SHORT-TERM, SMALL DOLLAR LENDING: THE CFPB'S ASSAULT ON ACCESS TO CREDIT AND TRAMPLING OF STATE AND TRIBAL SOVEREIGNTY

HEARING

BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

OF THE

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SHORT-TERM, SMALL DOLLAR LENDING: THE CFPB'S ASSAULT ON ACCESS TO CREDIT AND TRAMPLING OF STATE AND TRIBAL SOVEREIGNTY

Thursday, February 11, 2016

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
AND CONSUMER CREDIT,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 1:01 p.m., in room 2128, Rayburn House Office Building, Hon. Randy Neugebauer [chairman of the subcommittee] presiding.

Members present: Representatives Neugebauer, Pearce, Lucas, Posey, Luetkemeyer, Stutzman, Mulvaney, Pittenger, Barr, Rothfus, Guinta, Tipton, Williams, Love, Emmer; Clay, Hinojosa, Scott, Maloney, Sherman, Heck, Sinema, and Vargas.

Ex officio present: Representatives Hensarling and Waters.

Also present: Representatives Stivers, Green, Carney, and Ellison.

Chairman NEUGEBAUER. The Subommittee on Financial Institutions and Consumer Credit will come to order. Without objection, the Chair is authorized to declare a recess of the subcommittee at any time.

Today's hearing is entitled, "Short-term, Small Dollar Lending: The CFPB's Assault on Access to Credit and Trampling of State and Tribal Sovereignty."

Before we begin, I would like to thank the witnesses for traveling to Washington, D.C., today for the hearing. Many of you had pretty long commutes, and we appreciate your time and your willingness to participate in this process.

I now recognize myself for 5 minutes to give an opening statement.

Today, we hold a hearing to exam the short-term, small dollar credit marketplace and examine the CFPB's efforts to regulate the market for the first time at the Federal level. This hearing is especially timely given the Bureau's efforts to put out a proposed rule in the next month or two.

Short-term, small dollar credit is essential to millions of Americans. According to the FDIC, roughly 51 million American consumers are unbanked or underbanked, meaning they don't have sufficient access to traditional banking services or products.

Short-term credit customers are disproportionality drawn from low- or moderate-income segments of the population. These individuals are more likely to have a limited discretionary income after necessities and to be much more vulnerable to unexpected expenses. Fortunately, these individuals have been able to access a variety of products from non-bank lenders, from payday loans, to vehicle title, installment lending, and the marketplace is evolving and, more importantly, it is becoming much more competitive.

The characteristics that makes these sorts of loans distinctive is their availability to consumers who have difficulty qualifying for many types of credit. These loans may not fit the needs of all consumers in all circumstances, but they are often essential to forestall consumer harm.

Last week, I had an opportunity to visit a small dollar lender in Virginia. In addition to seeing the sophisticated backroom underwriting process and understanding the diverse product offerings other than the credit products, I had the chance to actually talk to the very customers who use these products.

One couple that I met with were taking out their very first payday loan. The husband told me he works nights and that public transportation was not reliable. His family's car was in the shop, and he had to get it out so he could make it to work that night. He had two options—miss a day of work and risk losing his job, or take a short-term loan to get him through this emergency.

This is the same story that is repeated over and over in letters that I get from my constituents in the 19th District of Texas. From the mother of five, to the disabled veteran, to the painter trying to get a truck repaired, a common theme emerges in all of these stories, and it is: Please don't take away my choice and my availability to use these products.

Unfortunately, the CFPB's efforts are yet another example of Washington-knows-best mentality. Using behavioral economics—which very principles say policymakers should make choices for unsophisticated individuals—the CFPB has set down a road of paternalistic erosion of consumer product choices and access to credit.

By its own analysis, the Bureau expects roughly a 60 percent to 70 percent market contraction of these products. This is the type of behavior that people across this country are tired of seeing coming from Washington.

Now my colleagues on the other side of the aisle will point out that there are high APRs associated with many of these products. But I must remind them the vast majority of these products aren't annualized. The consumers we will hear from who use these products today aren't thinking about using these products over a course of a year. They are in and out of the product to meet a short-term need, and paying a service charge to access those funds quickly. I, and many consumer-lending scholars, believe that APR is not the appropriate way for consumers to measure the cost of these products.

Other constituencies that I have heard from regarding the Bureau's efforts are States and tribal nations. Short-term, small dollar loans are historically State-regulated products. Yet, the Bureau explicitly states that proposals under consideration, if implemented, would establish a Federal floor for consumer protection of covered loans.

Despite this recognition, the Bureau has made no signs of showing that any State or Tribe lacks the authority to regulate these products, nor has it shown that any State or Tribe is incapable of adequately protecting its citizens from potential risks associated with using them responsibly.

Of the 50 States, the legislatures of 35 have deliberately enacted small dollar lending laws of varying protections, including and up to outright bans. The remaining 15 States have also addressed this issue, either by affirmatively declining to enact an authorizing law to govern the industry or choosing to regulate through interest rates.

Crucially, and contrary to the Bureau's appeal to a greater moral obligation, no State lacks the authority to enact, repeal, or amend its own payday lending laws in order to provide greater protections to its consumers. In fact, we are going to hear in the Washington State example, that the State legislature amended its own law after realizing that the previous version had a problematic impact of decreasing credit availability. Unfortunately, the Bureau has ignored this reality.

Acting Director Silberman, who is testifying today, told this committee last April that, "We have not thought about a State that doesn't have the authority."

And in an effort to double down, Director Cordray has told this committee, "I am not thinking about it," meaning the rule this way.

As we hear testimony from this panel of witnesses, I hope everyone will remember the rulemaking in this case is discretionary and was not statutorily mandated. This is an example of the Executive Branch making the choice to preempt State laws without the direction of this Congress. This should give us all pause.

In conclusion, I hope members will leave today's hearing with a better understanding about the people who use the products, why they are important, and how they are already regulated.

And with that, I now yield 5 minutes to my good friend, the ranking member of the subcommittee, Mr. Clay from Missouri.

Mr. CLAY. Thank you, Chairman Neugebauer, and thank you to each of today's witnesses for your testimony.

Mr. Chairman, I realize that this issue does not find us in the same place. And I am sure that this hearing will highlight the reasons why.

With the APR on small dollar loans in Missouri averaging 454 percent, thousands of vulnerable Missourians continue to fall victim to costly small dollar loans. Even after reforms in Missouri law, payday lenders can still assess fees equally up to 1,950 percent APR. Equally problematic, vehicle title loans in Missouri have grown dramatically after Missouri's so-called reforms, where in 2014 alone, TitleMax repossessed 8,960 cars in Missouri.

And last summer, Attorney General Chris Koster shut down eight online tribal lenders from operating in Missouri after finding that these lenders were not properly licensed in Missouri and charged illegal fees on their payday loans.

Our experience in Missouri underscores the real need for minimum national standards for small dollar lending, and States simply cannot be expected to adequately protect consumers and rein in a $46 billion industry acting alone. The CFPB should be commended for their work to date in seeking to develop minimum national standards that can coexist with current State laws, but that also ensure access to affordable credit.

And central to the question of ensuring affordable access to credit is understanding what constitutes a fair interest rate for a payday loan. More specifically, I hope that today's testimony can clarify why a 36 percent interest rate is good enough for military personnel but not for the thousands of Missourians who use small dollar products.

I also hope that we can gain some clarity on the universe of more responsible alternatives that already strike the appropriate balance between access, affordability, and consumer protection.

Thank you again, to each of today's witnesses.

And at this time, I would like to yield the balance of my time to the ranking member of the full Financial Services Committee, Ms. Waters.

Ms. WATERS. Thank you very much, Mr. Clay.

To Mr. Neugebauer, the chairman of this subcommittee, and Ranking Member Clay, I am very appreciative for this hearing today. And, Congressman Clay, I want to thank you for all the work that you have done. You have tried for some period of time now to work with the payday lenders and to come to some agreements about what is fair and what is predatory. And whether it is with regard to mortgages or credit cards or small dollar loans, we all agree on one thing: that access to credit is important.

However, there is also an important distinction in what we believe. We are focused right now on what is happening in Flint, Michigan, where children are being poisoned because there is lead in the water. The residents of Flint have plentiful access to water. Surely all of my colleagues agree that access to water, any water, is not enough, if that water is contaminated with lead, or if that water is a vector for Legionnaire's Disease. I am very concerned about what kind of water our citizens have access to, and I believe in access to clean, drinkable water. We all do.

However, I also believe the same about mortgages and credit cards and payday loans. Consumer credit products shouldn't be available if they hurt their customers. We depend on our State regulators and the CFPB to make sure that our constituents don't have access to just any kind of credit, but to safe and fair credit products that won't put them and their families at risk.

Too many credit products are contaminated with predatory fees, reckless underwriting, and toxic fine print. I think my Republican colleagues should agree that access to loans, like access to water, should be safe. I believe our job and the job of the CFPB is to ensure access to safe, affordable credit to everyone.

I look forward to discussing how we can support the CFPB and their mission. I yield back the balance of my time.

Chairman NEUGEBAUER. Before we turn to our witnesses, I ask unanimous consent to allow non-subcommittee members to ask questions after all subcommittee members have finished. Without objection, it is so ordered.

Today, I would like to welcome our first panel of witnesses. We will introduce each panel separately, but in panel number one, we have the Honorable Greg Zoeller, the attorney general for the State of Indiana; the Honorable Sherry Treppa, chairperson of the Habematolel Pomo of Upper Lake; and Mr. David Silberman, acting Deputy Director of the CFPB.

Mr. Zoeller, you are now recognized for 5 minutes.

STATEMENT OF THE HONORABLE GREG ZOELLER, ATTORNEY GENERAL, STATE OF INDIANA

Mr. ZOELLER. Thank you, Mr. Chairman, and members of the subcommittee. I am here really to thank you for the opportunity to speak today and really not talk so much on the policy side, which is really the focus of what a lot of the testimony will be on, but really about the role the attorneys general play in terms of our own efforts to regulate the credit space that you are focused on.

I was involved when the legislature in Indiana had some of these same discussions about, how do you properly balance the access to credit with the protections against predatory lending? Some of the people who are engaged in this same hearing were involved with that. And we do have a difficult time.

I will let others argue the policy side. I am here really to argue the role of the sovereign states. I will just stick with my own, but in Indiana, we have done a fairly competent job of regulating this space. And when there are problems, there are amendments to the regulations. There is legislation. And we passed a number of bills. In fact, a lot of it looks much like what the CFPB has proposed. So it is not that we are unfamiliar with the types of arguments or what has been put into our regulations, but really it is the fact that in Indiana we have a fairly competitive market. We have made the balancing as it relates to our own State.

I have heard the complaints from different parts of the State. You get up near Chicago, near the lake, there are efforts about we should have looser regulations. We can go over into Chicago and get different kind of loans. You can cross the borders and get other loans.

We have the same kind of pressures that, why do you have to regulate it out of the State when we could do these things on a more local level? But my argument to you today is that the States are free to choose. We have a legislature that has to make these same balancing arguments based on our own borders and our own people. It is not that we don't care about the access to credit or the predatory lending. So we are doing these same things in our sovereignty.

What I am here to argue is to let the States protect our own people. If we need your help, we will call. But I think the State of Indiana and other sister States are free to, let's say, explore our own opportunities. This is a very diverse type of market, especially on the online space, so these are very fast moving types of products that we will regulate and see if we do it better than other States.

If you can come in and solve all the problems in all 50 States, it would be surprising to me. So, again, I have worked with Director Cordray when he was an attorney general in Ohio. A lot of the people I have a lot of respect for. They have really not engaged in each of the discussions with different States or they would have recognized that we don't ask for their help.

So, again, it is not that this is not space that shouldn't be regulated. We do it in Indiana, and, again, it is not all that much different than what the CFPB is proposing. It is just a question of who is going to regulate and whether that is what the people of our State wish.

The same arguments that I have heard about needing to protect people, I hear all the time that States can't be expected to regulate in a big industry. You could essentially shut down all of the role of an attorney general with that kind of approach. We would no longer need State regulation if Washington would just regulate the country as a whole, like they do in Europe. They don't have States that have their own sovereign. That is what makes us unique.

We do have Federalism. And I am here to defend the Federalist principles that really allow the sovereignty of Indiana to stand up and to be responsible for protecting our own people, allowing access to credit. And if we make mistakes, we are free to do that, and we will fix it ourselves. We won't come back to Washington and ask for little minor changes, because of the changing landscape of these very diverse products. We are much more flexible. We are much more able to address these things on an ongoing process. Coming back to Washington and trying to get something done to protect our consumers is not something I am anxious to do.

We can do it much more pliably and flexibly at a State level than coming back here and asking this committee and the CFPB to engage in the local nuances that we are finding in our State. We had five complaints last year. We have handled those pretty efficiently. And if we need more help from Washington, I will call you.

Thank you.

[The prepared statement of Mr. Zoeller can be found on page 135 of the appendix.]

Chairman NEUGEBAUER. I thank the gentleman. Ms. Treppa, you are recognized for 5 minutes.

STATEMENT OF THE HONORABLE SHERRY TREPPA, CHAIRPERSON, HABEMATOLEL POMO OF UPPER LAKE

Ms. TREPPA. Chairman Neugebauer, Ranking Members Clay and Waters, and members of the subcommittee, thank you for the opportunity to testify at this important hearing. My name is Sherry Treppa, and I am the chairperson of the Habematolel Pomo of Upper Lake, a federally recognized Indian Tribe.

I have served on the Tribe's executive council for the past 11 years and as Chair since 2008. I also am the vice chairperson of the Native American Financial Services Association, an intertribal organization advocating for tribal sovereignty and responsible business practices in e-commerce.

Our Tribe owns online lending businesses. I want to share how we regulate these businesses and the considerable tools we use to protect consumers. I will also offer my thoughts on the CFPB's effort to restrict this marketplace and the impact that it will have on consumers and Tribes.

Our Tribe has resided in rural Upper Lake, California, since time immemorial. Our people flourished until migration and settlement brought conflict and diseases, and in one generation, reduced the Pomo Indian population by nearly 95 percent.

Flawed Federal policies further subjected our people to enslavement, internment, abuse, and slaughter. In 1956, the California Rancheria Act terminated our Federal recognition. Despite these efforts to destroy our Tribe, we persevered. From 1975 to 2004, we fought and succeeded in restoring our Federal recognition. The inherent sovereignty of Indian Tribes predates the United States and is memorialized in the Constitution and affirmed in numerous court decisions and statutes.

Congress has consistently acknowledged a Tribe's authority to govern its own jurisdiction. Indeed, the Dodd-Frank Act recognizes the Tribe's role in consumer protection by granting it the same authority as both States and the CFPB in bringing legal actions. When our Tribe decided to enter the industry, we took thoughtful, measured steps based on our sovereign power to regulate the businesses that would operate within our jurisdiction.

The lending ordinance we enacted requires lenders to be licensed. It also imposes ongoing compliance obligations. It prohibits tribal lenders from using practices that are unfair, deceptive, or misleading to customers, and established an independent regulatory authority to oversee lending operations.

Pursuant to our ordinance, tribal lending entities may not charge consumers an application fee or penalize them for early repayment. Lenders also must maintain a system to ensure compliance with tribal and applicable Federal law, written policies that cover all aspects of lending, including underwriting and internal controls to ensure that their operations follow their policies.

