable loans, but it must be strengthened to ensure it stops the debt trap once and for all.

South Carolina Appleseed has advocated for low income consumers since 1979. SC Appleseed was a connected to the state's Legal Services programs until 1996 when Congress cut funding and placed restrictions on the types of work that the organization could do, becoming a separate organization that year. In 1998, we began an affiliation with the Appleseed Foundation and officially became the South Carolina Appleseed Legal Justice Center. We have a staff of 4 full time attorneys as well as organizers and administrative staff. Our attorneys provide litigation, advocacy, mentoring and training for the low income community. Our goal is to influence policymakers to ensure the law is fair, to educate the public and their advocates about the law, and to assist attorneys in bringing systemic litigation where the law is unfair.

The CFPB has before it this unique opportunity, and indeed obligation, to bring meaningful reform to the marketplace. This reform has been thwarted numerous times in our state due to heavy influence peddling by the industry. We urge that any rule addressing high-cost payday, car title or installment loans, accomplish the following: 1). Require the lender to determine the borrower's ability to repay the loan, including consideration of income and expenses; 2). Not sanction any series of repeat loans or provide any safe harbor of poorly underwritten loans; 3). Establish an outer limit on length of indebtedness that is at least as short as the FDIC's 2005 guidelines – 90 days in a twelve-month period. 4). Restrict lenders from requiring a post-dated check or electronic access to a borrower's checking account as a condition of extending credit. The above principles are the foundation for an effective rule to end the debt trap. The recent release of Department of Defense proposed rules to update the Military Lending Act serves as a powerful reminder that rules need to be comprehensive to block evasions. All consumers deserve protection. The changes we are urging put predatory lenders on the same footing as other lenders, requiring them to play by the rules and make fair loans. We greatly appreciate your attention

South Carolina has been a deregulated state since 1982, meaning that a lender can charge any interest rate it desires as long as it files the rate with the South Carolina Department of Consumer Affairs and posts it "conspicuously" in its place of business. This has allowed for high interest rates and abusive lending since that time. It was not unusual to see triple digit interest rates.

As a deregulated state, South Carolina's consumers, particularly low income and people of color have been at the mercy of both abusive and high cost lending practices since 1982. In 1995 the state legislature was offended that consumers could pay as much as 100% interest for small finance loans, yet turn around and sanction 391% for payday loans in 1999 and unlimited interest for auto title loans in 2004. It is not unusual for auto title loans that have a 300% APR. Small loans from finance companies regularly have interest rates upward of 85% APR. This is the statutory rate permitted under South Carolina law.

In 1995 the law was amended to limit, not abolish, abusive refinancing of these small loans in an effort to limit the incentives for automatic refinancing of loans. It also limited the interest rates to a statutory rate permitted under the state Consumer Finance act to all loans that were $600 or less. Prior to this many lenders getting licensed under the state Consumer Protection Code so they could continue to charge triple digit interest on small consumer loans.

In 1995 South Carolina also started to see the emergence of payday lending. This industry was operating unregulated until 1999. In the legislation passed in 1999 lenders were limited to advancing up to $300.00, plus the lender's fee of 15%. During these debates consumers' attempted to limit the rate to 12% but this was changed last minute due to industry pressure. The amount that can be borrowed has been increased to $550.00 in February 1, 2010. The industry tried to legitimize their lending model by rebranding it as "pay day."

When this industry first began to emerge, businesses providing pay day services thrived by charging exorbitant fees and allowing borrowers to extend, or "flip," the original loan if they still did not have the money to cover the entire check in exchange for paying *another* fee. For example, the borrower could pay $20 every two weeks for a year to avoid having check deposited. This would result in paying $520 in fees for "borrowing" $100.00. In an effort to protect the consumer from this perpetuation of debt, the Legislature in 1999 passed the South Carolina Deferred Presentment Act, which regulates payday lenders.

Under this Act, businesses making payday loans must obtain and post a license from the State Board of Financial Institutions for each of its locations. To receive a license, the business must, among other things, have a minimum net worth of $25,000 for each location it wishes to operate. As of February 1, 2010 a company wishing to engage in this business with a consumer who resides in South Carolina, whether or not the company has a location in the state must be licensed by the Board of Financial Institutions. This is intended to make internet lending illegal for those who are not licensed and complying with the limitations on number of and amount of loans.

