<u>Executive Summary of Comments Authored by:</u>

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

<u>Joined by:</u>

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
October 7, 2016

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]

***

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] 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.

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. 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.

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."[3]

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.

[3] 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.

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.[4] 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 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 CFPB 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

[4] 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.

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.

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.

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 a 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.

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.

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.

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.

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.

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.

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.

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.

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.

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.

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.

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).

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.

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.

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.