The New Mexico Small Loan Industry and the Impacts of Newly Proposed Federal Consumer Protection Rules

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Presented to: Indian Affairs Committee, Mentmore, NM

July 19, 2016

Overview

- 2016 Updates to 2015 HM 131 “Examine Consumer Lending Industry” report presented by LFC Staff at IAC Nov. 9, 2015 meeting
  - Consumer and Industry Group comments
  - Applying Studies on Payday Lending Impact
  - Lending in Native American Communities
- New Consumer Financial Protection Bureau rules
  - Consumer and Industry Group comments
- New Mexico data
- Considerations

Consumer and Industry Group Comments

- Following the LFC report on Nov. 9, 2015, consumer and industry groups submitted comments
- LFC Staff is evaluating and reviewing comments submitted
- New Mexico Fair Lending Coalition commented that the 2015 report:
  - Does not evaluate whether interest rate caps harm borrowers
  - Does not clearly present total small loan volume increasing since 2007
  - Provides a helpful list of regulatory faux pas by other states
  - Provides false claims that interest rate caps force lenders to provide longer and larger loans that have higher total dollar costs
  - Provides misleading impressions that lenders are being responsible by underwriting and rejecting half of all applicants during the loan making process
  - Provides misleading facts supporting high interest rates for unreliable borrowers

Consumer and Industry Group Comments

- New Mexico Fair Lending Coalition commented that the 2015 report:
  - Should evaluate the effects of strict interest rate caps in other states
    - AR, CT, ME, MD, MA, MT, NJ, NY, NC, PA, VT, and WV
  - Should promote 12%-36% APR no credit check products offered by alternative lenders and credit unions
  - Should evaluate loopholes that allow multiple lenders to provide loans to the same borrower in NM
  - Should consider whether high overhead costs (i.e. marketing) of lenders are the primary driver for higher interest rate loans

Consumer and Industry Group Comments

- OneMain Holdings, Inc. commented that the 2015 report:
  - Does not clearly define different types of loan products (i.e. payday v. installment loans)
  - Does not clearly define "all in rate cap" as used in DOD Military Lending Act rules, which conflicts with Truth in Lending Act definition of APR (ancillary products are not included in TILA calculation)
  - Provides misleading facts about debt protection, suggesting that coverage can be mandated or denied
  - Should extrapolate on ability to repay to include willingness to repay
  - Should consider customer satisfaction and charge-off rates of responsible installment lenders
  - Should consider the access and scalability of payday alternatives
  - Should re-evaluate the legal standing of 2014 Supreme Court case on "unconscionable" interest rates over 15%
  - Should re-evaluate the effects of Colorado's payday reform law