Unfortunately, lenders were very clever in their effort to keep consumers in the cycle of debt of payday loans and consumers began running into difficulty with pay day when they enter into multiple contracts. What often happened was the consumer entered into a contract with a second company to pay off an existing check. Then, the consumer enters into a second contract with the original company in order to maintain cash flow. Although this is a form of "flipping," since the same business is not used to pay off the original check, it does not violate the letter of the law. It was not unusual to encounter consumers indebted to more than ten companies at one time and who pay over $500 every two weeks in fees. When consumers brought this to the state regulator it refused to find that this practice violated the intent of the act, despite legislators stating it was always the legislature's intent to limit loans to one at a time.

In 2009, following five years of debate and millions of dollars spent by the payday loan industry, the legislature amended the pay day statutes. While the initial effort included an attempt to mirror federal laws that protect military borrowers, this ultimately did not pass. While the new South Carolina law, effective February 1, 2010, did not cap the interest rate, it provided some additional protections for consumers to limit the number or loans that can be entered into at any given time to just one per consumer.

To enforce the provision mandating that a consumer shall not have more than one loan at a time from any lender, the legislature has authorized the enactment of a database and requires that every lender shall:

1) Check database before entering into a loan with a consumer;
2) Note in the database when it enters into a loan with a consumer and then when the loan is paid in full;
3) Note if the consumer has entered into an Extended Payment Plan (EPP) with the lender and when the loan is paid through the EPP;
4) Not make a loan to a consumer that has an outstanding payday loan or EPP with any lender.
5) Not make a loan to a consumer on the same day that she has paid her loan off in full and once the consumer has made seven consecutive loans the lender must wait two full business days.

6) The consumer can be charged one half of the actual fee charged by the data base provider, but the consumer cannot be charged more than $.50, and only when the loan is consummated.

While the new law finally limited the number of loans that a consumer may have to one at a time, the amount that can be borrowed was increased to $550.00. The lender must give the consumer the right to rescind the loan, at no cost, on or before the close of the next business day. A borrower may re-borrow one business day after she pays off her loan for the first seven loans and then must wait two business days for the eighth and subsequent loans. This provides absolutely no protection from flipping loans and South Carolina data proves this. In 2015 64,450 of 112, 058 borrowers or 57% took out 6 or more loans in that year. In fact, less than 25% of all borrowers or 25,846 of those who took out payday loans had two or less loans in that year. South Carolina data demonstrates that most borrowers cannot afford these loans and are serial borrowers in an effort to prevent default.

Consumers in South Carolina are allowed to apply for an Extended Payment Plan (EPP), and while it is required to be provided, it falls on the consumer to request one before the due date, which is very rare. One may apply for an EPP once every twelve months. Sadly, the EPP does not normally allow someone to break the debt cycle for it requires that the consumer repay the debt in full over the span of four equal payments. In the case of a $550 loan, that would be four payments of $158.13. This plan is written in a way that pushes consumers to instead pay the loan in full, then return the next day to take out another loan. As part of the changes in February 1, 2010, there was an increase in the licensing fee with the increase going to the SC Attorney General's office as funding for prosecuting violators. SC Appleseed has taken violations to this office and been informed that it cannot prosecute violations and it has refused to help consumers. For any further changes in payday lending laws in South Carolina, a detailed report on payday lending activities must be presented to both chambers of the legislature to provide information as to trends in the industry based on information from the data collected.

Auto Title lenders are also abundant in our state This industry lures consumers with promises of "no credit checks," "quick cash," and "bad credit, no problem." However, the solution is only short-term, and the long-term effects are often devastating. Consumers end up facing enormous interest rates and many times losing their cars when they cannot make the loan payments. Title lenders target and take advantage of low-income individuals, military members, and the elderly population. They have been described as legal loan sharks.

Auto title lenders have proliferated in the state since the late 1990s. When they started they made loans that were usually no longer than thirty days. The loan was written with an interest rate for that time period. For example, the loan will show a 25% interest rate, but if this rate is annualized it is actually 300%. By way of example, a credit card debt, which also accrues monthly, may show a rate of 1.5% monthly, but its actual annual rate is about 21%. When the loan came due, the lender will accept the interest payment and allow the debt to be rolled over for another month. On a $600.00 loan, the interest is approximately $150.00. This means at the end of the thirty days the consumer will owe $750.00. Since in most case the consumer will not be in a position to pay the loan in full, the interest will begin to accrue all over again at this high rate.

Since 1995, lenders can only charge obscenely high rates, versus very high rates, on loans over $600.00. This is because loans under $600 are limited to the rates allowed under Title 34, usually averaging 70-90%. Therefore, in South Carolina you will never see an Auto Title Loan under $601.00. In fact, auto title lenders often refer to themselves as 601 lenders, telling borrowers it is illegal for them to make a loan under that amount. What they mean is they cannot charge you 300% APR if they make a loan for an amount under $601.