Our regulatory commission conducts regular audits. If deficiencies are identified or if a lender is non-compliant, the commission is empowered to issue fines, penalties, or revoke the lending license. The Tribe takes consumer protection seriously for an important reason—it receives 100 percent of the net income from loans made by these businesses. This allows us to fund important government services including elder care, education assistance, and vital social service programs.

Our regulatory framework and loan products together successfully meet both the Tribes' and consumers' needs. We do not offer payday loans. Our lenders offer loans that are repaid in installments and are not eligible for rollovers.

Our Tribe's commitment to consumer protection is reflected in these following statistics. In 2015, only 2 percent of all applications submitted were approved and funded. Put another way, 98 percent of new customers are rejected in underwriting. Although loans have a 10-month schedule, most customers repay their loans in 4 months. Customers have moderate borrowing patterns with an average of 1.6 loans in 2 years.

Finally, our complaint volume in 2015 was less than 2 percent of all loans issued. Our statistics underscored that tribal self-regulation can successfully achieve responsible lending and consumer protection. Before the CFPB seeks to impose new regulations, I would first ask them to acknowledge the rigorous regulatory framework that our Tribe has created and that our lending businesses are operating within. The answer is clear—additional CFPB rules are not necessary because all of the tools necessary to protect consumers already exist.

From my perspective, the CFPB's proposal would do nothing more than choke off consumer choice and access to needed credit, while destroying economic developments for opportunities for Tribes.

Thank you for your time. And I am happy to answer questions at the end of the session.

[The prepared statement of Ms. Treppa can be found on page 129 of the appendix.]

Chairman NEUGEBAUER. Thank you. And now, Mr. Silberman, you are recognized for 5 minutes.

STATEMENT OF DAVID SILBERMAN, ACTING DEPUTY DIRECTOR, CONSUMER FINANCIAL PROTECTION BUREAU

Mr. SILBERMAN. Chairman Neugebauer, Ranking Members Waters and Clay, and members of the subcommittee, thank you for the opportunity to testify today. My name is David Silberman, and I serve as Associate Director of the Division of Research, Markets and Regulations at the Consumer Financial Protection Bureau. Last month, I also was named an acting Deputy Director.

When the Dodd-Frank Wall Street Reform and Consumer Protection Act was enacted, payday loans were a particular area of concern to many in Congress. Indeed, the Dodd-Frank Act gives the Bureau plenary authority to supervise any entity that offers payday loans, regardless of size. As a result, when the Bureau began supervising non-depository institutions in 2012, payday lending was the first industry that was brought into our supervisory program.

At the same time, the Bureau decided to begin the process of fact-finding to assess whether there was a need for Federal regulations to prevent unfair, deceptive, or abusive acts or practices in this market, as those terms are defined within the Act.

In January 2012, the Bureau held a field hearing in Birmingham, Alabama, in order to hear directly from stakeholders and the public about actual consumer experience with small dollar loans. During the year that followed, the Bureau engaged in an in-depth study of the market, and based on that study, the Bureau issued a White Paper.

That White Paper showed that making these short-term loans to low- and moderate-income consumers without assessing the consumer's ability to repay puts many consumers at risk of turning short-term emergency loans into a long-term expensive debt trap.

In 2014, the Bureau published a second report. In that report, we traced borrower sequences and found that only 35 percent of borrowers were able to repay the loan when due without quickly re-borrowing, and that 15 percent of borrowers took out 10 or more loans in rapid succession. We found also that 50 percent of all loans went to consumers in these lengthy loan sequences.

Looking at payday consumers who receive their incomes on a monthly basis, the report found that 1 out of 5 remained in debt for the entire 12 months of the Bureau's study. The consumers who fall into this category include elderly Americans and persons receiving supplemental security income and Social Security disability.

Finally, the Bureau found that over the course of a sequence of loans, 20 percent of consumers end up defaulting and finding themselves in the hands of debt collectors. The Bureau then held a government-to-government tribal consultation with tribal leaders interested in small dollar lending to hear their input as we were thinking about how best to proceed. And all this brings me to the outline of proposals that are currently under consideration.

The Bureau released that outline in March of 2015, when it convened a small business review panel to gather input from small entity representatives. The goal of the proposals under consideration is to prevent consumers from being offered unaffordable loans while still preserving access to affordable credit. To do that, the proposals under consideration would require that before making a loan, lenders would be obligated to make a good-faith, reasonable determination that the consumer has the ability to repay the loan. That is to say, the lenders would have to reasonably determine that after repaying the loan, the consumer would have sufficient income left to pay major financial obligations such as rent or mortgage and also to cover their basic living expenses, such as food or transportation or childcare or medical care, without the need to reborrow in short order.

As an alternative to the basic prevention requirement, the proposals under consideration also contain protection provisions. These provisions would allow lenders to extend certain short-term loans without considering the ability to repay, so long as the loan satisfies certain screening requirements and contain certain structural protections to prevent short-term loans from becoming long-term debt, turning into a collections nightmare for the consumer.

Stakeholders on all sides of the issue have provided us with valuable feedback on the proposals under consideration. Consumer advocates have argued that the Bureau should not permit any lending which does not meet the basic ability-to-repay standard. Industry stakeholders argue that the protection alternative under consideration is too restrictive because these requirements would allow no more than three loans in a sequence or six loans in a year. State policymakers have urged the Bureau to both protect consumers across all small dollar lending markets and to seek feedback from the States on their regulation of small dollar lending products.

After the Bureau released the proposals under consideration, we convened a second tribal consultation that was a frank discussion that allowed tribal leaders to share their views with the Bureau about the proposals. We continue to receive feedback from Congress, State, local and tribal officials, consumers, industry, and others. The Bureau's next step will be to formally issue a proposed rule, a rule which will seek to balance access to affordable credit with protecting consumers from loans that are beyond their ability to repay.

Once the proposal is issued, the public will have the opportunity to make written comments. The Bureau will carefully consider those comments before final regulations are issued.

Chairman Neugebauer, Ranking Members Waters and Clay, and members of the subcommittee, thank you for the opportunity to testify today. I look forward to your questions.

[The prepared statement of Mr. Silberman can be found on page 94 of the appendix.]

Chairman NEUGEBAUER. I thank the gentleman. Mr. Silberman, I want to ask you a question before I get started with our questions. Have you ever visited a small dollar credit store?

Mr. SILBERMAN. Mr. Chairman, a number of members of my staff have done so. I personally have not.

Chairman NEUGEBAUER. I didn't ask about your staff. I said, have you ever personally visited a small dollar store?

Mr. SILBERMAN. As I indicated, I have not. They have.

Chairman NEUGEBAUER. Okay. I think that is a little disconcerting, because you are talking about a fairly major revamping of an industry that has been in place for a number of years and that millions of people are using on a daily basis to help manage the ups and downs of life. And for you to not go out and visit with people in the stores and visit the stores and understand better what is going on, doesn't speak well. So I would encourage you to make that trip before you make any final decision.

Last April, you told me, "We have not thought about a State that doesn't have authority." When moving forward this rule, have you done any more thinking about this issue? Specifically, which Tribe or State lacks the authority to regulate payday or small credit lending? Do you know of a State that does not have the authority to do that?

Mr. SILBERMAN. Mr. Chairman, as I hope I said when I was last before you, our mandate from the Congress is to enforce Federal law and ensure that every citizen has the rights provided by Federal law. One of those rights—

Chairman NEUGEBAUER. Do you know of any States or Tribes that aren't enforcing the Federal law?

Mr. SILBERMAN. The obligation to enforce the Federal law rests in the first instance on the Bureau.

Chairman NEUGEBAUER. I know. But I am just saying that you would be enforcing them if nobody else was. Where is the gap in the—where is the hole in the system that you feel like that the CFPB has to fill?

Mr. SILBERMAN. I think the gap is that the statute says that it is the obligation of the Bureau to issue rules to identify and prevent unfair, deceptive, and abusive acts and practices. Once we issue those rules, the States are free to enforce those rules, but it is in the first instance up to us to determine what rules are required to prevent such kind of unfair and abusive practices.

That is why we have spent the last year studying this issue. That has led us to the determination that there is a problem that we need to address with respect to loans being made without regard to consumers' ability to repay.

Chairman NEUGEBAUER. I think a number of State attorneys general, including Mr. Zoeller, have said they think they are doing a pretty good job of regulating this space. They have been at it a lot longer than you have. Many of the States have had small credit or lending statutes on their books for a long time. They have had an opportunity, as been mentioned here, to balance between making sure that people are protected, but also making sure that they have access to credit.

Have you found a State that is not enforcing their laws?

Mr. SILBERMAN. No, I think the States are enforcing their laws. And for the reasons you state, Mr. Chairman, what we are doing is establishing a Federal law floor, and the States will continue to be able to enforce their laws and their specific requirements in addition to the Federal floor that implements the obligation that has been placed upon the Bureau.

Chairman NEUGEBAUER. Here is kind of the problem. It is really up to the Congress to determine if it is appropriate to preempt a State's law; it is not up to the Bureau to do it. And to me, the fact that the Executive Branch has decided that they are going to preempt 50 States' rights to govern an area of finance in their States isn't up to the Bureau to do that. To me, that would be up to the Congress.

One of the very things that people are very frustrated about right now, is they feel like that this Administration is trying to tell people how to run their lives. And I think when you are seeing this record turnout in some of these early primaries, both on the Democratic and Republican side, I think what you are seeing is an outrage at the direction of the country.

So, Mr. Zoeller, what is your response to the fact that Mr. Silberman doesn't think you are doing a good job?

Mr. ZOELLER. I will leave it to the policymakers in our legislature to defend the weighing that they make. And I will defend their authority to do it. I guess there are a lot of things where States can't do it ourselves. And we will look to Congress to service in those areas, and this is not one of them.

The policy decisions and the weighing of these collective rights and the balancing for our protections, I do go to our legislatures and argue these same areas where consumers are not being treated fairly. But, again, a lot of it is not necessarily that the CFPB's rule would, let's say, be bad in Indiana. It is that we are much more flexible, so when there are things that we need to change, I can go upstairs to our legislature and they usually will recognize a problem in Indiana, and we can address it.

There are so many things changing in this area that I think the snapshot that the CFPB is taking might be their best guess today, but the ability to come back and change things is much easier at the State level to protect our consumers and maintain access to credit. So we will keep our own authority, thank you.

Chairman NEUGEBAUER. Last question. Yes or no? Are you enforcing the laws that your legislature had passed?

Mr. ZOELLER. Yes, sir.

Chairman NEUGEBAUER. Thank you. I now recognize the ranking member of the full Financial Services Committee, Ms. Waters, for 5 minutes.

Ms. WATERS. Thank you very much, Mr. Chairman. Before I ask this question, I would just like to give a little bit of the backdrop.

I receive many calls in my district office about people who are in trouble, people who are oftentimes low-wage earners, some as desperate as has been described here, but the fact of the matter is, they get hooked in the payday loan scenario. They start out by getting a loan. They can't afford to pay it back on time, so it is rolled over. Then, it is rolled over again. And they are never able to get a hold on their finances, and they find themselves doing six, seven, eight of these loans a year on and on and on and on. So it is a problem.

And for anybody who says it is not a problem, you are wrong. There is a problem that has been identified dealing with payday loans. I, of course, have not been in a payday loan and asked to go in their back room and see their criteria or anything like Mr. Neugebauer, but I have not been in JPMorgan Chase, I have not been in Bank of America, and I have not been in Wells Fargo, any of them. And I am sure if I did, they wouldn't let me in their backroom, anyway.

I just want to have it on record and to have us understand that the CFPB is not just venturing into something because they have nothing else to do. The fact of the matter is, it is a problem. There is a problem out there. And we are hearing about it from constituents. It seems to be spreading, you know, free money tree, get your money here, whatever those names are of these places are just springing up everywhere, particularly in poor communities. The poorer the community, the more of these street-level operations we have.

While I normally do not believe in Federal preemption, I think we have a responsibility to step in when our constituents tell us they are hurting, that they think that they are not being treated fairly, that they think that they are being ripped off. We have a responsibility to do that. And we are seeing more of this kind of discussion from our constituents about the haves and the have-nots and the 1 percent.

And they are hating government. They are hating corporations. They are hating the financial services community because even the middle class are not doing well.

But I want to ask you, Attorney General Greg Zoeller, later today we are going to hear from financial services industry lobbyists on the second panel who will argue that the CFPB's proposed payday lending rule will choke off access to needed credit for vulnerable consumers. These lobbyists made the exact same arguments when the Department of Defense was working on amendments to the Military Lending Act that sought to protect servicemembers from excessive interest rates and fees on short-term credit products.

You wrote to the DOD asking them to strengthen, not weaken, their MLA rules in a latter with other State AGs from December 2014. In essence, you rejected the industry's arguments as crying wolf. Why don't you think the industry is again getting it wrong when it comes to the CFPB's rules?

Mr. ZOELLER. I think that does help set this up, because we were working with Attorney General Beau Biden and a number of other people who were focused on the credit that is extended to military personnel who move throughout the State and throughout States. There may be more of a need for those consumers who aren't always under the protection of a State the same way that others are. So we do think that there are certain consumers who aren't residents, who may be transient. And I do think that the focus on the vulnerability of military personnel is somewhat of, I would say, a unique group.

But in the other areas that you are talking about, in California, if they have had a problem and the attorney general there has not addressed it or the legislature, they might call and ask for the State to focus on it. And, again, we were asking Congress to look at some of these things as it relates to a different kind of category. But the people in our State are protected. Some of the military men and women, I think were a unique case.

Ms. WATERS. Let me just say this. We all know that it is politically powerful and safe to talk about protecting our military, because these are people who put their lives on the line for us, whether they are active or veterans or whatever. It is good politics to talk about helping veterans.

But what is good for the goose is good for the gander. If you are willing to write letters to protect veterans from predatory lending practices, you ought to do that for everybody.

I yield back the balance of my time.

Chairman NEUGEBAUER. I thank the gentlewoman.

And now the vice chairman of the subcommittee, Mr. Pearce from New Mexico, is recognized for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman.

Mr. Zoeller, Ms. Treppa, I think you might be better qualified to answer. You heard Mr. Silberman's testimony that 20 percent of the loans default. Do you find 20 percent default on your loans?

Mr. ZOELLER. No.

Mr. PEARCE. I was asking Ms. Treppa. Sorry.

Ms. TREPPA. Thank you for that question. No, we have quite far less than that kind of a default rate.

Mr. PEARCE. Okay. And, Mr. Zoeller, do you think that institutions across an industry would be able to stay in business if they had a default rate of 20 percent?

Mr. ZOELLER. Not in Indiana.

Mr. PEARCE. Yes. Mr. Silberman, I see in your testimony also that you declare that APR is 391 percent to 521 percent. What is a fair percent to where the CFPB wouldn't declare it to be extortion or abusive?

Mr. SILBERMAN. Thank you, Congressman. The CFPB has no authority to regulate interest rates.

Mr. PEARCE. I didn't say regulate. I said, when do you believe, as the CFPB, that it becomes abusive? Because you say you are after the abusive techniques. So when does a rate become abusive?

Mr. SILBERMAN. The CFPB views the abusiveness not about the rate, but about the practice of making a loan—

Mr. PEARCE. Why did you put the rate in your testimony if it does not apply to what you are trying to tell us today? Why did you put that in there? I find that offensive. Because you come in here and you try to mislead us on that, and then you tell me when I ask you that you have no opinion, that it is not your purview, that you don't even have an opinion. What is your personal opinion about when it is too high?

Mr. SILBERMAN. Congressman, I don't believe it would be appropriate for me to offer you my personal opinion.