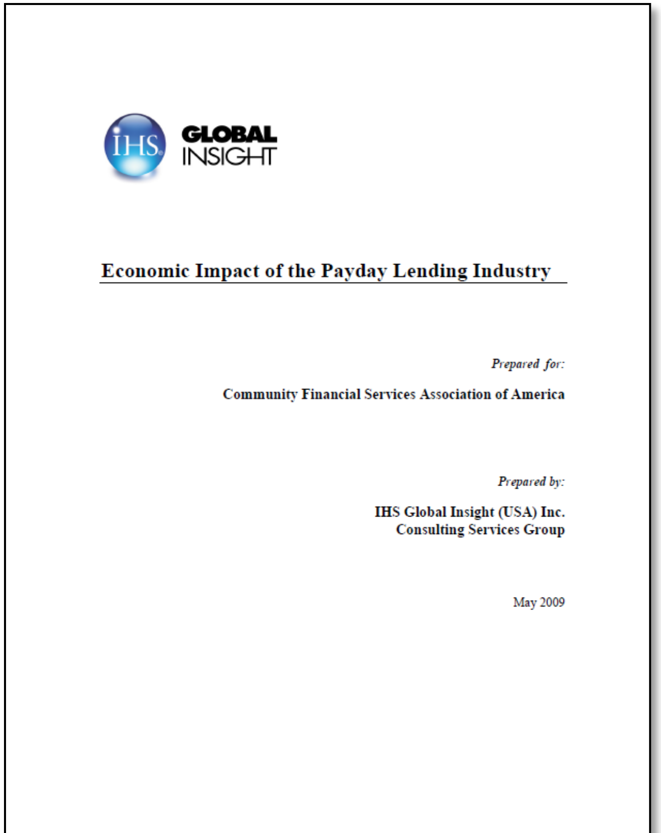
Consumer and Industry Group Comments

- Consumer Installment Lenders Association commented that the 2015 report:
  - Should provide more detail on the relationship between total interest paid (TIP) and APR
  - Should promote a 175% APR, rather than 36% APR, cap
  - Should evaluate complaint data further
  - Should evaluate payday loan alternative programs
    - FDIC Small Dollar Loan Pilot and NCUA Payday Alternative Loans

Consumer and Industry Group Comments

- MJS Consulting commented that the 2015 report:
  - Should consider separate regulation of tax refund anticipation loans from other loan products that :
    - Places an 85% APR cap on tax refund loans
    - Prohibits rollovers, refinancing, and late fees after 31 days
    - Caps the amount of interest charged to $18 per $100 loaned, including a $10 document fee
    - Prohibits retention of personal identification documents as a loan condition
    - Provides disclosures on associated costs and fees
    - Informs consumers of their right to file income tax refunds without applying for a tax refund anticipation loan

Applying Studies on Payday Lending Impact



GLOBAL INSIGHT

Economic Impact of the Payday Lending Industry

Prepared for:

Community Financial Services Association of America

Prepared by:

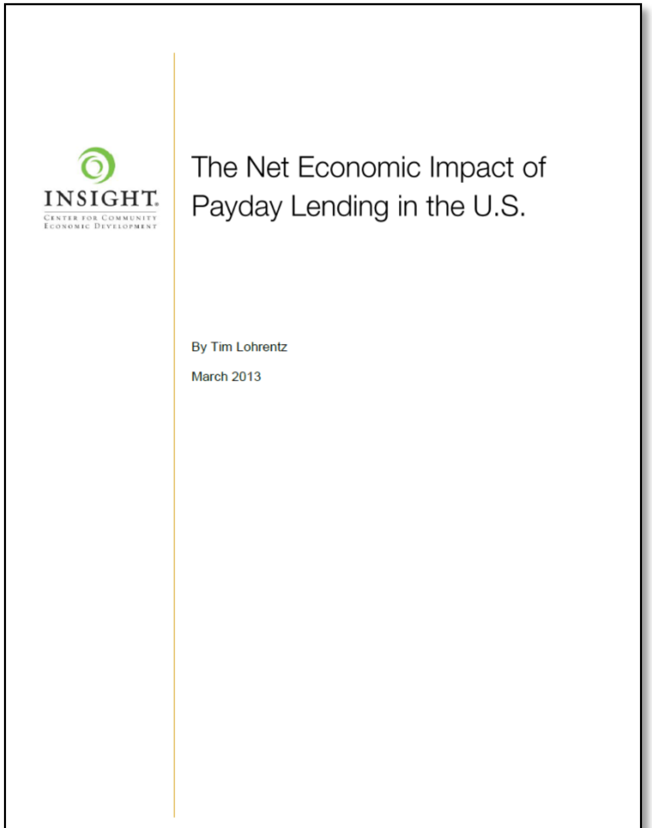
IHS Global Insight (USA) Inc.
Consulting Services Group

May 2009

IHS Global Insight Inc. (2009). Economic Impact of the Payday Lending Industry. IHS Global Insight. *Community Financial Services Association of America.*

- 2009 IHS Global Insight study found the payday lending industry
  - Supported 155,000 jobs nationally
  - Contributed $10 billion to national GDP in 2007
  - Generated $2.6 billion in federal, state, and local taxes
- IHS found, in New Mexico, the industry
  - Added $103 million in employee compensation, indirect business taxes, and other income
  - Directly and indirectly affected 1,729 jobs through employment and employee spending

Applying Studies on Payday Lending Impact


INSIGHT
CENTER FOR COMMUNITY ECONOMIC DEVELOPMENT

The Net Economic Impact of Payday Lending in the U.S.