Up until 2004, there were no laws restricting or addressing these Auto Title loans. This meant that an auto title lender could flip this type of loan indefinitely. A $601.00 loan could earn an auto title lender literally thousands of dollars in interest, and the car could still be repossessed if the consumer eventually got behind. The legislature has attempted to address these abuses by enacting a new law, Short-Term Vehicle Secured Loans. The statute defines a short-term vehicle secured loan as a non-purchase money consumer loan that is secured by a motor vehicle and has an original repayment term of less than 120 days but excludes loans made by supervised financial organizations. The law provides that the original period of the loan has to be at least one month in duration. The lender may allow the loan to be renewed no more than six additional periods. Each renewal period has to be the same length as the original period, and the total number of days renewed cannot exceed 240. In addition, the loan may not accrue interest after the maturity of the sixth renewal period. After the maturity of the final renewal period, the borrower may repay the remaining principal, without additional interest, in six equal monthly installments." A renewal is an extension of a short-term vehicle secured loan for an additional period without changes to the terms of the loan. The only type of change allowed is a reduction in the principal. In addition, the accrued interest cannot be capitalized or added to the principal of loan at the time of renewal Finally, fees cannot be charged with the exception of a lien recording fee in the exact amount of the governmental entity's charge.

Like payday loans short-term title lenders often target low-income individuals who do not have the resources to repay an auto title loan. Before making a short-term title loan, the lender has to form a good faith belief that the borrower has the ability to repay the loan. In forming this good faith belief, the lender should consider the borrower's, and if applicable the co-borrower's: employment; monthly income; and other monthly expenses.

The lender is considered to be in compliance with this subsection if he obtains a signed statement from the borrower that the information provided about employment, income, and expenses is correct. The borrower must express a belief that given that information, he has the ability to repay the loan. This statement must be on a form separate from the loan agreement. Short-term title lenders may not make loans in a principal amount greater than the fair market retail value of the motor vehicle securing the loan. With the exception of borrower fraud, the lender's sole remedy if the borrower defaults is to seek possession and sale of the vehicle. The lender may not pursue the borrower personally in an action for repayment of the loan. Finally, the lender may not advertise or offer a rate of interest that is lower in the original period if the interest rate increases in later renewals. For example, the lender may not advertise a 10% interest rate, if that rate increases to 22% in the renewal periods.

What is the result in South Carolina's effort to limit auto title lending? To circumvent the law passed in 2003, title lenders no longer make short term loans but operate under South Carolina law as any other consumer lender, making loans for 12 months or more, disclosing an APR usually around 300%, lending to people who often cannot afford the payment and repossessing the car due to lack of payment. It is business as usual. They have fought all efforts to further limit their business or allow for tracking of their particular form of loans. All data collected concerning consumer lending mixes auto title lending with all other supervised loans. They are well aware of the danger of allowing any disclosure of data about their industry.

South Carolina Appleseed has worked to eliminate Payday and title lending since 1998. It was the intent of all that oppose these lenders to limit their reach and to protect consumers. Sadly, this did not occur. Payday lenders were able to circumvent the laws of 1999 to grow their reach and industry. In fact, before the 2010 changes more than 4.5 million loans were made each year with charges reaching more than $150 million. To put that in context there were only 4.7 million people living in the state at that time.

Changes to the law were needed and an alliance was formed with SC Appleseed, AARP-SC, SC Fair Share and the South Carolina Baptist Convention to reign in the multiple loans and constant flipping that was occurring around the state. We were met with huge opposition by the industry. Numerous high powered lobbyists were engaged against us including a former state Senator who had spent 20 years in that body. Their reach was across party lines. Unaffiliated pastors were brought in to speak, claiming to represent the faith community although they had no pulpit. The industry would get individuals who went to their offices trying to pay their bills on the phone with their state Senators to say how much they loved the industry. When a hearing was held they would bus in employees to tell elected officials that they were worried about losing their job if any changes were made to the law. They knew no shame.

The experience with Auto Title Lenders was similar. The law for this industry was changed in 2004. The industry knew that there was a target on their lending model. To keep themselves from being exposed they immersed themselves in the mortgage lending legislative debate. They understood that if they were not being examined alone they would be less vulnerable to any real change. The industry proposed the current law for short term auto lending. They also knew they would change their model of how they made these loans as soon as the law was passed. Later efforts to change the industry have been unproductive. Both industries make donations to candidates and nonprofits in an effort to keep their business model alive.