Mr. PEARCE. You are the Deputy Director.

Mr. SILBERMAN. And so therefore, I am here to represent the Bureau.

Mr. PEARCE. Why did you put it in your testimony then?

Mr. SILBERMAN. Because we thought—that portion of the testimony was describing a report we issued. We are a data-driven—

Mr. PEARCE. Why did you issue a report on something you have no interest in? You said it is not right for the agency to take a position on that, so why did you issue a report on it? It is obvious that you have an opinion about it as an agency.

Mr. SILBERMAN. Congressman, we did not issue a report about that. We issued a report about the practice of making unaffordable loans. As part of that report, we thought it was important to describe the facts as we understood them so we could—

Mr. PEARCE. Okay.

Mr. SILBERMAN. And that was one of many, many facts, but not what the subject of the report was.

Mr. PEARCE. But let me give you a contrast, sir. So let's say 15 percent is a higher rate of interest. You can go to a bank today and get a loan for 6 percent, 15 percent, you go in, you borrow $100 for a month, at a 15 percent rate of interest, which is $1.50 for the year, just roughly speaking. I know it would come out a little bit different. You divide that by 30 days, and you get 75 cents.

Now, I am asking you, would you loan $100 for a month for 75 cents rate of return? And that is what you, the agency, are doing by putting numbers like this in reports. And you are going to an industry where I have two letters today that come from constituents who this past week walked into places where one says, I had a medical emergency, I have a disabled daughter. I just needed help to make it to the end of the month. And you are going to shut down 70 percent of these people, you. You, Mr. Silberman, are going to shut down 70 percent of these people if you put this rule into place.

Now, if the industry is so profitable, 391 percent to 521 percent are your numbers, if it is that profitable, how come all institutions are not flocking into it? Do you as an agency consider that?

Mr. SILBERMAN. Congressman, actually that goes to the question you asked Ms. Treppa.

Mr. PEARCE. No, it does not. I am asking you. So, Mr. Silberman, you used to work for Kessler Financial.

Mr. SILBERMAN. I did indeed. Yes, sir.

Mr. PEARCE. And Mr. Kessler is one of the richest men in America by far in the 1 percent, $300 million net worth. Did you ever suggest that maybe he ought to get into this lucrative market that is down here and is ripping people off? This industry leader of Kessler could get into here and we could clean it up by ourselves by competitive advantage that we are offering. Did you ever once as executive vice president of that operation suggest that to Mr. Kessler that he might increase his rate of return by taking out these bad actors that you are trying to take out as an agency?

Mr. SILBERMAN. Mr. Kessler did not need my advice as to how to make more money.

Chairman NEUGEBAUER. The time of the gentleman—

Mr. PEARCE. But you, I would note, are avoiding the answer of whether you took a moral position at that company on whether or not you all were supporting an industry that does far more to the poor. Thank you. I yield back.

Chairman NEUGEBAUER. The time of the gentleman has expired. The Chair now recognizes the gentleman from Missouri, the ranking member of the subcommittee, Mr. Clay, for 5 minutes.

Mr. CLAY. Thank you, Mr. Chairman. And this question is to Ms. Treppa. In March of 2015, Missouri Attorney General Rich Koster announced that eight online lenders acting through business entities operating from a Native American reservation in South Dakota could no longer operate in Missouri, finding that, "These predatory lending businesses operated in the shadows, taking advantage of Missourians through outrageous fees and unlawful garnishments."

Given that a majority of tribal lenders' businesses occur off tribal land, could you elaborate on how you advertise and acquire customers like those in Missouri who were the subject of the AG's enforcement action, and specifically what marketing channels do tribal leaders utilize?

Ms. TREPPA. Certainly, Congressman. Thank you for the question. I can't speak to the specifics of that issue. However, we originate loans on tribal lands. They are accessed via the Internet by customers. We acquire customers online through various ways: search engine optimization; lead generation; and paper click, all of the standard access opportunities.

Mr. CLAY. Does your Tribe have its own tribal usury rate? And if so, what is your usury rate?

Ms. TREPPA. We don't have a usury rate, per se. The cost of the product is commensurate with the cost of customer acquisition, as well as the cost of underwriting and the cost to regulate.

Mr. CLAY. What would be a normal rate of short-term loans?

Ms. TREPPA. The rates for our installment loans—and they are not payday products—are dependent upon the customer's cycle to repay, whether it is semi-monthly or biweekly.

Mr. CLAY. So the longer it takes to repay, then the higher the interest rate?

Ms. TREPPA. Congressman, the installment loans are up to 10 months. However, the majority of our customers pay it off within 4 months.

Mr. CLAY. What percentages goes into default of those loans? Do you have any idea?

Ms. TREPPA. Default rates are under 16 percent, typically. We have a high rate of satisfaction with our customers, 98 percent. And as I mentioned, default rates are relatively low.

Mr. CLAY. Let me ask you, why do you think people come to companies like yours and others for these products, for the loans?

Ms. TREPPA. Because they have an immediate need, and there is a lack of supply in the market.

Mr. CLAY. So maybe a bank that they have a regular account with or a checking account would deny them outright and so they look for alternatives? Is that it?

Ms. TREPPA. Congressman, typically banks don't loan small dollar amounts. Our loans are $1,200 or less.

Mr. CLAY. You fill a niche, then, correct?

Ms. TREPPA. Sure. There is a need and we—

Mr. CLAY. People need the money, apparently.

Ms. TREPPA. —provide a badly needed product to our consumers.

Mr. CLAY. Would you not agree that State AGs like Attorney General Zoeller and my attorney general had the right to protect their own citizens from lenders in whatever way they see fit, including through State licensing requirements or State usury caps?

Ms. TREPPA. As I had mentioned earlier, the consumers access our product via the Internet. And the loans are originated on tribal lands. We have a robust internal compliance department, as well as a regulatory commission that oversees and licenses all of our lenders that operate on our tribal lands.

Mr. CLAY. Yes, but these are people from different States, too, correct?

Ms. TREPPA. Correct.

Mr. CLAY. Okay. I will wait for the next round. Thank you. I yield back.

Chairman NEUGEBAUER. I thank the gentleman. Now, the gentleman from Missouri, Mr. Luetkemeyer, the chairman of our Housing and Insurance Subcommittee, is recognized for 5 minutes.

Mr. LUETKEMEYER. Thank you, Mr. Chairman.

Mr. Zoeller, I certainly appreciate your, "don't call us, we will call you" attribute. I think that is what we all would hope that the people from the States would be having, because I think that is how we as a country should operate. We are not the country of America. We are the country of the United States of America, which means emphasis on "States." We are all a group of States that are as one country. And therefore, the States have the ability to make these rules and regulations, and that needs to be allowed for you to continue. I certainly appreciate your testimony along those lines. To me, this is extremely important.

Mr. Silberman, you made the comment a while ago that your job was to enforce the law. And then you turn around and make a rule and intend for that to be the law. It is very disconcerting to me to have that statement made and turn around and you by rule can change law and/or make law. That seems to be going on, on a regular basis in this Administration.

Would you like to elaborate and give your position on it again?

Mr. SILBERMAN. Thank you, Congressman. Yes. The job of our Bureau, like many administrative agencies, is to particularize, if you will, laws that are passed by Congress. Congress defined "prohibited, unfair, deceptive, and abusive practices."

We think we have an obligation—we could go in, you are right, and just start enforcing that rule and suing people without giving them any notice that here is what we understand that to mean. We think that would be bad practice, so what we have tried to do is to do careful research and study—

Mr. LUETKEMEYER. Mr. Silberman, you are going through the rulemaking process here, but it certainly gives me pause—if you make this same rule the way you did others, you are not going to listen to what everybody says. I had a group of bankers one time come into my office and they told me that they had just left the CFPB. They were mad as the dickens. They said, you know what, we were told that we were the 42nd group that was talking to the CFPB over this issue of qualified mortgages.

And they were told, we appreciate you being here, but you don't know anything about what you are talking about. Now, you have a lot of responses and going to get a lot of responses on this issue. I hope you consider all that very carefully, because those are the consumers that you are going to be hurting by what you are doing.

Mr. Zoeller, quick question: You made the comment a little ago that you only had five complaints with regards to payday lending in your State?

Mr. ZOELLER. That is correct.

Mr. LUETKEMEYER. Is that correct?

Mr. ZOELLER. That was 2015's number.

Mr. LUETKEMEYER. How many transactions did you have over the course of that year? Do you know offhand?

Mr. ZOELLER. I am not part of the industry. I know it is a lot, though.

Mr. LUETKEMEYER. Thousands and thousands, no doubt.

Mr. ZOELLER. Yes, sure.

Mr. LUETKEMEYER. I can tell you from being a financial Services chairman back in Missouri, my good friend, Mr. Clay, I followed him in the legislature, and we put the model legislation in place for payday lending. And one of the jobs as chairman of the committee was to see once how it worked. And we actually had fewer complaints on our payday lending folks than we did with the banks themselves.

Mr. Silberman, by your own admission, the CFPB's admission, and taking the statement from the chairman, 60 percent or 70 percent of the payday loan folks are going out of business, which is going to restrict the ability to have access to credit for lots and lots of folks. What is your solution?

Mr. SILBERMAN. Thank you, Congressman. We have not said that 60 percent or 70 percent of companies—

Mr. LUETKEMEYER. Whoa, that is pretty well in print lots of places. Mr. Cordray has actually said that in this committee. In fact, I think in this committee, he made the statement of 80 percent. But we will take 60 percent or 70 percent, and give you the benefit of the doubt.

Mr. SILBERMAN. If I can finish, Congressman, what we have said is not that. What we have said is that of the loans that are made today, 60 percent to 70 percent go to consumers who have received more than 6 loans in the course of a year, and that if nothing changed and if industry simply said what they are going to do is stop making loans after 6, that would mean 60 percent or 70 percent of the loans would stop.

We have also been very clear to say that is not at all what we expect to happen, that we expect to see changes, and in that regard, I would indicate that what we have said is actually no different than what the industry had said long before we issued our proposals.

Mr. LUETKEMEYER. I have one more quick question. I am about out of time here. I asked the question originally, what are you going to do about the alternative? What are people going to be able to do? I didn't get an answer.

In the President's budget, he has a line item in there, in the community development financial institutions fund program account for $10 million. The program will support broad-based access to safe and affordable financial products and provide an alternative to predatory lending by encouraging CDFIs to establish and maintain small dollar loan programs, $10 million. So the President is going to set up his own payday lending business? Is that what is going on?

Mr. SILBERMAN. Well, Congressman—

Mr. LUETKEMEYER. Mr. Silberman, I realize we have left you speechless here. But the bottom line of this is, we have the Administration that is going to get in the payday lending business, and they know they can't make money at it, and they are going to subsidize it by $10 million. You know what? How about if we just go give them grants? Every time you need a set of new tires on your car, just go to the government to get a grant to get $500 to go get a new set of tires. Okay. How about if your kids need new braces? Go to the government and get a grant for $2,000. That is what you are talking about here. That is wrong. I yield back.

Chairman NEUGEBAUER. The time of the gentleman has expired. The Chair now recognizes the gentleman from Texas, Mr. Hinojosa, for 5 minutes.

Mr. HINOJOSA. Thank you, Chairman Neugebauer and Ranking Member Clay, for holding this hearing. I also want to thank our distinguished panelists for their appearance here today and for sharing their insights with us.

Time and time again, we hear about hardworking families being exploited by predatory, small dollar, short-term lenders such as payday lenders. While these loans are meant to help unbanked and underbanked individuals in need of quick cash, far too many times the borrower ends up trapped in a vicious cycle of rollovers of fees and more debt.

We sell our families short when we accept that high-interest loans are the best we can do for our communities. Payday and auto title loans with uncapped annual percentage rates have long enticed families in moments of desperation, offering short-term fast cash at the cost of long-term debt at rates averaging $500 annual percentage rates.

Let me share with you that in Texas, an average $500 payday loan costs an astounding $1,100 or more to repay in a period of just a few months. In Texas, payday and auto title loan businesses have the second highest number of consumer complaints by their regulator. In addition, payday and auto title lending is a top reason why scores of families end up at the doors of social services agencies in my State.

Let me go to the first question. Mr. Silberman, can you tell us about what the CFPB research has found regarding the payday and auto title lending industry? What are the consumers being harmed by in this industry?

Mr. SILBERMAN. Thank you, Congressman. Our research which we have done over—as I indicated—a period of several years through several studies, field hearings and the like, confirms very much what you have indicated, that for a significant number of consumers, they enter into these loans and then find that they had a need, but when it comes due, they can't afford to make the payment.

Some of them default and wind up in a collections experience, perhaps having their wages garnished. Some wind up in bankruptcy. But many wind up borrowing again, and then 2 weeks later the same thing happens and they borrow again and again.

The analogy that I found quite helpful is, the CFSA on their website talks about—analogizes to taxis and says that taxis are useful as a ride—if you are going a short distance, a taxi is a good way to get there. But if you are going on a long trip, taxis can be very expensive.

And what our research really shows is that if you open the door to the taxi without assessing whether consumers have the ability to repay, consumers think they are taking a short ride and wind up taking a very long, long journey at great cost.

Mr. HINOJOSA. With response to that, listening to your answer, will the result from the Bureau's rulemaking allow consumers to continue to be able to borrow short-term loans?

Mr. SILBERMAN. Thank you. The result from the Bureau's rulemaking—and I should emphasize that right now, we have not yet even proposed a rule. We have outlined proposals under consideration. But our goal would be that consumers would have the opportunity to get affordable loans. Whether they are short-term loans or not, that is harder to say.

One of the problems is that for folks who need these loans but can't actually repay them in the short-term, longer-term loans may be a better solution. But affordable loans are very much what we are trying to ensure will be available to consumers.

Mr. HINOJOSA. Tell me about the 5 percent option included in the proposed rule. Will it be included in the final rule?

Mr. SILBERMAN. Congressman, I can't answer that question at this time. I can't even answer the question of whether it will be in the proposed rule. We indicated that was one of the options we were considering as a streamlined way of enabling assessments of whether consumers have the ability to repay. But it would be premature for me to speculate what would be in the proposal or the final rule.

Mr. HINOJOSA. Thank you. Ms. Treppa, you note that your Tribe and others have developed lending businesses that have constructed strong regulatory frameworks. How often has your Tribe brought enforcement actions for unfair, deceptive, or fraudulent practices in connection with the transactions that do not occur on trust land?

Ms. TREPPA. Congressman, first, all of the transactions occur on trust land.

Mr. HINOJOSA. Okay.

Ms. TREPPA. Currently, we have a very robust internal compliance regime that ensures that consumers are protected and it is—to date, there have been no enforcement actions against the tribal lenders that we have licensed.

Mr. HINOJOSA. My time has run out. I yield back.

Chairman NEUGEBAUER. The time of the gentleman has expired. And the Chair now recognizes the gentleman from Colorado, Mr. Tipton, for 5 minutes.

Mr. TIPTON. Thank you, Mr. Chairman. And I would like to ask unanimous consent to submit a letter from our AG, Cynthia Coffman, for the record.

Chairman NEUGEBAUER. Without objection, it is so ordered.

Mr. TIPTON. Thank you. Mr. Silberman, I would like to be able to follow up, frankly, on the chairman's question. When we were talking about what gap is to be filled, what need do we have to have your rules issued, I am not sure I heard an answer. What is the gap?