By Tim Lohrentz

March 2013

Lohrentz, T. (2013). The Net Economic Impact of Payday Lending in the US. 14 Insight. *Center for Community Economic Development.*

- 2013 Center for Community Economic Development (CCED) study on the payday lending industry estimated nationally:
  - $774 million was lost in economic growth from interest payments
  - $169 million was lost from households due to bankruptcies
  - 11,000 - 14,000 jobs were lost
- "Principal lent to borrowers" was evaluated at virtually zero net impact on the economy

Applying Studies on Payday Lending Impact

- Using the CCED methodology, total economic impact of payday lending in NM was ($1,245,208) during 2011.

Payday Lending Interest Payments, Total Value Added, Net Value Added, and Estimated Jobs Lost, 2011

	Total Payday Lending Interest Payments (estimated)	Total Value Added from Payday Lending Industry	Total Value Added from Household Spending with No Payday Lending Interest Payments	Net Value Added (or Lost)	Estimated Jobs Gained (or Lost)
United States	$ 3,309,926,773	$ 5,562,789,003	$ 6,336,679,556	$ (773,890,553)	(11,303)
New Mexico	$ 4,700,000	$ 7,898,999	$ 8,997,901	$ (1,098,902)	(16)

Economic Impact of Increased Bankruptcies Resulting from Payday Lending, 2011

Explanation	United States	New Mexico
Total number of payday loans	96,000,000	83,077
Estimated percentage of payday loans made to first-time borrowers compared to total payday loans	3.699%	3.699%
Estimated number of first-time payday customers	3,551,040	3,073
Percentage point increase in the occurrence of Ch. 13 bankruptcies in one year	1.587%	1.587%
Additional Ch. 13 bankruptcies due to payday lending	56,355	49
Average cost of a Ch. 13 bankruptcy	$3,000	$3,000
Total economic cost due to increased bankruptcies	$(169,065,014)	$(146,306)

Lending in Native American Communities

- LFC staff attended the Reservation Economic Summit (RES) New Mexico conference on November 16, 2015
  - Tribes are offering financial service products
    - To increase access to credit for Native American borrowers
    - As an alternative to gaming operations for revenue generation
    - To decrease tribal dependence on federal government funding
    - According to Native American Financial Services Association, in 2014 there were 30 tribes participating in online lending
- Case Studies
  - Habematolel Pomo of Upper Lake
  - Chippewa Cree tribe of Montana

Lending in Native American Communities

- Habematolel Pomo of Upper Lake Case Study†
  - Explored e-commerce and online small dollar lending in 2010
  - Tribal council regulatory framework
    - Created an independent regulatory commission charged with oversight and enforcement of licensed tribal lenders
    - Prohibited tribal licensees from engaging in unfair, deceptive, or fraudulent practices or any financial services outside of the permitted ordinance
  - Tribal lenders offered unsecured installment loans
    - Data analysis and algorithmic tools were used to assess consumer income and existing credit obligations, determining ability to repay
    - Applicant repayment history was evaluated for willingness to repay
    - Tribe's underwriting process rejected 98.3% of applicants in 2015
    - Typical borrower was 45 years old with a median income of $45,000
    - Median loan amount was $700 on a 10-month payment schedule with no early payment penalties
    - Borrowers generally repay loans in less than 4 months and borrow an average of 1.6 loans over two years

†Treppa, S. (2016). Short-Term, Small Dollar Lending: The CFPB's Assault on Access to Credit and Trampling of State and Tribal Sovereignty. *Testimony before U.S. House of Representatives*. 10 Feb 2016.