The law that went into effect in 2010 has caused a decline in the number of payday loans in South Carolina. We have gone from 4.5 million in 2009 to 876,985 in 2015. It should be noted that the amount an individual can borrow for a loan increased from $300 to $550 a loan. The number of loans went down by 75% but the amount of fees charged, $53.9 million, only represents 64% decline in charges. We are unable to track title lending in the state as they hold a supervised license under the Consumer Protection Code and the loans for all supervised lenders are reported in aggregate. Efforts to require Title lenders to report separately from other supervised lenders has failed due to intensive lobbying by the industry. Even with the changes to the laws governing predatory lending, many consumers continued to be targeted and become trapped in endless cycles of debt due to unaffordable loans.

SC Appleseed continuously hears from consumers who are suffering from this industry's abusive lending practices. Many are elderly and/ or people of color. One such family, the Browns of Great Falls, South Carolina contacted SC Appleseed about a problem with a pay day loan. This elderly couple only receive for retirement and Social Security for a combined income of $1039 a month along with $170 SNAP, totaling $1210 a month for living expenses. With this limited income, the Browns are paying a mortgage payment of $461 a month on top of a $600 power bill, a $440 car payment, and a cable bill at $80 which totals $1581 a month. This does not count other family expenses. This creates a deficit of roughly $371 a month which is only exacerbated whenever the Brown's take out a loan to try and cover the expenses. The Brown's went to Advance America, a company that knew of their financial situation yet and still made them multiply loans over the course of three months that totaled $978.30. Not only did Advance America make loans that never should have been approved in the first place, but proceeded to call and harass the Brown family as they got behind. First with calls trying to collect debts, then once some of the debts were paid, calls attempting to get the Brown family back in to take out another loan. The Brown's inability to pay should have prevented them from being able to take out these loans. Instead, the Browns became trapped in the debt cycle because of an inability to repay. At one point the company offered the couple and Extended Payment plan but only if they would write Advance America four postdated checks.

Another individual, Ms. Nancy of Irmo, South Carolina, also shared her story with SC Appleseed. Ms. Nancy is an 84-year-old African American woman who despite having worked as a nurse in New York City from 1970 to 1993 has no retirement fund or pension. She has a monthly income of $753 from Social Security and $57 in food stamps. Her family today consist of one son and two daughters along with nine grandchildren. She has buried three of her children. The family members are located in New York and Arizona and can offer no financial help in any form. Ms. Nancy requires a walker to move any distance and as the years have gone on, her house has fallen into disrepair as it became infested with roaches. It was only with the kindness of church members that help that she was able to get her house returned to a livable state. Her church is now helping her with some repairs to her kitchen. In 2014, Ms. Nancy took out a loan for approximately $3,000 dollars from Smart Loans as a way to afford the funeral costs for her recently deceased son. Ms. Nancy could not keep up with the high payments from Smart Loan, which were more than $600 a month. After seeing an advertisement for Motor Max on television she applied to refinance her loan. After Motor Max completed the switch, the company told Ms. Nancy to come in and not only sign her new contract but also pick up a $500 check. Before having her sign, the new contract, Motor Max proceeded only to ask what Miss Nancy's income was but never asked about bills or monthly living expenses. By the time they were finished Motor Max had her indebted for $5,604.21 and set her monthly payments at $319.28. She was paying an APR of 51% for 33 months and sent her on her way For almost two years she has struggled to make this payment, often not taking care of her monthly needs. By the time Ms. Nancy finishes her 33 payments, she will have paid back the originally borrowed $5,604.21 along with $4,932.03 totaling a combined payment of $10,536.24. The caveat being that this would be the total if Miss Nancy paid on time every time a payment is due, which is impossible. The small income she has is even more necessary now as Ms. Nancy has been admitted to the emergency room twice in the past few months which costed her upwards of $500 dollars for the ambulance ride. While in the hospital Ms. Nancy called Motor Max and informed them that she would be behind in her payment due to the fact that she could not get there to make the payment. Motor Max responded with a $16.50 late fee and told her she would have to find a way. Motor Max went on to request that she just mail them her debit card so that the company could do auto withdraws, a request she declined. Ms. Nancy continues to struggle with not only making the loan payments, but also in the upkeep of her own home. When posed with the question of what would she do if she did not have to keep making these loan payments, she responded, "I would buy a vacuum, you never really realize what you take for granted." The loan that Miss Nancy was given by either company should never had been approved and would never had been approved had the companies inquired about Miss Nancy's income and debts.

The CFPB must close the loopholes that present in the proposed rule.

South Carolina Appleseed applauds the CFPB in its efforts to address the real problems with all types of predatory lending. With these regulations in place our consumers will have a strong and interested regulator that is willing to ensure that consumers are protected, something that is missing in our state. SC Appleseed has been unable to get help from our Attorney General to stop internet pay day and auto title lending by unlicensed lenders. The Attorney General's office and the State Board of Financial Institutions both state that only the federal government can address these issues, so we welcome this help.