Mr. SILBERMAN. Thank you, Congressman. The gap is that—as I indicated, our research indicates that loans that are made without assessing a consumer's ability to repay wind up creating a great deal of harm for consumers. And we believe there is a need at this point for a Federal regulation which establishes that it is an unfair or abusive practice to make a loan of this type without regard to the consumer's ability to repay.

Mr. TIPTON. So you want to have fairness, but you aren't able to specifically point to anything; it is basically just to be able to write rules as filling the gap?

Mr. SILBERMAN. No, I think quite to the contrary we have pointed to a great deal of evidence in two reports and other studies to identify the harm that we are seeing, and so we think there is a need to establish a principle that—

Mr. TIPTON. Let's look at some of the solutions. You have held roundtables, forums with States, I think you had indicated, seeking it out. You are familiar with what has happened in Colorado?

Mr. SILBERMAN. Yes, sir.

Mr. TIPTON. They have done a good job.

Mr. SILBERMAN. Colorado has made a set of choices.

Mr. TIPTON. Is it good?

Mr. SILBERMAN. It is not appropriate—

Mr. TIPTON. Have they fulfilled those requirements you are talking about?

Mr. SILBERMAN. It would be quite inappropriate for us as a Federal agency to judge what States are good or bad.

Mr. TIPTON. Well, aren't you judging if you are going to start writing rules to preempt them?

Mr. SILBERMAN. We will—Congressman, the rules that we are considering proposing would not preempt what Colorado has done, or what any other State has done. It would add an additional requirement that—the requirement that the assessment be made of the consumer's ability to repay. So that Colorado has said, for example, that the minimum—

Mr. TIPTON. Effectively, we need the Federal Government to step in because Mr. Zoeller and Ms. Treppa don't care about the people who live in their States. Is that what you are telling us?

Mr. SILBERMAN. I am saying, Congressman, that we have an obligation to enforce Federal law. The Federal law provides consumers, all consumers in every State, with protections against unfair and abusive practices. And that is our role, to try and provide that protection which would sit as a floor on which States could add their own rules, like the rules that Colorado has added.

Mr. TIPTON. Like the rules that Colorado has added. Now I would like to be able to cite our attorney general, Cynthia Coffman, in regards to the rules that you want to be able to put forward. She states in her letter to you, "Colorado's extensive experience with these types of measures tells us that such proposals—your proposals—will not work in the real world, if the intent is to preserve access to credit."

That is feedback from the States. That is what they are telling you. You are overreaching. You are overregulating. You are overpromising. But the States are the ones that are actually performing.

Mr. Zoeller, I would like to be able to go and visit with you just a little bit in terms of what you are seeing out of the State of Indiana. In your own experience, do you think that the CFPB, their proposal requires significant changes and that they are going to have a chance of really succeeding for the State of Indiana?

Mr. ZOELLER. Quite frankly, we do have a focus on consumer's ability to pay. And we have kind of a monthly income as the basis of that. So we may not be as, let's say, may not have as much impact.

We do a lot better job than other States, so I defend our State every day. I will say we have stronger consumer laws and some of the space might be better regulated in Indiana, but we are still willing to look and see if we can do it better and—

Mr. TIPTON. Since you are here—I would love to have our attorney general here—tell me, has the CFPB reached out and asked for your advice?

Mr. ZOELLER. We have submitted letters. And they did have a field hearing in Indianapolis on auto loans. But I would say not enough. We really wanted to have much more of a dialogue on what areas in which we are lacking. And I think the chairman's point and other points about where is the gap in coverage is what is missing.

And, again, if there are gaps where we don't have authority, we may need some help, but quite frankly, in Indiana we don't.

Mr. TIPTON. They haven't really had a dialogue with you, as they have indicated that they said they did. I would be interested to know, have they used your personal expertise or data concerning small dollar loans in their proposals?

Mr. ZOELLER. I can't say whether they modeled theirs after mine. Our legislature did have similar hearings, though, and talked about these same areas, and came up with a focus on consumer's ability to pay. But, again, that was our choice, the legislatures that are elected to make those policies. I will always just defend their decisions.

Chairman NEUGEBAUER. The time of the gentleman has expired. The Chair now recognizes the gentlewoman from New York, Mrs. Maloney, for 5 minutes.

Mrs. MALONEY. I thank the gentleman for yielding. I would like to thank all of the panelists for their testimony.

Before I ask my questions, I would like to yield as much time as Mr. Silberman would like in order to finish some of the questions. Regrettably, we are under a 5-minutes rule, and I have noticed that many times you have been cut off because the time is just not sufficient.

I do understand you have quite considerable experience and research in this area, and if there were some points that you were cut off and you could not make, or some statements you would like to make about your research, I would like to yield you as much time as you would like to consume of my 5 minutes.

Mr. SILBERMAN. Well, thank you very much, Congresswoman.

I really think there are three or four points I just wanted to make sure I have made as clearly as I can. The first is that the Bureau has been engaged in a very thoughtful, extensive, data-driven research effort with respect to this product. We have held three field hearings. We have done two research reports. We have had extensive outreach. We have read—I think it is safe to say—the entire academic literature that exists. We have met with scholars in order to come to the place that we are.

Second, as I hope I have made clear, what all that has told us is that if you make a loan like this without assessing a consumer's ability to repay, consumers are put in harm's way, and many consumers wind up in dire situations.

As a result, what we think is needed is a very simple principle, which is really a principle that is pretty well settled and standard practice in most lending industries, that before you make a loan, you should assess whether the consumer has the ability to repay that loan. That is standard practice.

And I would like to just point out that a couple of years ago, 2½ years ago, I had the privilege of testifying on the Senate side, and with me that day was Dennis Shaul, the CEO of the CFSA, the trade association for the payday lending industry. And Mr. Shaul said at that time something with which I profoundly agree. He said that based on his conversations, his members recognize that payday loans as we know them are not likely to survive another 5 years. And that is a quote. And he also said that, "what we need to do is a different and better form of underwriting so we can catch people much earlier who might end up in a cycle of indebtedness."

That is a quote. And that is really the heart of what we are trying to do here. And the final point I would make, Congresswoman, is that we are still in an early stage of this process, not the early stage for research, but the early stage of the rulemaking process.

We have put a proposal—an outline of proposals out for consideration. We spent the last 10 or 11 months listening to feedback. We will put forward a proposal, and that will start another round of communication, and we will take all that into account in finalizing whatever rule we finalize.

Mrs. MALONEY. Thank you. I quite frankly found the research from the Bureau absolutely staggering. One out of every five consumers who takes out a short-term payday loan ends up being in debt for an entire year. I would hardly call that a short-term loan.

But the most interesting finding to me was that only 35 percent of payday borrowers were able to repay the loan when it was due without reborrowing. And I want to ask, is that roughly the percentage of payday borrowers who would be able to borrow under the Bureau's proposed ability-to-repay standard? And has the Bureau to your knowledge done any analysis of what percentage of current payday loans would likely be prohibited under the ability-to-repay standard?

Mr. SILBERMAN. Congresswoman, I think that is somewhat difficult to do, because the lenders today are not getting the information, because they are making loans without regard to ability to repay. It is hard for anyone to know what they would decide if they actually asked that question.

So the fact that 30 percent of the people are able to repay, certainly that would suggest that those people are able to pay. There are also alternatives, such as the kinds of products that Chair Treppa was talking about, which have a longer term, which would allow more people to be able to repay.

Mrs. MALONEY. Your research basically focused on what you called debt traps, which are currently the most abusive practices. But it does not really focus on other practices that might be termed abusive that may not rise to the level of a debt trap.

What is your response to the argument that some people have made that you put too much emphasis on focus on the debt trap as opposed to other traps that are out there that might be causing problems to consumers?

And I for one feel that to catch someone in a neverending circle of debt is one of the most painful things I have ever seen in a person's life. And anything we can do to help them avoid that, I feel is important to quality of life and really economic strength of people in our communities.

Chairman NEUGEBAUER. The time of the gentlewoman has expired. The Chair now recognizes the gentlewoman from Utah, Mrs. Love, for 5 minutes.

Mrs. LOVE. Thank you. I just have a few questions. Mr. Silberman, to what extent did the Bureau analyze the regulation of short-term credit products in the States before designing its own plan or rules to regulate these small dollar products at a Federal level?

Mr. SILBERMAN. Congresswoman, we have reviewed, I think, the laws of all of the States and understand what those States provide. As I have indicated, our obligation, of course, is to assess what is required to implement Federal law, but we certainly are aware of what the State laws provide.

Mrs. LOVE. Okay. So what was it about your analysis of State law that made the Bureau think that State legislators and regulators like those in my home State of Utah were doing a bad job of protecting Utah residents?

Mr. SILBERMAN. What our analysis has told us is that there is a problem, that there are a large number of consumers who are getting loans that they cannot afford to repay, and that is leading to harm, and that there is a need—it is appropriate and indeed necessary to implement Federal law which we are obligated to enforce to make clear that—

Mrs. LOVE. So you did actually look at Utah State laws also and you found problems in our State, also?

Mr. SILBERMAN. We have found a problem in the market. We are trying to address the problem in the market by implementing the Federal law that prohibits unfair and abusive and deceptive acts and practices.

Mrs. LOVE. Okay. So it is my understanding that the CFPB's rulemaking would eliminate some of the commonsense Utah laws and that the Federal law would likely eliminate these important short-term credit options for my constituents. Is that—

Mr. SILBERMAN. The rule that is under consideration—and, again, this is just an outline of proposals, not a proposed rule—would not eliminate any State law, including a law of Utah. We also do not believe it would drive lenders out of business. It would create a level playing field in which affordable loans could be made.

Mrs. LOVE. Okay. I believe that you are only telling—and I think that everyone else here can sense it—part of the story. You are telling one side of the story and you are not telling the other side of the story.

For instance, a young, hardworking, single mom comes home from work—and this is a true story—late at night to find out that her babysitter ran out of formula for her daughter 3 hours ago. She uses her last resort option, goes to her payday loan place, goes to the store, and buys formula for her daughter. What would you suggest that she do? Knock on everybody's door? What would you suggest that she do? Because there are other actors that have used this as a last resort and it has worked for them.

And I'm sorry, but I find it offensive that you would say that people aren't smart enough to make decisions for themselves. And so you have to go into States, you have to go into cities, you have to go into all of these other places to say, trust Washington. We know what is best for you. Trust Washington to make the decisions for you. We know what is best. Don't worry. Your States aren't doing a great job. They don't understand what your needs are. We understand more than anybody else. Have you ever been to Saratoga Springs? Do you know where that is, in Utah?

Mr. SILBERMAN. Oh, no, I'm sorry. I have been to Saratoga Springs in New York, but not in Utah.

Mrs. LOVE. Okay, in New York. Well, have you ever been to Utah?

Mr. SILBERMAN. Yes.

Mrs. LOVE. Yes? Skiing?

Mr. SILBERMAN. No, ma'am.

Mrs. LOVE. No, just visiting? Do you know the people in my districts? Do you know the people who actually use it who have said, thank goodness it was there as a last resort?

Mr. SILBERMAN. We have had the opportunity during the course of our work to hear from many consumers who use these products.

Mrs. LOVE. Have you heard—okay, let me ask you this question. How many people have you heard from who actually have used these products and said they have worked for us, it has gotten us out of a terrible situation, thank goodness it was there?

Mr. SILBERMAN. I'm sorry. I don't know the number offhand.

Mrs. LOVE. You have met with some, right? But I have yet to hear you talk about their stories.

Mr. SILBERMAN. Congresswoman, I think we did indicate from our research which was confirmed by our experiences that there are 30 percent of the people for whom this product works exactly as it was intended, and it enables them to bridge emergency and to get to—and they have the ability to repay.

It is the other two-thirds who don't have the ability to repay for whom we want to create a market in which there are options for them so they don't have to take out the loan and then 2 weeks later find they have to take out another loan because they don't have the money to repay the first loan.

Mrs. LOVE. Okay, so I am going to—I am running out of time. But this is a fair question to ask. And maybe you could just keep it in the back of your head. But is the CFPB doing anything to make sure that consumers of these small dollar credit products have the option at credit unions or community banks to be able to have some of these options, also? Or is it just rulemaking?

Mr. SILBERMAN. Mr. Chairman, may I answer the question? I see that time is up.

Chairman NEUGEBAUER. Yes, the time of the gentlewoman is—

Mrs. LOVE. Yes or no? I just need a yes or no.

Mr. SILBERMAN. Yes.

Mrs. LOVE. Yes? Okay.

Chairman NEUGEBAUER. Okay, thank you. The Chair now recognizes the gentleman from Washington, Mr. Heck, for 5 minutes.

Mr. HECK. Thank you, Mr. Chairman. I would like to direct a couple of questions as time allows to Deputy Director Silberman. I noted that last week your boss gave an interview in The Wall Street Journal in which he indicated that he would encourage credits and credit unions to make short-term loans. I know that NCUA has some longstanding experience actually setting rules for encouraging payday advance loans and on the banking side, FDIC and OCC, another product, deposit advance product.

What I am actually interested in is understanding a little bit about your conversations at the Bureau with other regulators, what you think of their rules, and what changes, if any, you contemplate to how it is they have structured their approach and yours?

Mr. SILBERMAN. Thank you, Congressman. And you are absolutely right that the National Credit Union Administration (NCUA) has adopted provisions for what they call a payday alternative loan to enable credit unions to make a loan that they think works. The evidence is that a significant number of credit unions are taking advantage of that. In the outlines of the proposals under consideration, we indicated that we would allow that to continue as essentially an exception to the general rule.

Mr. HECK. So you would not preempt their approach?

Mr. SILBERMAN. Correct. We have—as you indicated, Director Cordray—we believe that there is an opportunity here for community banks and credit unions who know their customers, don't have the same kinds of expenses that others might have to provide safe, affordable products to their customers and that we are encouraging them—

Mr. HECK. Excuse me, Deputy Director. I apologize for interrupting. But I want to get to the banking side of that question, too, because I think the experience has been a little bit different or the perception in the industry has been a little different than it is on the credit union side. Could you answer the question for them, as well? Or did you mean for it to cover both NCUA and the other regulators?

Mr. SILBERMAN. The proposals that we indicated we are considering would allow any institution, a depository or non-depository, a credit union or a bank, to take advantage, to make payday alternative loans within the parameters of their regulation.

Mr. HECK. And your proposed rule will be explicit in that regard?

Mr. SILBERMAN. I don't want to speculate on what our proposed rule will do. I can say that is what the outline of proposals under consideration says.

Mr. HECK. Secondly, probably lastly, it is my belief that we have a lot of legal products out there that are well used by the vast majority of the population in some instances. But on occasion, there can be a small slice or a slice—I don't want to get into splitting hairs here—whom for whatever circumstances have not used that product well, whether it is their fault or anybody else's fault.

But we have this approach to regulation. You can have a casino, but we have 1-800-BETS-OFF. You can have a bar, but you can't serve somebody if they are clearly inebriated. In some States—Colorado, Washington—you can have a marijuana dispensary, but we have a lot of restrictions on how you can engage in that industry.

And I don't know if this is a fair analogy. I am interested in your response. Are short-term small dollar loans a fair analogy where you have some percent of the population for whom that becomes a problematic usage? And if so, what have we learned from those other industries where we have mechanisms for intervening and helping and the like?

Mr. SILBERMAN. Congressman, the distinction I would draw is that the first question we want to ask is whether that product is safe for its intended use. What our research indicates here is that we have a product that is really not safe for its intended use. It is not simply a handful of people abusing the product, and that we have to deal with that as that kind of problem. It is really we have a product that when this product is made without assessing ability to repay, it is not safe for its intended use. And that raises a very different kind of problem for lawmakers and regulators.