Lending in Native American Communities

- Chippewa Cree tribe of Montana Case Study†
  - Created a joint venture (Plain Green Loans) with Think Finance in 2011
  - Tribe received about $7 million annually, or 4.5% of revenues
    - Although the tribe owned 51% of Plain Green Loans, it only had a nominal role in managing operations
  - Plain Green Loans offered short-term online loan products
    - Loans between $250 and $1,000 were offered to first time borrowers; up to $3,000 for returning customers
    - Think Finance's software processed borrower information to evaluate loan eligibility and calculate loan fees (up to 379% APR)
  - In 2015, the U.S. District Court of Vermont filed a complaint against Plain Green for engaging in predatory loan practices and using tribal immunity to avoid liability for these practices
    - Chippewa Cree ended its relationship with Plain Green Loans during proceedings
  - Pennsylvania's attorney general also filed a lawsuit in 2015 against Think Finance, alleging the defendants violated the state's racketeering, consumer protection, and lending laws

†Walsh, B. (2015). Outlawed by the States, Payday Lenders take Refuge on Reservations. *The Huffington Post.* 8 Sept 2015.

Lending in Native American Communities

- Considerations
  - Online tribal lenders and off-reservation "rent-a-tribe" lenders have increased
    - Tribe-owned websites loaned about $4 billion in 2013[†]
    - About one-third of the payday lending market is in online lending[††]
    - Online payday lending revenue increased from $1.4 billion in 2006 to $4.1 billion in 2013[††]
  - New federal rulings may affect tribal lending regulations
    - *Consumer Financial Protection Bureau v. Great Plains Lending*, currently pending in the 9th Circuit Court of Appeals, could determine whether the Consumer Financial Protection Act requires tribes to be treated as co-regulators or not

† Faux, Z. (2014). Behind 700% Loans, Profits Flow Through Red Rock to Wall Street. *Bloomberg Technology*. 23 Nov 2014.

†† Bourke, N., Horowitz, A., Lake, W., & Roche, T. (2014). Fraud and Abuse Online: Harmful Practices in Internet Payday Lending. *The PEW Charitable Trusts*. Oct 2014.

Consumer Financial Protection Bureau

- Proposed new federal rules for:
  - Short-term loans that have terms of 45 days or less
    - Includes typical 14-day and 30-day payday loans
    - Includes short-term vehicle title loans, usually made for 30-day terms
  - Longer-term loans with terms of more than 45 days that
    - Have a total cost of credit that exceeds 36 percent and either a lien or other security interest in the consumer's vehicle or a form of leveraged payment mechanism
    - Have a balloon payment
      - Requiring the consumer to pay all of the principal in a single payment, or
      - Make at least one payment that is twice as large as any other payment

Consumer Financial Protection Bureau

- CFPB is proposing to exclude from the new rules:
  - Loans extended solely to finance the purchase of a car or other consumer good in which the good secures the loan
  - Home mortgages and other loans secured by real property
  - Credit cards
  - Student loans
  - Non-recourse pawn loans
  - Overdraft services and lines of credit