The CFPB must close the 5% payment-to-income loophole. Assessing income alone is not sufficient to determine if a loan is affordable or not. Without looking at all expense along with income there is no ability to assess a consumer's ability to pay. This test only gives part of the picture. The CFPB's research shows that there is still a high default rate (28 to 40%) on longer-term payday loans when payments are 5% of income or less. Finance Company loans are never in default as the company will flip the loan repeatedly over the years ensuring that that consumer is on the hook in perpetuity allowing the company to collect fees and interest on a loan made years earlier.

The ability-to-repay standard should apply to all covered loans. Even a single unaffordable loan can trap borrowers. As discussed earlier, in South Carolina we allow up to seven loans in a row with only one business day in between. More than one third of borrowers take out a subsequent loan each of those seven times. They are not borrowing within one day due to new expense but due to the fact they could not afford the initial loan and could only keep up with daily expenses by borrowing a new loan immediately. It increases to 65% of borrower taking out an immediate subsequent loan when getting to loan 12. This proves that the ability to repay should not be considered for even the first loan and clearly six short-term payday loans without any ability-to-repay is six loans too many. In addition, the *exemptions* exist for longer-term loans that carry high origination fees, such as the exemption for loans with a 36% APR and origination fees of $50 or higher. Therefore, apply it to every single loan where the lender takes control over the borrower's checking account, car, other property, or wages. These must also be closed.

In South Carolina we have an incredibly short cooling off period. During our payday lending debate consumers had proposed a modest 7 cooling off period which the lenders rejected. In fact, the industry wrote our virtually non-existent cooling off period to ensure that they could continue to keep those who could not afford to pay the debt in a trap for as long as possible. We urge the CFPB to increase the length of the cooling off period to 60 days to protect consumers from repeated flipping of loans. Implement a limit of total indebtedness for short-term loans of 90 days every 12 months, consistent with the FDIC's long-time standard for the banks it regulates.

The regulation must ensure that unaffordable short term debt does not become unaffordable long term debt. South Carolina recognized this in changes it made to its laws to take away financial incentives for small finance loans more than 20 years ago. While extra charges were removed it never eliminated this problem and to this day we see small loans flipped on a regular basis. Refinancing a loan is often a strong indication of the unaffordability of the prior loan.

The rule's proposed criteria to address flipping of longer-term loans is insufficient to prevent lenders from flipping borrowers from one unaffordable loan to the next. This loophole can be closed by allowing that the refinancing of a longer-term loan should carry a presumption of unaffordability if the borrower is delinquent by even one day or the borrower has paid less than 75% of the loan principal. The rule should also prohibit the refinancing of a covered longer-term loan a second time. Last there should be an objective assessment of the borrower's basic living expenses rather than allowing the lender to forecast this, to ensure that the borrower has enough money to cover his or her basic living expenses.

The proposal requires only that the lender not have unusually high default, delinquency, or reborrowing rates. However, even low default or reborrowing rates is not sufficient evidence when lenders have direct access to borrowers' bank accounts. Cover <u>any</u> loans where the lender has leverage to coerce payment or reborrowing. The CFPB is proposing a dangerous loophole that is ripe for evasion: exempting high-cost longer-term loans if the bank account access or car title is taken by the lender more than 72 hours after the loan has been disbursed. All loans secured by a bank account or car title should be covered by the rule, regardless of when security is taken. Additionally, loans secured by personal property and those where the lender retains the right to garnish wages are currently not covered but the rule. Due to the same tendency to compel reborrowing when a loan proves to be unaffordable, these loans should similarly be covered by the rule. Failure to do so would allow business as usual. We continue to see borrowers in this practice of being trapped into long term debt. We have seen that even with stripping away certain financial incentives, lenders continue to flip loans, especially to those with guaranteed incomes from retirement, disability or veteran's benefits. Engaging a borrower who has this type of income is the gift that keeps giving to lenders. Why would they ever need to stop serial lending when they can have their hand in a borrowers bank account for life?

South Carolina has had a long and troubled history of predatory and abusive lenders in an environment of deregulation. Coupled with being the home of the country's largest and most profitable Payday Lender, Advance America, consumers have never had a chance to truly escape the clutches of this industry. Our regulators are timid at best, but better described as hands off. We applaud the CFPB for recognizing the need to address the myriad of problems related to these high cost industries.

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 clarification on these comments, please contact me at sberk@scjustice.org or (803)779-1113 x101.

Sincerely yours,

Susan B. B

Susan B. Berkowitz

Director