Mr. HECK. Very good. Thank you very much, sir. I yield back the balance of my time.

Chairman NEUGEBAUER. I thank the gentleman. And now, the Chair recognizes the small businessman from Texas, Mr. Williams, for 5 minutes.

Mr. WILLIAMS. Thank you, Mr. Chairman.

Mr. Silberman, in full disclosure, you need to know that I am a car dealer. So you know how I feel about you and your agency, okay?

Mr. SILBERMAN. I remember from the last time I was here, Congressman.

Mr. WILLIAMS. Let's move on, all right? First of all, you keep saying that you have done careful work, but if I heard you correctly when you talked to the chairman earlier, you have never visited a store. Now, how can you claim to understand the market or a business if you have never visited it before?

Mr. SILBERMAN. Congressman—

Mr. WILLIAMS. Make it short, because I have other questions.

Mr. SILBERMAN. I have met with many store operators. My staff has visited many, many stores. We as a Bureau had a consumer advisory board meeting last summer where the entire consumer advisory board, including the Director—

Mr. WILLIAMS. You went on a field trip.

Mr. SILBERMAN. —went to visit a store.

Mr. WILLIAMS. I did that in the sixth grade. Now, I get it. Okay. The other thing is, you talked about how scholars have helped you make these decisions. What the heck is a scholar on payday lending? Who is that person?

Mr. SILBERMAN. There are—

Mr. WILLIAMS. Someone like you who has never been there?

Mr. SILBERMAN. There are many economists who have studied this industry, some funded by industry to do research, some funded by consumer advocates to do research, some independent. We have read all of their research.

Mr. WILLIAMS. I got it. Okay. Let me move on. Section 1022 of the Dodd-Frank Act under standards for rulemaking reads, "The Bureau shall consider the potential benefits and costs to consumers and covered persons, including the potential reduction of access by consumers to consumer financial products or services resulting from such a rule." And, in fact, Mr. Silberman, the Bureau has explicit authority under 1022 to exempt any class of covered persons, service providers or consumer financial products or services from the requirements if statutes are implementing regulations that you are implementing, okay?

In fact, I must tell you, I am proud that, along with those two, I have offered legislation last year that would have helped strengthen that exemption. So my question is straightforward. Do you believe the CFPB has used Section 1022 exemption adequately?

Mr. SILBERMAN. Yes, sir.

Mr. WILLIAMS. Okay. Has the CFPB taken into account the impact of all these new regulations have on financial institutions like community banks, credit unions, and auto dealers?

Mr. SILBERMAN. Yes, sir.

Mr. WILLIAMS. Okay. What about studies that show how these rules like the upcoming payday rule, how they affect the service these institutions are able to give their customers? Have you looked at those studies and seen that customers—the very people you are trying to save—you are hurting them? Do you understand that?

Mr. SILBERMAN. Congressman, we have carefully evaluated the practices in the industry, the effects on consumers, what happens to consumers when you make loans without assessing whether they are affordable, without assessing their ability to repay, and done our best to project the consequences of the proposals that we are considering. We continue to receive feedback and think about that and refine our thinking based on what we are learning.

Mr. WILLIAMS. Okay, question to you. Do you—you and the Bureau—know better than the individual people making the loans? Are you just smarter than they are?

Mr. SILBERMAN. Congressman, we believe that the people making the loans have the capacity and should exercise the capacity to assess whether the consumers have the ability to repay those loans.

Mr. WILLIAMS. Okay, but are you just smarter than they are?

Mr. SILBERMAN. No, not—as I say, we are trying to—

Mr. WILLIAMS. You are advising them?

Mr. SILBERMAN. We are—actually, I would say—obligating them to—before making a loan to assess whether the consumer has the ability to repay. We have complete confidence that is something that can be done efficiently, effectively, and will produce a better world for consumers.

Mr. WILLIAMS. You will help make a better deal for them?

Mr. SILBERMAN. We are not, as I have indicated, trying to affect the price of the product.

Mr. WILLIAMS. Let me just say this to you. I am a business guy. And let me tell you, government—I am telling you, government doesn't create a good deal like you think you are helping your customer. It just doesn't happen. Do you know what makes a good deal? It is competition. It is reputation. It is the private sector that makes the deal.

And the strength of the economy and the ability to realize that we all talk about the American Dream—it is not delivered by you, okay? It is delivered by the people that you actually are hurting. You know, I would tell them, trust the people. Trust yourself. Don't trust the Bureau. Don't trust the government. You see?

All I am saying to you is, I can tell you, because I am living this dream 24/7 in my industry, it would be great if you would back off a little bit and realize that consumers actually know better and the private sector can create the competition, create the reputation that will fix these problems without you all even being involved.

I yield back, Mr. Chairman. Thank you.

Chairman NEUGEBAUER. I thank the gentleman. And now the Chair recognizes the gentleman from Georgia, Mr. Scott, for 5 minutes.

Mr. SCOTT. Thank you, Mr. Chairman.

Mr. Silberman, I am having a bit of trouble understanding why you are trying to destroy small dollar loans. They are much needed. We have 75 percent of the American people who live paycheck-to-paycheck. Americans have emergencies. They have a need for being able to acquire money to fix those emergencies. We have 62 million unbanked and underbanked Americans who do not use the traditional banking system.

These small loans are highly transparent. They require heavy disclosures and compliance with Federal law. They have all received positive feedback from our borrowers. They are monitored by the bank first to determine whether they have sufficient regular cash flow to repay the loan. They have built-in controls to limit the use of the loan. They even have a cooling off period so that customers and consumers do not become overly reliant.

The banks provide clear disclosure of the products. They limit the size of the loan to ensure that the consumer can repay that loan and that they don't get into a cycle of debt. They provide consumers with access to short-term credit, all positive things that are controlled.

Yet, you and the OCC and the FDIC appear to be trying to kill these loans, leaving the consumers with less choice and more expensive options, because without access to these short-term, small dollar loans, it creates a number of consumers who will be pushed out from access.

I have to ask you, with all of this, why? Why are you and other regulators, trying to make it even harder for consumers to make ends meet, to deal with some of these emergencies, by effectively regulating out of business those small dollar loans? Why are you doing that to the American people?

Mr. SILBERMAN. Thank you, Congressman. We are not doing that. What we are trying to do is to make sure that the loans that consumers get are affordable loans, that this is a loan that somebody can repay and still meet their other obligations, continue to put food on the table, continue to pay their medical expenses, and not having to continue to borrow and reborrow and reborrow, because that is what our research tells us is happening today, that a large percentage of consumers who take out these loans—and it is not surprising, if you need this loan, that 2 weeks later, you are not going to be able to repay and walk away.

We are trying to ensure that consumers can get loans that they can afford to repay, and not wind up either in the hands of debt collectors or in the spiral of continuing indebtedness.

Mr. SCOTT. Why are you making the rules or regulations so complex, so complicated? See, the whole point is that, why not make it more convenient? Why are we getting all of this push-back that you are trying to deny Americans from these small loans and that you are doing it by very skillfully putting forward very complex, hard-to-understand, complicated understandings of the rules?

My whole point, Mr. Silberman, is that we as a government oftentimes tend to overextend our efforts in regulation and we wind up hurting the very people who need the help the most. Can you see some room here where you may need to—with all of these complaints, with all of these concerns that we are raising here—that maybe, Mr. Silberman, the CFPB stands back, takes a look, and says, well, no, like you told me, you are not wanting to kill them and put it out of business and stop the American people from doing it, but unfortunately this is the results that is happening. And too many people feel like this, that maybe we can move to address this issue.

Are you willing to do that?

Mr. SILBERMAN. Mr. Chairman, may I briefly respond?

Chairman NEUGEBAUER. Briefly.

Mr. SILBERMAN. We have spent the last 11 months since we put our outlines, our proposals under consideration listening to precisely those concerns, and we are continuing to think about how to best balance achieving our objectives in a way that is cost-effective and that achieves the maximum good.

Mr. SCOTT. Thank you, sir.

Chairman NEUGEBAUER. The time of the gentleman has expired. The Chair now recognizes the gentleman from New Hampshire, Mr. Guinta, for 5 minutes.

Mr. GUINTA. Thank you, Chairman Neugebauer, and I also want to thank the panel for being here today.

I would like to ask a few questions on the impending rulemaking for payday vehicle title and similar loans. I am concerned because as outlined by the Bureau in March of just last year, 2015, there was an acknowledgement that this rulemaking would reduce revenue by up to 70 percent of these short-term, small dollar, community-based credit providers, and potentially even put them out of business.

As we know from the FDIC, 51 million people in our country are either underbanked or have no banking options at all. That is roughly 7 percent of American households who rely on a short-term, small dollar, community-based product to meet their day-to-day, week-to-week, and month-to-month needs.

My question I guess is, how would a hardworking American family manage their money if they don't belong to an institution, if they don't have access to a credit union or community-based bank or larger institution? They rely on products that short-term lenders offer. So that can essentially help them meet their weekly or daily or monthly obligations and hopefully get them in a place where they have greater self-sufficiency.

Pew Charitable Trust recognizes in its research that these products—on these products, most borrowers that leverage these short-term credit products do so because they have no alternative. And that is I think the crux of the issue here. There is no alternative for them.

As I understand it, this rulemaking would restrict millions of Americans' access to the credit on which they rely. I want to ask Mr. Silberman, you started out your testimony and you said the Dodd-Frank Act gives the CFPB plenary authority—you used the term "plenary authority." Plenary means absolute, complete, unlimited authority.

So my question to you is, in Dodd-Frank Title 10, Section 1011, it states that the Bureau exists to ensure that all consumers have access to credit and financial products. I would like to follow up on Mr. Pearce's line of questioning. Can you explain to me on what basis is the CFPB justified and empowered to take steps that are clearly designed to eliminate the access to credit that we are talking about?

Mr. SILBERMAN. Thank you for your question, Congressman. Section 1011 of Dodd-Frank, to which you referred, says that the Bureau's goals are to ensure that consumers have access to financial products and services and that the markets for those services are fair, transparent, and competitive. That is a goal of the Bureau to ensure that these markets are fair. Section 1031 states that we have the authority to identify and prevent unfair, deceptive, and abusive acts and practices.

We are considering exercising that authority based on the research that we have done as provided for in Section 1022, which has identified a market failure, if you will, a problem in which consumers are getting loans that they cannot afford to repay.

Mr. GUINTA. Okay, so how does that line up with Title 10, Section 1027, which—and I have it here—says no authority to impose usury limit. And I will read it very quickly: "No provision of this title shall be construed as conferring authority on the Bureau to establish a usury limit applicable to any extension of credit offered or made by a covered person to a consumer."

That would suggest that you can't set an APR limit, yet that is exactly what this rule establishes. But right here, it says you can't do it.

Mr. SILBERMAN. Congressman, with all due respect, the outline under consideration does not establish a limit. We agree completely that we cannot do so. We have not proposed doing so. We have not contemplated doing so. We will not do so.

Mr. GUINTA. Repeat that. You will not do what?

Mr. SILBERMAN. We will not establish a usury cap, an interest rate limit for these or any other lending products.

Mr. GUINTA. You are not looking to establish a 36 percent APR?

Mr. SILBERMAN. No, sir.

Mr. GUINTA. And you are saying that the CFPB will not under any circumstances move to establish that?

Mr. SILBERMAN. Correct.

Mr. GUINTA. Okay. So despite that, I appreciate that, and I hope that you will hear that, because the concern here is that very issue, that the rule exactly does that. And let's assume for the sake of the argument that does happen. Where do people who are underbanked or are not banked at all, what is their alternative for banking and financial stability?

Mr. SILBERMAN. Mr. Chairman, may I answer? I see—

Chairman NEUGEBAUER. Briefly.

Mr. SILBERMAN. Congressman, the products we are talking about are actually only available to people who are banked. And the goal of this rule is to ensure that there are affordable products available to them, rather than products—

Mr. GUINTA. All right, I appreciate that. But 51 million people are utilizing this who are underbanked or have no banking ability whatsoever. And I yield back the balance of my time.

Chairman NEUGEBAUER. I thank the gentleman. And the Chair now recognizes the gentleman from Texas, Mr. Green, for 5 minutes.

Mr. GREEN. Thank you, Mr. Chairman. I thank the ranking member and the witnesses for appearing today.

I find it quite interesting to say the very least that when we enacted laws in 2007 with reference to our military, the payday lenders were concerned. The argument was that you can't cap interest rates at 36 percent. People can think for themselves. They ought to be able to borrow money at whatever rate we would like to charge.

But Congress decided otherwise. We capped the interest rate for loans to military personnel and their families—2007—people said, payday lenders, we are going to go out of business. You are going to run out of business. If you do this, we won't be able to make loans, and we will go out of business. Congress thought otherwise, apparently. We passed the law that limits what payday lenders can do.

As a matter of fact, there were people who were saying that you can't pass laws that prohibit us from using the car title as some sort of collateral. People can do whatever they want with their property. It is their car. It is their title. Let them do what they may. Why would you do this, Congress? You can't do it.

Congress thought otherwise. Congress did it. You can't do to a serviceperson what you can do to that mom whose child needs milk. You can't do it, Mr. Attorney General, and you know it. Am

I correct? Could you speak a little louder, please? This has to be on the record.

Mr. ZOELLER. That is right. For military personnel.

Mr. GREEN. Yes, for military personnel. You can't do it. Military personnel, they are good people. I support them. I fight for them. I don't think we ought to send them into war and spend billions of dollars and then when they come back home we have to find money to make sure that they get good health care or find money to make sure that they get proper housing. I think that if we can spend billions to put them into war, trillions literally, we can spend that on when they come back.

But I have friends who want to find other places to cut so that we can help them when they come home. I support the military. But I also support people who live in the streets of life who find themselves in need of money and find themselves being taken advantage of. If they are not loan sharks, they are putting a lot of loan sharks out of business, payday lenders.

You are in here. I know you are. I know you are listening. Someone talked about the moral hazard associated with some of the things that we would do to regulate. Where was the moral hazard argument when we did this for our military? Are these folks who are being taken advantage of with these loans that roll over and over and over and over again, paying these extremely high rates, are they not decent red-blooded Americans, too? Do they not deserve the same kind of legislation from this Congress that we did for the military?

No, I don't think the CFPB has to do it. We have the responsibility to do it. And we are not. I don't think the CFPB is engaged in making laws. They make rules to enforce existing laws. Is that a fair statement, sir, Mr. Silberman?

Mr. SILBERMAN. Yes, sir.

Mr. GREEN. Thank you. So now, let's just be real, as we say back in my neck of the hood. Let's just be real. Here is what is going on. You have people on this side who want to protect the consumer. And you have—not everybody, but a lot of people on the other side who want to protect payday lenders. And by the way, they are doing a pretty good job of it.

Payday lenders can and should be regulated. It really is that simple. If we can do it for the military—good, loyal, red-blooded Americans—we can do it for other good, loyal, red-blooded Americans.

I yield back the balance of my time.

Chairman NEUGEBAUER. I thank the gentleman. The Chair recognizes the gentleman from Kentucky, Mr. Barr, for 5 minutes.

Mr. BARR. Thank you, Mr. Chairman. And I appreciate my colleague talking about the need to regulate small dollar, short-term lenders.