Consumer Financial Protection Bureau

<table>
<tr><th></th><th>SHORT TERM LOANS</th><th colspan="2">LONGER TERM LOANS</th></tr>
<tr><td rowspan="2">Ability to repay (ATR) requirements</td><td>Short-term ATR</td><td colspan="2">Longer-term ATR</td></tr>
<tr><td>Lender must assess borrower’s finances and determine ATR without reborrowing within 30 days by:
• Verifying net income
• Verifying debt obligations
• Projecting housing costs and basic living expenses
• Overcoming a presumption of unaffordability for loans with a balloon payment sought within 30 days of another loan
  • Prohibits loans to borrowers who have taken out 3 loans within 30 days of each other</td><td colspan="2">Lender must assess borrower’s finances and determine ATR by:
• Determining ability to make all required payments
• Verifying similar factors outlined under short-term ATR loans
• Accounting for possibility of volatility in borrower income, obligations, or basic living expenses
• Overcoming a presumption of unaffordability for loans with a balloon payment sought within 30 days of another loan
  • Prohibits loans to borrowers who have taken out 3 loans within 30 days of each other</td></tr>
<tr><td rowspan="2">Alternative (ALT) requirements</td><td>Short-term ALT</td><td>Longer-term ALT: NCUA-type loans</td><td>Longer-term ALT: 5% annual default rate loan</td></tr>
<tr><td>Lender must:
• Confirm specified borrowing history
• Provide required disclosures
• Provide first loan with a principal amount no larger than $500
  • Second loan at least 1/3 smaller than first
  • Third loan at least 2/3 smaller than first
• Not lend to borrowers if it results in:
  • 6+ loans per 12-months
  • 90+ days of indebtedness per 12-months
  • Vehicle security connection with loan</td><td>Lender must:
• Provide loan amounts between $200 to $1,000 with
  • 46 days - 6 mo. terms
  • Fully amortizing payments
  • Maximum 28% interest and $20 fee</td><td>Lender must:
• Provide a loan with
  • 46 days - 24 mo. terms
  • 36% modified total cost of credit (excluding a $50 fee)
  • Fully amortizing payments
  • 5% projected default rate on all loans
• Refund all origination fees if lender portfolio default rate exceeds 5%</td></tr>
</table>

Consumer Financial Protection Bureau

- Proposed New Rules for Payments Practices
  - Prohibits more than 2 consecutive attempts to withdraw payment from an account with insufficient funds
    - Applies to any combination of payment channel(s)
  - Requires written notices to borrowers on upcoming payments, unusual payment attempts, and new authorizations
- Additional Requirements
  - Requires lenders to provide and update comprehensive information on most covered loans in a registered information system (RIS)
  - Requires lenders to obtain and review a RIS consumer report before making most covered loans
  - Establishes lender compliance program and anti-evasion clause
- Effective 15 months after final rule is published in the Federal Register

Consumer and Industry Group Comments

- CFPB Rules (comments by New Mexico Fair Lending Coalition):
  - Have the right intent of requiring that lenders ensure loans are affordable without reborrowing or defaulting but has shortcomings by not closing certain loopholes
  - Should require lenders to use objective measures for projecting borrower's living expenses rather than relying on default and reborrowing rates
    - NM lenders already use various practices to determine ability to repay that meet CFPB core requirements but still charge 64% of installment loan borrowers delinquent or late fees
  - Should ensure a 60-day, rather than 30-day, cooling off period
  - Do not have the authority to cap interest rates at 36% APR