In my congressional district, at least, I know that many of these lenders are regulated under Federal law by the Bank Secrecy Act, the Electronic Funds Transfer Act, the Equal Credit Opportunity Act, the Fair Credit Reporting Act, the Gramm-Leach-Bliley Act, the Truth in Lending Act, the Fair and Accurate Credit Transaction Act, the Electronic Signatures in Global and National Commerce Act, the Servicemember Civil Relief Act, and the registration requirement for money service businesses with FinCEN.

In 2010, in Kentucky, our split legislature—Democrat and Republican—bipartisan, working together, in conjunction with a Democratic governor, modernized a consumer lending law, and that was in 2010. The result was the following. A regulation that required a license, limits on rollovers, disclosure requirements, a bond requirement, financial requirements for licensing, capped fees, limits on advanced terms, a maximum loan amount, exam and audit requirements by the Office of Financial Institutions, headed by a regulator appointed by the Democratic governor, Commissioner Charles Weis, who I know who is a very excellent regulator. Limits on—no, allowance for fines against lenders, a prohibition on lender prosecution of customers, and finally, a requirement of background checks and industry experience requirements for those lenders.

Those are the requirements at minimum that apply to these entities in my district. So my question to Mr. Silberman is this: What about these statutes, Federal and State requirements, are inadequate to protect consumers?

Mr. SILBERMAN. Thank you, Congressman. These statutes—all the provisions you cited would continue to be in full force and effect in protecting consumers in your district if the proposals under consideration were finalized. What we would do is add one more requirement, along the lines of what I indicated and Mr. Shaul said we need to do. We need to ensure that in addition, an assessment is made as to whether consumers have the ability to repay the loan.

Mr. BARR. Yes. And do you not believe that the regulators in Kentucky, Commissioner Weis, is he unable to do that under the Kentucky law? Have you analyzed the Kentucky law? And was there anything wrong with the process of a bipartisan general assembly with a Democratic governor passing an update to the consumer protection laws in Kentucky?

Mr. SILBERMAN. I spent last week with Commissioner Weis when we had our field hearing in Louisville on a different subject, and I am sure he is entirely capable of enforcing Kentucky law. We are not talking about enforcing—we are establishing an additional requirement—

Mr. BARR. Right, so I understand, what justifies the Federal Bureau canceling the collective judgment of Kentucky legislators, a governor, and a regulator in Kentucky?

Mr. SILBERMAN. Again, Congressman, we are not canceling that judgment. We are saying that as a matter of a Federal law, there is an additional requirement—

Mr. BARR. I'm sorry, Mr. Silberman. You are a Harvard Law graduate. You understand the concept of conflict preemption. You are canceling the collective judgment of the general assembly of Kentucky.

Mr. SILBERMAN. No, Congressman. What I learned in law school is that we are not doing that at all. If we were to say, for example, that Kentucky cannot require the disclosures that they now require, that would be preempting and canceling. We are not doing that. We are saying there is an additional requirement in addition to—

Mr. BARR. Right. And to the extent—

Mr. SILBERMAN. And that is—that is part of—

Mr. BARR. —the general assembly has passed a law that is inconsistent with that, it is conflict preemption. Let me move on very quickly to the SBREFA process. A constituent of mine felt that their input was completely disregarded in the course of the SBREFA process and that your regulators failed to demonstrate a comprehension of the current very stringent State regulator structure. That constituent wrote you a joint letter and asked—with consent, I would like to submit this letter to the record—my question—

Chairman NEUGEBAUER. Without objection, it is so ordered.

Mr. BARR. —to you, Mr. Silberman, is how significant of the input from the SBREFA process has been included in the rulemaking process? Because based on a FOIA-produced record, it indicates that all of the small business feedback as required by law was completely dismissed out of hand in formulating your rule.

Mr. SILBERMAN. Congressman, we are carefully considering the feedback we received through the SBREFA process. I have read many of the submissions. I attended much of the hearing. Our staff has carefully digested it. That is a valuable input into our decisionmaking process. Anybody who says that we have not considered that cannot make that statement because we have been spending 11 months deliberating since that process, so no one has any basis to say that we are not considering it. We are doing precisely that.

Mr. BARR. It would be very disappointing if this was just checking the box and that their feedback was not incorporated into the final rulemaking.

Thank you. I yield back the balance of my time.

Chairman NEUGEBAUER. I thank the gentleman. Now, the gentleman from Minnesota, Mr. Ellison, is recognized for 5 minutes.

Mr. ELLISON. Thank you, Mr. Chairman, and Mr. Ranking Member.

We all know that competitive markets by their very nature spawn deception and trickery. I am not quoting Bernie Sanders here. I am actually quoting two Nobel Prize-winning economists, Robert Shiller and George Akerlof.

In their new book, "Phishing for Phools: The Economics of Manipulation and Deception"—I recommend that book, by the way—they explain how financial transactions can target people for fraud. And we see it all the time, hidden commissions, illegal kickbacks, steering to higher-cost products. We know that criminals who perpetuate mortgage fraud and price-fixing schemes try to exploit the gaps between Federal and State enforcement to target innocent consumers.

Now, Attorney General Zoeller, on the screen is a quote from a State attorney general, a very wise man. He said, "One of the things that we have learned from a wave of mortgage fraud, price-fixing schemes, and other scams is that white-collar crimes don't occur neatly within a single jurisdiction. They cross State lines and international borders, and the criminals try to exploit the gaps between Federal and State enforcement to target innocent consumers."

The same AG, very sharp guy, said that to fight the ingenuity of these criminals, Federal and State and law enforcement agencies must operate seamlessly without jurisdictional disputes, bureaucratic roadblocks, or inertia. Do you recognize these words, sir?

Mr. ZOELLER. I will pass.

Mr. ELLISON. Well, I do. They are your words.

Mr. ZOELLER. All right.

Mr. ELLISON. You said those things.

Mr. ZOELLER. I wrote them. I didn't say them.

Mr. ELLISON. Yes, well, said them, wrote them.

Mr. ZOELLER. All right.

Mr. ELLISON. You communicated them to the world.

Mr. ZOELLER. No, I will stand by that. I think that is a healthy approach to it. No, it is exactly—

Mr. ELLISON. You are not running from those words, are you?

Mr. ZOELLER. No, absolutely not.

Mr. ELLISON. Good. Because I agree with those words. They are from your November 2009 statement on the interagency task force on fighting white-collar criminals. Now, I just thought I would pull that out to light. Why should—could you just share with me your take, why should abuses in small dollar lending industry not be subject to the same national standard you advocated in 2009? What is the difference?

Mr. ZOELLER. There is a major difference in the markets here. When we are talking about mortgage lending and some of the big banks and the enterprises like that, you are really talking about a different type of consumer. There were some difficulties there.

In the small market, I think what is really missing is you are already talking about people who are underbanked or nonbanked. They are in a different financial position. They may be in stress already. And right next to me is the representative of the loan sharks. So they are not here today, but if we close out this market, that is where people will go.

Mr. ELLISON. Let me ask you this. Thank you for your answer. Mr. Silberman, I wonder, is there any overlap between the person who might go to a payday lender and a person who might have gotten a mortgage on a no-doc, low-doc, ninja loan and gotten defrauded and had false terms put before them before they signed up? Is there overlap between these two different markets? Or are they pretty much mutually exclusive?

Mr. SILBERMAN. Congressman, in truth, I really don't know the answer to the question.

Mr. ELLISON. That is too bad. Okay. You know what? You may not know the answer to the question. I have a feeling that there is a very large degree of overlap to those two bodies of people. I can say that based as a politician who knocks on doors and talks to citizens every single day that when the mortgage foreclosure crisis was banging, a lot of those people who were facing foreclosure actually did go to payday lenders, and there is a tremendous amount of overlap. And I don't agree that there is much of a difference.

Let me just ask you if you know this, Mr. Silberman. I want to thank you and your staff for your important work and the work you are doing to improve the financial marketplace. Specifically, I want to applaud you for considering the rule in payday lending traps. And I hear from constituents, both borrowers and the pastors and imams who serve them, and rabbis, as well, the faith community is in this space and wants to protect people, about the damage of these short-term, high-cost loans.

On the screen is a map of the state of payday loan laws which show great gaps in consumer protections. And I want to urge you to move forward with the proposed rule. I discussed the agency's March statement with my constituents, and we want to ensure that borrowers can realistically be able to repay the loan.

The outline of your payday lending proposal suggests that the rulemaking will include a process for verifying a borrower's income. Could you provide some insight into what that process could look like for small dollar lenders, particularly those with respect to borrowers that are paid primarily in cash? And I think we are low on time.

Chairman NEUGEBAUER. The time of the gentleman has expired. If Mr. Silberman would respond in writing to the gentleman's final question?

Mr. SILBERMAN. I would be happy to do so, Mr. Chairman.

Chairman NEUGEBAUER. The Chair now recognizes the gentleman from Pennsylvania, Mr. Rothfus, for 5 minutes.

Mr. ROTHFUS. Thank you, Mr. Chairman.

For Mr. Silberman, borrowers have diverse credit needs. To meet those needs, there should be a vibrant market with many choices for short-term, small dollar credit. These choices should include credit cards, installment loans, single payment loans, deposit advance loans, and debit overdraft protection services.

Given the small amounts and short terms of loans, banks and other institutions need a simple, streamlined processes to evaluate and provide credit in a manner convenient for customers. I have significant concerns that the Bureau's proposed small dollar lending framework will choke off the ability of banks and others to meet their customers' needs for short-term loans.

Will the Bureau's proposed rule allow banks and other institutions to continue offering short-term loans using simple streamlined procedures?

Mr. SILBERMAN. Thank you, Congressman. Again, I don't want to get ahead of ourselves and speculate as to what the final rule or even proposal will say. What I can say to you is that we have been meeting very closely with representatives of community banks and credit unions. It is not our intention to disrupt the kind of thoughtful, relationship lending that they do, and we will be carefully trying to make sure that we issue a proposal that is respectful of loans that they are making to consumers that are affordable loans for those consumers.

Mr. ROTHFUS. Can you tell me, is there anything wrong with the way that Florida regulates its payday lending industry?

Mr. SILBERMAN. I'm sorry. Could you repeat the question, Congressman?

Mr. ROTHFUS. Is there anything wrong with the way Florida regulates its payday lending industry? And I ask that because the entire Florida delegation, both Republicans and Democrats, across the ideological spectrum, from conservative to liberal, wrote the CFPB expressing concerns about the CFPB rulemaking.

Mr. SILBERMAN. Thank you, Congressman. We have actually looked separately at data from Florida and we find the very same pattern that we find in reports on the Nation as a whole, which is to say a significant percentage of consumers getting loans they cannot afford ending up in long-term cycles of indebtedness so that we believe there is a need to add on top of the rules that Florida has adopted another rule.

Mr. ROTHFUS. Let me ask you this. The cozy relationship between the Bureau and the Center for Responsible Lending has been widely reported. Employees have moved between the Bureau and the CRL during the rulemaking process. There has been extensive communication and coordination between staff. And at one point, the CRL provided the CFPB with an outline of their proposal to regulate small dollar lending so that the CFPB could work to improve it.

In fact, there were so many meetings between the Bureau and the CRL that in an April 2014 e-mail, you remarked that it had been almost 3 weeks since you communicated and that you were "starting to have withdrawal pains."

I think most people would consider this intimate type of relationship to be inappropriate. How do you respond to that?

Mr. SILBERMAN. Thank you, Congressman, for the opportunity to respond. We have throughout this process engaged extensively with stakeholders across the spectrum with advocates, with representatives—

Mr. ROTHFUS. Were there others that you started to have withdrawal pains for not being in touch with them?

Mr. SILBERMAN. I would—if I did not have regular input from any side of the debate, I would certainly feel that I was not doing my job. I have been particularly careful, since I came to this job from an industry perspective, having worked for 12 years, as Congressman Pearce noted, for a financial services firm, I have been particularly careful to make sure that I hear perspectives that are different from the perspectives that I was used to coming to this job—

Mr. ROTHFUS. Do you know whether the Center for Responsible Lending has any affiliates that would provide services that would compete with payday loans?

Mr. SILBERMAN. I understand the Center for Responsible Lending does have an affiliate which is a credit union. From what I am told by the payday loan industry representatives I have spoken to, they don't believe that products of that kind would be competitive with—the credit union product would not be competitive with their product, but they do have products—

Mr. ROTHFUS. You are taking a proposal from the Center for Responsible Lending, where they are in that space of short-term loans or they have an affiliate is, correct?

Mr. SILBERMAN. Congressman, we received proposed outlines suggesting what our proposal should be from many different people from all sides of the issue.

Mr. ROTHFUS. Do you know whether the affiliate of the Center for Responsible Lending does any business in Florida?

Mr. SILBERMAN. I do not.

Mr. ROTHFUS. I yield back, Mr. Chairman.

Chairman NEUGEBAUER. I thank the gentleman.

And now the gentleman from South Carolina, Mr. Mulvaney, is recognized for 5 minutes.

Mr. MULVANEY. Thank you, Mr. Chairman.

Mr. Silberman, let's stay on this same topic. In 2006, our neighbors to the north, North Carolina, banned payday lending outright. Do you think they were right to do so?

Mr. SILBERMAN. Congressman, I don't really feel it is my place to make a judgment of that sort here representing the Bureau.

Mr. MULVANEY. Okay. Neither do I. In 2014, South Carolina passed some laws dealing with payday lending. We allowed it to exist and put certain restrictions on it. Were we wrong to do so?

Mr. SILBERMAN. Congressman, again, I would not want to make those judgments. As I have tried to emphasize, our role is to make sure that all citizens and all States have the benefit of Federal law.

Mr. MULVANEY. I only wish that your Director agreed with you. I just got a letter today from Mr. Cordray that says the exact opposite. It says you do have an opinion. It says, "While these markets are in many jurisdictions subject to State regulation, like South Carolina, we remain concerned that consumers across the country face risk from practices in these markets." So clearly, the CFPB does have an opinion as to whether or not we were right or wrong, for example, to put a 2-day cooling off period in our law in 2013.

Earlier today, you said in response to Mrs. Love that you would not eliminate any State law. You remember that, right?

Mr. SILBERMAN. Correct.

Mr. MULVANEY. You then told Mr. Luetkemeyer that you did not seek to preempt anything and that you are only creating a floor. Do you remember that, as well?

Mr. SILBERMAN. Yes, sir.

Mr. MULVANEY. Okay. The proposal that you have made, at least on your website, is for a 60-day cooling-off period. We have a 2-day cooling-off period in South Carolina. Would you still consider a 60-day cooling off period to act as a floor in South Carolina vis-a-vis our 2-day rule?

Mr. SILBERMAN. Congressman, let me first say that the outline of the proposals under consideration said that after 3 loans in succession, there then would be a 60-day cooling-off period. We would not have—

Mr. MULVANEY. That is fine. And ours says after a certain number as well; I think it is eight. But go ahead. Keep going.

Mr. SILBERMAN. We would view that as a floor. You could add on top of that. You could—

Mr. MULVANEY. A floor. Well, let's think that through. So if I am there in South Carolina and I have taken my third loan, you would now require a 60-day wait period before my fourth and we would require a yes-or 2-day. Do you still think your 60 day is a floor? Or is my 2-day the floor?

Mr. SILBERMAN. I think our 60 day is a floor on which you could add additional protections, yes.

Mr. MULVANEY. Really? Do you really believe that? Or is that just what you were told to say? Come on, now. Because nobody believes that is a floor. It is a ceiling, isn't it?

Mr. SILBERMAN. No, sir.

Mr. MULVANEY. We have a lower threshold than you are suggesting.