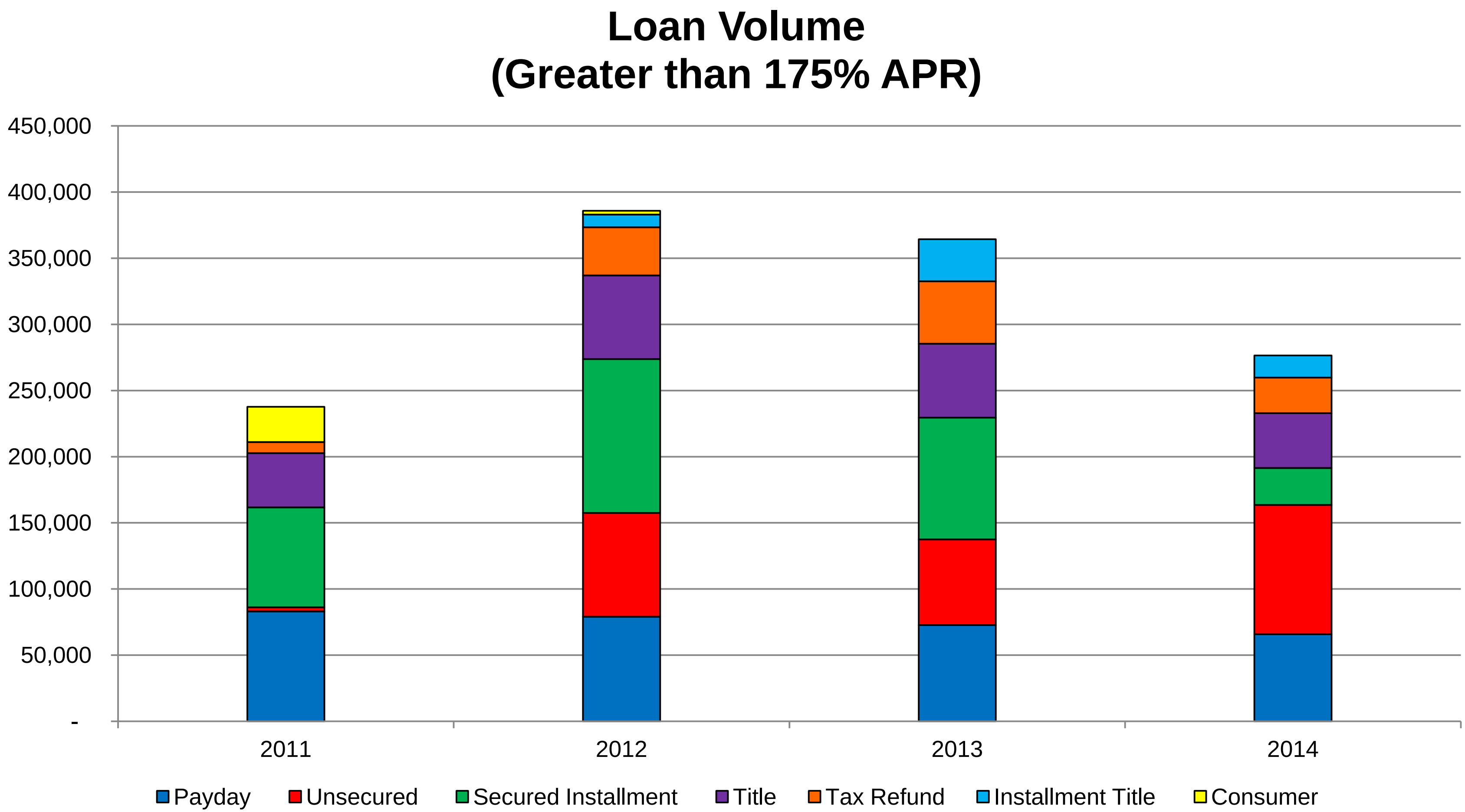
Consumer and Industry Group Comments

- CFPB Rules (comments by Community Financial Services of America):
  - Will cut off access to credit for millions of Americans
    - 2015 Charles River Associates study finds payday lending revenues will decrease an average of 82% under CFPB 2015 Proposed Rules
  - Do nothing to address illegal, unregulated lenders operating beyond U.S. jurisdiction
  - Do not consider that CFPB data shows less than 1.5% of complaints are related to payday loans
  - Were developed on data and research provided by the Center for Responsible Lending and Self Help Credit Union
  - Do not consider benefits from extended use of loan products
    - 2015 Kennesaw State University study found borrowers who engage in loan rollover activity have better credit scores than borrowers whose borrowing is limited to shorter periods

Consumer and Industry Group Comments

- CFPB Rules (comments by American Financial Services Association):
  - Clearly intend to eliminate payday and title lending industry
    - 75% to 80% projected revenue loss for payday industry
  - Will still impact traditional installment lenders
    - About 90% of products would fall under CFPB covered loan definition
    - Lender portfolio default rates range from 5% to 10%
  - Will impact ancillary products
    - 36% cost of credit all-in APR cap includes add-on products such as credit insurance

New Mexico Data



SOURCE: New Mexico Regulation and Licensing Department, Financial Institutions Division, "Payday Loan Annual Report 2008 through 2014" and "Installment Loan Annual Report APR greater than 175% 2011 through 2014"

New Mexico Data

Number of Alternative Financial Service (AFS) Products Used for New Mexico, Multiyear by Selected Household Characteristics

	2011							2013						
	Number of Households (1000s)	Number of Households (PCT)	Used 0 AFS	Used 1 AFS	Used 2 AFS	Used 3 or more AFS	Unknown	Number of Households (1000s)	Number of Households (PCT)	Used 0 AFS	Used 1 AFS	Used 2 AFS	Used 3 or more AFS	Unknown
All Households	816	100.0%	66.2%	21.9%	4.1%	3.2%	4.7%	857	100.0%	64.8%	19.0%	7.1%	3.7%	5.4%
Race/Ethnicity (PCT)														
Black	NA	0.0%	NA	NA	NA	NA	NA	NA	0.0%	NA	NA	NA	NA	NA
Hispanic	269	33.0%	61.6%	24.9%	5.1%	5.0%	3.4%	346	40.4%	58.6%	18.7%	8.1%	7.1%	7.4%
Asian	NA	0.0%	NA	NA	NA	NA	NA	NA	0.0%	NA	NA	NA	NA	NA
American Indian/Alaskan	69	8.5%	37.1%	39.7%	16.0%	7.3%	-	NA	0.0%	NA	NA	NA	NA	NA
Hawaiian/Pacific Islander	NA	0.0%	NA	NA	NA	NA	NA	NA	0.0%	NA	NA	NA	NA	NA
White non-Black non-Hispanic	425	52.1%	74.2%	16.5%	2.0%	0.5%	6.8%	410	47.8%	77.8%	14.7%	3.7%	0.7%	3.1%
Other non-Black non-Hispanic	NA	0.0%	NA	NA	NA	NA	NA	NA	0.0%	NA	NA	NA	NA	NA
Age Group (PCT)														
15 to 24 years	NA	0.0%	NA	NA	NA	NA	NA	NA	0.0%	NA	NA	NA	NA	NA
25 to 34 years	128	15.7%	59.6%	26.7%	2.2%	4.3%	7.2%	147	17.2%	50.8%	28.4%	10.2%	7.2%	3.4%
35 to 44 years	144	17.6%	64.2%	14.1%	3.5%	12.0%	6.2%	135	15.8%	57.0%	19.3%	11.1%	5.0%	7.6%
45 to 54 years	127	15.6%	64.8%	23.0%	11.5%	0.7%	-	165	19.3%	64.6%	18.3%	10.2%	1.4%	5.6%
55 to 64 years	169	20.7%	69.4%	25.4%	1.1%	-	4.2%	161	18.8%	72.8%	16.0%	3.0%	3.6%	4.6%
65 years or more	186	22.8%	78.4%	13.5%	1.5%	1.3%	5.3%	200	23.3%	81.7%	9.9%	1.9%	-	6.5%
Education (PCT)														
No high school degree	95	11.6%	64.4%	16.9%	3.5%	12.0%	3.3%	123	14.4%	51.4%	26.8%	7.4%	10.3%	4.1%
High school degree	202	24.8%	66.6%	21.9%	4.8%	3.7%	3.1%	191	22.3%	51.1%	28.6%	11.6%	3.3%	5.4%
Some college	270	33.1%	56.8%	29.9%	6.9%	2.7%	3.7%	260	30.3%	68.7%	12.0%	6.3%	4.2%	8.7%
College degree	249	30.5%	76.7%	15.1%	0.7%	-	7.5%	283	33.0%	76.2%	15.5%	4.7%	0.6%	3.0%

SOURCE: 2013 FDIC National Survey of Unbanked and Underbanked Households

New Mexico Data

Number of Alternative Financial Service (AFS) Products Used for New Mexico, Multiyear by Selected Household Characteristics