Mr. SILBERMAN. It is certainly not a ceiling, since you could have a 61-day or a 70-day.

Mr. MULVANEY. Yes.

Mr. SILBERMAN. It is a floor.

Mr. MULVANEY. And it would be a floor if ours was 61 and yours was 60. Ours is 2. Yours is 60. This is just the English language, Mr. Silberman. It is okay to admit that either you are wrong or you are taking a different position, but you can't call it a floor when your requirement is more restrictive than ours is. If you were to pass a regulation that requires a 60-day cooling off period, wouldn't that preempt my 2-day cooling-off period?

Mr. SILBERMAN. Congressman, I don't mean to be splitting hairs, but I think there is a—

Mr. MULVANEY. I don't want you to split hairs. I just want you to answer the question.

Mr. SILBERMAN. That is what I am going to try and do, sir. I think there is a well-understood definition of what preemption means and that the answer is, no, that we would be establishing a floor. You are certainly right that if a State had a less restrictive rule, our floor would take precedence in that sense. But it would—

Mr. MULVANEY. So if I am not preempted, then I am still allowed in South Carolina—you pass a Federal rule on a 60-day wait period, I have a State rule at a 2-day period. You are taking the position you are not preempting me. It would still be legal for me as a payday lender in South Carolina to acknowledge and abide by the 2-day rule?

Mr. SILBERMAN. You would be obligated under Federal law to comply with Federal law, of course.

Mr. MULVANEY. And it is still your position, as you sit here, that that is not preempting the State law? Do you really—when people look back at your Harvard degree, is that really what you want them to look at?

Mr. SILBERMAN. Yes, Congressman.

Mr. MULVANEY. Okay, good. That is fine. All right. Let me ask you a different question. You said earlier in response to Mrs. Love that in your research, you actually had talked to people who had benefited from, and then other people who had been negatively impacted by, the payday lending system. And you said it was roughly two-thirds, a third in your analysis. I will assume that is the same roughly from State to State. It may be different from various States, but let's just assume for sake of discussion it is the same.

As between you and the legislature of the State of Ohio, who is better suited to balance the interests of those two-thirds versus the third?

Mr. SILBERMAN. Congressman, we have an obligation under the Dodd-Frank Act, under the statute Congress passed to protect all consumers in all States from practices that are unfair or abusive.

Mr. MULVANEY. So it is your belief that you are better suited than the legislature of Ohio to do that balancing act?

Mr. SILBERMAN. It is my belief, our belief that we have an obligation to protect all—

Mr. MULVANEY. So you don't believe that you are better suited?

Mr. SILBERMAN. Congressman, as I said, it is my belief—

Mr. MULVANEY. I am just trying to—I mean, do you believe or don't you believe? Which one?

Mr. SILBERMAN. I believe we have an obligation—we don't make judgments about who is better suited. We make judgments about what our obligations are, and our obligation is to provide the protections that Congress has given.

Mr. MULVANEY. I will look forward to continuing this another day.

Thank you, Mr. Silberman.

Chairman NEUGEBAUER. I thank the gentleman. Mr. Pittenger is recognized for 5 minutes.

Mr. PITTENGER. Thank you, Mr. Chairman.

Mr. Silberman, I am on your right. Welcome. You are the man of the house. And reasonably so. You have a very impressive background. Graduate of Brandeis University, graduate of Harvard Law School, you clerked for Justice Thurgood Marshall. You are esteemed in every respect. You have worked for the AFL-CIO as their general counsel. You are the acting Deputy Director of the largest agency ever created in the history of this country, funded at $600 million a year, with no accountability to anybody.

It is pretty remarkable, your background and really the power that you have. Do you believe, Mr. Silberman, that Big Brother is a good thing?

Mr. SILBERMAN. I'm sorry, Congressman, I missed—I was listening to the biography and I missed the question.

Mr. PITTENGER. It sounded good and it is very impressive. Do you believe in Big Brother?

Mr. SILBERMAN. Do I believe in Big Brother? I am not sure how to answer that question, Congressman.

Mr. PITTENGER. Do you believe that there are those who know best, who are better educated, have more background, better expertise than the common guy and really can help them direct their lives better?

Mr. SILBERMAN. I do not believe that is our role, sir.

Mr. PITTENGER. Do you believe that your policies would convey that? Do you believe—let me ask you this—when you see a Snickers commercial on TV, do you believe people are being exploited when they see that commercial and they want to go eat a candy bar, and maybe that might lead them to a health problem, perhaps diabetes or some other concern?

Mr. SILBERMAN. That is far outside our jurisdiction, sir.

Mr. PITTENGER. But let's follow the train of thought. I wish you would have known my dad, Mr. Silberman. He was a very funny guy. My dad, we grew up in central Texas. And he loved his barbecue, and he loved his fried catfish and his Jimmy Dean sausage with biscuit. Or he would trade off and maybe have pancakes with a lot of syrup and butter. And he lived his life.

And he was told by my sisters occasionally when they could get a word in that, "That is not good for you, Dad. You really need to not be eating those things." And Dad said, "You know, I am really not interested in that. I like the quality of my life. I am not worried about quantity." Dad lived until he was 91.

But he made his choices. And that is what freedom is all about. Do you believe that the American people are entitled to make choices?

Mr. SILBERMAN. Congressman, again, I believe that surely they are entitled to make choices so long as they are protected from situations where they are unaware of the risks, the costs, and they are able to protect themselves. That is what Dodd-Frank tells us—

Mr. PITTENGER. From your opinion, from your point of view, isn't that correct?

Mr. SILBERMAN. No, we try and—that is—

Mr. PITTENGER. No, that is an opinion. That is your opinion, isn't it?

Mr. SILBERMAN. No.

Mr. PITTENGER. That is your opinion? Yes, sir, that is my point. Then you do believe in Big Brother. And I think that is the disconnect between Washington and outside this beltway. The people really want to live their lives. And they are tired of—if I can say this respectfully—elites in Washington who know best how to lead their lives.

And there is an enormous reaction to that today. It is a very compelling statement that is being made. I don't know if you have been out there in the hinterlands to sense that, but people are allowed to make choices with what they want to do with their lives. And what you are saying is, we want to limit your choices because we know what is best for you.

And I think that is the problem, the current—the real fundamental problem that we are dealing with. People have needs in their lives or desires in their lives, and whatever it is, it is their choice. And don't you think people should be allowed the freedom to make choices? When I grew up, I left the umbrella of my family. I wanted to make my own choices. Some were good, and some were bad. But I wanted to make my own choices. Did you have that experience when you grew up and you were ready to live your life? Did you want to make your own choices?

Mr. SILBERMAN. Yes, sir.

Mr. PITTENGER. Okay. Well, let's allow people to make their choices. And that is a fundamental American freedom. And what you are saying is, no, you really aren't allowed to have that freedom because there is a group of us who live up here who really do know what is best for you. And let us determine that for you. That is the mentality that is repugnant to the American people.

Thank you. I yield back.

Mr. PEARCE [presiding]. The Chair would like to thank each one of the witnesses. You have been very gracious with your time and your answers. And you will be excused. We will take a 5-minute recess while we bring the next panel up. Mr. Silberman, if you feel like we have not asked you enough, please feel free to stay into the second panel. Thank you very much.

[laughter]

Mr. SILBERMAN. Can't get too much of a good thing, Mr. Chairman.

[recess]

Chairman NEUGEBAUER. For our second panel of witnesses, we have Mr. Dennis Shaul, chief executive officer of the Community Financial Services Association of America; Mr. Kelvin Simmons, who is testifying on behalf of the American Financial Services Association; Mr. Robert Sherill, a consumer; Dr. Thomas Miller, Jr., a visiting scholar at the Mercatus Center at George Mason University; and Dr. Frederick Douglass Haynes III, senior pastor at the Friendship-West Baptist Church in Dallas, Texas.

Each of you will be recognized for 5 minutes to give an oral presentation of your testimony. And without objection, each of your written statements will be made a part of the record.

Mr. Shaul, you are now recognized for 5 minutes.

STATEMENT OF W. DENNIS SHAUL, CHIEF EXECUTIVE OFFICER, COMMUNITY FINANCIAL SERVICES ASSOCIATION OF AMERICA

Mr. SHAUL. I thank you for the opportunity to speak this afternoon on behalf of my membership and I hope also on behalf of the customers whom we serve.

If I were to sum up our position in a single sentence, it would be that regulation is not decimation. And by any standard that one chooses to look at, whether it is the printed material given out to us on SBREFA or the Charles River study that we have done, this is an intention on the CFPB's part to decimate this industry and lay it to waste.

Now, if the proposal turns out to be less than that, so much the better. In his written testimony, Mr. Silberman is quoted on page 8 as saying—as going on—I know that they are honest, dedicated, hard working individuals, but we have a deep and profound difference with regard to where they are going.

And to put it in perspective, it is a difference both on substance and on procedure. The difference in procedure is what might be called for any athletic fan the "shifting goalposts." When we first met with them, we were told that the object was to do a better disclosure and that would cover things. Obviously, that didn't work.

Then we were told that if we came up with a set of discussions with them, perhaps we could iron things up. Those discussions came to nothing. Then we went through the SBREFA panel, and though Mr. Silberman thinks that it is still being considered, there is not one person who came through that SBREFA panel who believed that their words which went to the question of their continued existence found any hearing from those who represented the CFPB.

And then when we finally get to the point of the complaints that were supposed to be the guiding star, we were told, with regard to payday lending, we find two things—there are very, very few of them, and those that come through are often from States that do not have payday lending, suggesting a couple of things, that the complaint portal is a not very reliable guide, and that people find a way when they don't have legal payday lending in their State to still get the loan.

And, by the way, as an asterisk to that last point, the Administration's late effort to enter into some form of subsidy for private entities that are already partially subsidized, to enter into this field, is not a workable solution for any number of reasons that we cannot get into today, but it establishes one central fact. They finally recognize that this is a demand-driven product, and that is important.

Now, we heard a lot about the ability to repay. Do you really believe that there is anybody who loans money that doesn't seek an ability to repay? The question is this: Is the ability to repay that is outlined in the proposal anything but a sheet that covers up other aspects of what they want to do? Or as one of the writers of the impending rule said to us, you don't understand. The object of what we are doing with ability to repay is to make sure there isn't a second loan. That is not a second loan too close to the first; that is to make sure there is not a second loan at all.

And we heard a lot about how many sequences and so on. Let me show you—and I will make sure that you all get a copy of this—this is from the pages of the CFPB proposal or paper of last March, sequences: 3 loans or less, 64 percent; 6 loans or more, 25 percent; 17 percent for 8 loans or more.

I ask you, when you heard the testimony this morning, did you get a sense that was what we were talking about? Of course we are all concerned about change. This is a dynamic industry, and there will always be change. There will be problems to be fixed, and there are always answers for customers who are not well-served.

But there is not a ready substitute for what we provide. And one of the problems we face with the Bureau is they make no distinction between unlicensed payday lenders, people who are in the business of giving payday lenders online, tribal lenders, storefront lenders. And the differences are profound. We have a set of best business practices and we have lost members because of it.

It is not fair to any of us to equate us with those who go through no regulation at all. And where is the pending rule for those who operate illegally without any regulation at all? It is nonexistent.

I know that I have to wrap up, Mr. Chairman, in a quick way, but let me just say this. The ability to repay construct affords one and only one thing that I think could be construed as novel in looking at the field of how to do an ability to repay, and that is a greater attention to the obligations than individual borrower might have besides his obviously to pay off the payday loan.

Yes, that should be contemplated, that should be made a part of our analysis of ability to repay. But first of all—

Chairman NEUGEBAUER. Mr. Shaul, I am going to have to ask you to wrap up.

Mr. SHAUL. Yes, I will wrap it up. But it is, I think, amazing that anyone at the Bureau believes that our operators do not do a rather rigorous job of working out an ability to repay. They don't continue in business unless people pay off these loans.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Shaul can be found on page 80 of the appendix.]

Chairman NEUGEBAUER. I thank the gentleman.

Mr. Simmons, you are now recognized for 5 minutes.

STATEMENT OF KELVIN SIMMONS, TESTIFYING ON BEHALF OF THE AMERICAN FINANCIAL SERVICES ASSOCIATION

Mr. SIMMONS. Good afternoon, Mr. Chairman, Ranking Member Clay, and Ranking Member Waters.

My name is Kelvin Simmons, and I am here on behalf of the American Financial Services Association (AFSA) and the millions of traditional installment loan customers that AFSA member companies serve and they have served over the last 100 years.

Thank you so much for giving me the opportunity to talk about the Consumer Financial Protection Bureau's proposal for small dollar loans and the impact it could have on deserving consumers.

I ask that my full statement be submitted for the record so that I can focus on three basic issues: one, the need for small dollar credit; two, the fact that depository institutions are not equipped to address that need; and three, the demonstrated ability of traditional installment lenders to offer safe and affordable access to small dollar loans.

On my first point, there is a need for small dollar credit. And let me paint a picture of my experience in the community that I come from. I was born and raised in Kansas City, Missouri. I am a former State Director of economic development for the State of Missouri, and during my tenure, the State's banks, credit unions, and financial services divisions were under my executive authority.

I was president and CEO of one of the largest community development corporations in Missouri, and also vice president of one of the largest FQHCs in the State of Missouri. I also was elected twice to serve on the Kansas City City Council.

In the community that I came from, particularly in the ZIP Code that I came from, there were no locations in that area where I grew up that offered safe, reliable, affordable, small dollar loans. I characterize this as living in a community that had a financial services desert.

To further illustrate my financial services desert point, I served as the commissioner of administration for the State of Missouri from 2009 to 2012. In that role, I had dual signatory authority with the Missouri State treasurer to issue all checks on behalf of the State of Missouri. Even though my name appeared on all of those checks, there was not one bank in my hometown ZIP Code where I could even deposit those checks.

There is a need for small dollar credit because it is inevitable that a car will break down, things will happen, emergencies will occur. There is also a national need that has been recognized by CFPB Director Richard Cordray who testified last fall about preserving the ability of installment lenders and others to continue to make responsible loan products.

On my second point, depository institutions are not equipped to make those small dollar loans. And despite their effort, there have been studies, there have been pilot programs to encourage banks to lend in this space. The FDIC found that banks do not see small dollar loans as a profitable business line.

I have had an opportunity to work with one of the largest African-American-owned banks in Kansas City that is based out of New Orleans, Louisiana, Liberty Bank. They do a wonderful job of loaning to their customers. But this is one of the issues that they said was very difficult and they participated in the pilot program with the FDIC. They contended that it is difficult: They could do it, but it would require subsidization in order to be able to do that. And so it made it very difficult, even as it is a very good community bank.

So the question is, who is best suited to meet the need of high-quality small dollar loans? My answer is the third point, traditional installment lenders that offer safe and affordable small dollar loans. What are the installment loans, traditional installment loans? They are fixed-rate, fully amortized, small dollar loans repaid equally in monthly and payment installments. These loans are affordable and they basically give an opportunity for the borrower to meet their monthly budgets.

There are plain-vanilla loans, transparent, easy to understand terms, due dates and payment amounts. Installment lenders underwrite the loans based on consumer credit reports and other factors. The Center for Financial Services Innovation has published a guide outlining the characteristics of high-quality loans. Those characteristics which include ability to repay, opportunity to improve a borrower's financial health, transparency, accessibility, those are the kinds of characteristics.

I was in Los Angeles in December of 2015, and the National Black Caucus of State Legislators adopted a resolution, which is also in my full statement, endorsing the development of responsible underwritten small dollar loans.