	2011							2013						
	Number of Households (1000s)	Number of Households (PCT)	Used 0 AFS	Used 1 AFS	Used 2 AFS	Used 3 or more AFS	Unknown	Number of Households (1000s)	Number of Households (PCT)	Used 0 AFS	Used 1 AFS	Used 2 AFS	Used 3 or more AFS	Unknown
All Households	816	100.0%	66.2%	21.9%	4.1%	3.2%	4.7%	857	100.0%	64.8%	19.0%	7.1%	3.7%	5.4%
Employment Status (PCT)														
Employed	435	53.3%	67.2%	21.2%	4.3%	2.9%	4.3%	472	55.1%	62.1%	19.9%	9.3%	4.4%	4.2%
Unemployed	NA	0.0%	NA	NA	NA	NA	NA	NA	0.0%	NA	NA	NA	NA	NA
Not in labor force	330	40.4%	67.9%	20.5%	4.4%	1.9%	5.3%	357	41.7%	71.6%	17.7%	3.9%	-	6.8%
Unknown	NA	0.0%	NA	NA	NA	NA	NA	NA	0.0%	NA	NA	NA	NA	NA
Family Income (PCT)														
Less than $15,000	181	22.2%	57.2%	24.3%	3.8%	7.7%	6.9%	171	20.0%	52.4%	22.0%	10.2%	8.4%	6.9%
Between $15,000 and $30,000	180	22.1%	58.3%	30.3%	3.9%	4.5%	3.0%	176	20.5%	70.5%	16.5%	7.7%	2.3%	3.1%
Between $30,000 and $50,000	156	19.1%	66.7%	13.4%	8.7%	2.6%	8.7%	164	19.1%	49.9%	29.2%	7.5%	1.5%	11.8%
Between $50,000 and $75,000	124	15.2%	72.8%	21.0%	3.3%	-	2.9%	141	16.5%	70.2%	16.5%	6.5%	4.7%	2.1%
At Least $75,000	174	21.3%	78.4%	19.0%	0.9%	-	1.7%	206	24.0%	78.3%	12.1%	4.2%	2.0%	3.3%
Missing	NA	0.0%	NA	NA	NA	NA	NA	NA	0.0%	NA	NA	NA	NA	NA
Disability Status (PCT)														
Disabled	91	11.2%	56.1%	31.0%	-	8.4%	4.5%	81	9.5%	63.1%	31.9%	2.4%	-	2.5%
Not Disabled	476	58.3%	66.5%	20.6%	5.1%	3.4%	4.4%	528	61.6%	61.5%	18.6%	9.4%	4.8%	5.7%
Not Applicable	248	30.4%	69.2%	21.0%	3.6%	1.0%	5.2%	249	29.1%	72.1%	15.7%	3.8%	2.6%	5.7%

NA = Not available because the sample size was too small to produce a precise estimate.

For this table cell, the estimated proportion would round to zero. The population proportion, however, is likely to be slightly greater than zero. AFS use cannot necessarily be compared across years. Based on the following AFS products: Check Cashing, Money order, Remittance, Payday Loan, Rent-to-own, Pawn, Refund-Anticipation-Loan. Household income (imputed) can only be compared for years 2011 and beyond as it has imputed income which was not available in the 2009. Based on physical limitations or NILF - Disabled, applicable to ages between 25 and 64.

SOURCE: 2013 FDIC National Survey of Unbanked and Underbanked Households

Considerations

- Demand for short-term, small loans exists in NM
  - Need for safe, affordable loan products that are scalable
- Payday lending has an economic impact in NM
- Increase in tribal online lending
  - Debate continues over tribal or federal regulation
- CFPB rule implementation may take a few years
  - Intends to target payday and title lending industry
- Current data on lending in NM is limited
  - CFPB rule may include national registered information systems