We understand the CFPB concerns about trapping borrowers in the cycle of debt, but traditional installment loans, again, are fully amortized loans and paid off in equal payments in principal and interest over a period of time. I see that my time is coming to the end, so I will go to the conclusion.

In conclusion, I hope that I show to the members of this committee that there is a great need for high-quality, small dollar loans in communities like the one that I came from. Traditional installment lenders meet the definition of that high-quality, small dollar loan, and I hope that more importantly, the CFPB will be careful to preserve the ability of installment lenders to offer these responsible loan products.

Thank you. I look forward to any questions that you may have.

[The prepared statement of Mr. Simmons can be found on page 103 of the appendix.]

Chairman NEUGEBAUER. Mr. Sherill, you are recognized for 5 minutes.

STATEMENT OF ROBERT SHERILL, CONSUMER

Mr. SHERILL. Good afternoon, Mr. Chairman, and members of the committee. My name is Robert Sherrill, and I am here to give a consumer's perspective on this policies and stuff. I am not a policy guy or I am not a lobbyist or anything like that. I am just coming from the ground where it is really happening.

I have used these loans before. I went to prison, made some mistakes. Nothing violent, but I chose to get money in an illegal way. I got out. And when you are a felon, the odds are stacked against you. You can't get jobs. My family doesn't have money like that. So to call someone that I am related to, to get money is out of the question.

The alternative to that scenario is going to payday loans. I know a lot of people who utilize this service to cash their checks. I did it myself. I still do it from time to time. I have utilized getting the loans when I didn't have the means to get money. And my concern is, when they take it away, what are we going to do? Because from the looks of it, I don't see anybody here who looks like they need a loan from a payday place.

So me personally, I am on the ground. We need it. When the odds are stacked against you and you don't have anybody to call, what do you do? Has anybody here ever experienced that feeling? Because it is not a good feeling when, no matter where you turn, you have nowhere to go. And so, those places offer an alternative for us. And I will continue to use them, as will a lot of people I know use them, as well.

[The prepared statement of Mr. Sherill can be found on page 91 of the appendix.]

Chairman NEUGEBAUER. I thank the gentleman.

Mr. Miller, you are now recognized for 5 minutes.

STATEMENT OF THOMAS W. MILLER, JR., VISITING SCHOLAR, MERCATUS CENTER, GEORGE MASON UNIVERSITY

Mr. MILLER. Chairman Neugebauer, Ranking Member Clay, and members of the subcommittee, thank you for the opportunity to appear today.

A heated debate has surrounded consumer credit for many decades. Because banks do not make small dollar loans to consumers with damaged credit, the marketplace has responded with an array of small dollar loans. Americans who rely on these products are not wealthy and many live from uncertain paycheck to uncertain paycheck.

People who make regulatory decisions on behalf of these consumers are likely well-intentioned, but sometimes they might not fully understand how small dollar loans can help borrowers who are facing difficult financial circumstances. In my scholarly work on consumer credit, I seek to understand how small dollar loan markets work and how to restructure regulations to improve borrower welfare.

Access to credit is a fundamental freedom for all Americans. But our research shows that consumer credit regulation often reduces this freedom.

My testimony contains three main points: one, the small dollar loan market is diverse because consumers have diverse needs; two, eliminating credit supply does not eliminate credit demand; and three, States can provide more credit options for consumers by increasing or even eliminating interest rate caps.

Point one, the small dollar loan market is diverse because consumers have diverse needs. As noted in my written testimony, consumers generally know how to obtain small dollar loans and they generally understand the terms of these loans. In my experience, however, many people with good credit are not familiar with small dollar loans. It is incumbent, therefore, on anyone regulating, advocating, or studying any small dollar credit product to know the differences among them. My written testimony explains the basic workings of four types of small dollar loans. Importantly, these loans are not perfect substitutes for one another. These loans differ significantly in terms of loan size, length of loan, cost, repayment method, and underwriting processes.

Point two, eliminating credit supply does not eliminate credit demand. The CFPB is currently exploring new payday loan rules that could dramatically reduce the number of payday loans. Without a thorough exploration of why some consumers often use payday loans, the CFPB proposes to set a limit of six payday loans per consumer per year. Such an arbitrary rule would eliminate 60 percent to 80 percent of payday loans made. Where will payday borrowers go for credit?

Eliminating so many payday loans does not mean that consumers will magically stop borrowing or suddenly begin to borrow from other legal lenders. Instead, such a regulation could force some consumers already in desperate situations toward illegal lenders. Where is the compelling and convincing independent, rigorous research that shows repeated payday borrowing is, in fact: one, harmful to consumer welfare; and two, that a limit of six payday loans per consumer per year will do more good than harm?

Point three, States can provide more credit options for consumers by increasing or even eliminating interest rate caps. In the early 1900s, consumer credit reformers battled illegal loan sharks by appealing to legitimate capital. At the time, reformers decided that costs and risks of making small dollar loans merited an APR of about 36 percent, which was six times higher than prevailing interest rates at the time. By 1940, most States had adopted a form of the uniform small loan law of 1916.

The model law had urged that any rate cap set "should be reconsidered after a reasonable period of experience with it." Clearly, the succeeding 100 years exceeds a reasonable period.

Figure three of my written testimony, however, shows that 37 States still have rate caps at or below 36 percent. Nine have no rate cap. Policymakers of today would be wise to follow the innovative thinking of reformers in the early 1900s by dramatically revising or eliminating the 36 percent interest rate cap.

Figure one of my written testimony shows the results of a low interest rate cap. A legal loan desert can exist. There is demand but no supply. In 1916, installment lenders could make a profit on a much smaller loan than they can today. Why? For any set of loan terms, the revenue is the same now as it was then, but production costs are much higher. Figure two of my written testimony shows the CPI is about 20 times higher today than it was in 1916.

Let's look at a $500 loan. To bring installment lenders into this loan space, the allowable APR would likely have to be at least twice as high—that is, 72 percent—or even higher perhaps. APRs of 36 percent and 72 percent sound jarring, so let me put them in dollar terms.

Increasing the APR from 36 percent to 72 percent on a $500 6-month installment loan results in a monthly payment increase of $9.38, or $2.35 per week, the price of one big regular coffee. Consumers would willingly pay this small amount if the alternative is no loan or a loan product that does not suit their needs. Having more freedom of choice benefits consumers.

Thank you. I stand ready to answer any questions.

[The prepared statement of Dr. Miller can be found on page 73 of the appendix.]

Chairman NEUGEBAUER. I thank the gentleman. And, Dr. Haynes, you are now recognized for 5 minutes.

STATEMENT OF FREDERICK DOUGLASS HAYNES III, SENIOR PASTOR, FRIENDSHIP-WEST BAPTIST CHURCH, DALLAS, TX

Mr. HAYNES. Thank you so much. Thank you, Mr. Chairman. And to all of you, our public servants and Ranking Member Waters.

My name is Frederick Douglass Haynes, III. Several of my colleagues in pastoral ministry and I became alarmed as buildings once occupied by thriving restaurants and bank branches were taken over by payday and auto title loan stores. In the last 10 years, right there in Dallas, 20 payday and auto title loan shops opened within a 5-mile radius of our churches. Many of these stores are located right next to each other.

A community that was already suffering as a food, job, and opportunity desert was and is being overrun by these predatory stores. It appeared that our underserved and underbanked community was being intentionally targeted for these high-cost, debt trap loans.

Our concern was confirmed as we heard from members of our churches and residents in the community who were financially held hostage by these "loans." They confessed that in a situation of desperation they had sought to get a loan that eventually became a trap. They made payments, every other week or monthly, only to get deeper in debt. They were in a financial hole, and upon getting a payday or car title loan, received a shovel instead of a rope.

As a pastor, my heart went out to many who were victimized by these predatory practices. I will give you two case studies that are testimonies of persons who experienced this debt trap. A recently widowed 70-year-old grandmother took out a $300 loan. She ended up paying $800. She has always been fiscally responsible, but as you know, life happens, and she had to take out this loan. She paid back the loan in full, but she had to roll over the loan several times, ultimately paying much more in interest than she borrowed.

I am representing a 23-year-old college student. Both of his parents passed away, but he is determined to get his education in honor of his parents. He needed to purchase books for his classes. What was a $300 loan ended up costing him over $600. I could go on and on.

Suffice it to say, all of them were hoping for a life preserver, but they received shackles instead. Payday loans in Texas carry rates of 500 percent annualized interest. Car title loans are in the range of 250 percent to 300 percent APR range. The Texas Office of Consumer Credit shows that 61 percent of balloon payday loans are refinance loans that are taken in order to repay the previous unaffordable loan. Every week, car title loans result in 847 car repossessions. That is immoral and unethical and unacceptable.

A resident of our community shared with me that he had a car title loan that began as a $4,000 loan. The car was repossessed when he couldn't escape the debt trap, but ended up paying $8,200 in the process, and he still doesn't have a car. A coalition of churches and community groups sought to close the loophole in the State usury law in Texas that allows these businesses to charge over 500 percent in interest, but we were unsuccessful.

We were undaunted and determined to free our community from these predatory practices, and so as a consequence we petitioned the city government in Dallas to rein in the destructive dealings of the payday and car title lenders. Our church has taken a step to be a solution to the problem, which is symptomatic of a larger problem of greed and economic exploitation, which has produced a widening wealth gap that threatens the fabric and future of our nation.

We have launched a credit union, partnering with another church in our community, that held a Federal credit union charter. We now have several years of banking experience, and we now offer Liberty Loans, microcredit to members in need who are able to afford small dollar loans. We offer loans of up to $500 for 6 months at 28 percent annual interest, and 19 percent interest for members with a reasonable application fee.

The good news is there has not been one defaulted loan, and all of those who are benefitting from this loan are paying the loan back on schedule, because they can afford it. A novel concept. It is good business. It has empowered the powerless. And it is moral.

We are taking strides toward economic freedom in Dallas, but we still have a long way to go, not only in Dallas, but across the Nation. We want access to credit. But it must be quality credit. Anything less adds to the stress of the desperate and the needy.

Well-crafted and compassionate legislation can weed out the predators and enable responsible and reputable lenders to thrive while rendering a helpful service to communities in need. We don't want Jesus to say in the judgment, I was hungry and thirsty and you gave me a payday loan.

[The prepared statement of Dr. Haynes can be found on page 70 of the appendix.]

Chairman NEUGEBAUER. I thank the gentleman. They have just now called votes, so I think what we are going to do, now that the panel has given their opening statements, is we are going to ask you to be patient here. I am not sure exactly how many votes; we have one vote. And so, I would ask Members to go over and vote as quickly as you can, and then we will come back and reconvene.

So at this time, we are in recess subject to the call of the Chair.

[recess]

Chairman NEUGEBAUER. The hearing will come to order. Before I close, I want to make a correction here for the record. Mr. Simmons is testifying today on behalf of the American Financial Services Association and not the law firm, Dentons. So for the record, we are correcting that. Thank you.

I now recognize myself for 5 minutes to question the panel. And first of all, panel, thank you for your patience. Every once in a while, we have this little constitutional responsibility across the way there that we have to go over and do, and people that we represent kind of appreciate that.

Well, Mr. Sherill, you have a great story to share. Your testimony was very compelling. You mentioned you had a tough time accessing credit when you got out of jail. When you got out of jail, they didn't send you a credit card?

Mr. SHERILL. No, sir. They gave me about $30 and sent me on my way.

Chairman NEUGEBAUER. When you said, okay, I have to have some money, I have to get my life started here, kind of share with me, how did you go shopping for different places that made these kind of loans looking for the best deal or the good terms? Or can you kind of just walk us briefly through that?

Mr. SHERILL. I went to a traditional bank, like a Regions, and tried to open up an account. I was really there for a loan, not an account. But they didn't give me a loan. They said they don't offer short-term lending and things like that.

So I went to another bank, tried them out. I went to a credit union, and they didn't do it. You have to have an account with them. I didn't have time for that. I needed it right then. And so in my city, I went to one of the bigger payday lending places, and they gave me a loan.

Chairman NEUGEBAUER. And did you look at the conditions of the product? Did you think the product was fair? You asked them what the terms—it was very transparent what your costs were?

Mr. SHERILL. With the place that I go, they are strenuous. You just don't go in there and say, hey, I need a loan and they give it to you. You have to—it is protocol that you have to meet. It is criteria. And it is a protocol that is followed after you meet that criteria.

You know, make sure you aren't this, make sure you are that. Sign here. Are you clear on what they explain to you, and you sign it. So after that, then you understand what they are giving you. And if you choose to accept, then you choose to accept.

Chairman NEUGEBAUER. Yes. I think you shared something with our folks when we were interviewing you, and I think one of the questions that was asked of you was, what would have happened if you couldn't have gotten a payday loan?

Mr. SHERILL. Like I said, I had no other option. It is different when you have options. So people who sat around—I could have called my grandparents or something like that, I had no other option. And if I wouldn't have taken that alternative, then I would have maybe had to go back to the streets, because that is what I knew. And I knew I could get it that way. But I am trying to change my life, and that isn't the way I wanted to go.

Chairman NEUGEBAUER. You have heard some of the testimony in the first panel that—did you feel like that you were being taken advantage of?

Mr. SHERILL. Not at all. I am 32 years old, and I am very competent. So I went in, and they explained it to me: You pay this. If you don't, then the interest rates are going to go up, if you don't pay back on time. And I understood that. I needed to borrow it for a while. Two weeks later, I paid it back. Probably I think one of the first time I borrowed like $250. I paid like around about $280 back, maybe somewhere in there, which wasn't bad, because it met my need at the time, so I needed it. So I would do that today if I had to.

Chairman NEUGEBAUER. I think in one of the comments—I don't know if it was in your testimony or not—but you have started your own business now. Is that correct?

Mr. SHERILL. Yes, I am a minority-certified company with the governor's office of diversity, with the Better Business Bureau, and I am with the National Chamber of Commerce now. I started my company from the ground up, due to loans from these type of places. So it works for me.

Chairman NEUGEBAUER. And I think you mentioned that you even from time to time still have used that to supplement your working capital in your business. Is that right?

Mr. SHERILL. Yes, I currently use that now. I employ 20 people now. And some of them use the payday loan places to cash their checks and get money orders and pay their bills.

Chairman NEUGEBAUER. You heard the gentleman from the CFPB say that this product is hazardous. Did you find it hazardous?

Mr. SHERILL. No, because I heard all the testimony today, and no one is producing a better alternative. It is easy to come in here and say, this isn't going to work, that isn't going to work, but not one person has said, okay, we are going to implement this instead of that and it would be better. No one is doing that. So, no, it is not hazardous.

Chairman NEUGEBAUER. Dr. Miller, you have written extensively on consumer demand. Does the demand go away if the product goes away?

Mr. MILLER. No, sir. Demand will still stay for credit. And people will seek out sources for credit.

Chairman NEUGEBAUER. I see my time has expired. I now yield to the gentleman from Missouri, the ranking member, for 5 minutes.

Mr. CLAY. Thank you, Mr. Chairman. And let me thank all of the witnesses for being here. In the interests of full disclosure, let me mention that I have known Mr. Simmons for over 25 years, so it is good to see you.

In part of your testimony, you talked about the need, Mr. Simmons, for high-quality small investment lenders, and the need was there. What has been the experience of people in your community when they go to a traditional bank? What do you think happens to them that the industry that you represent is able to fill this void? What are you—

Mr. SIMMONS. Congressman, there are a couple of different things with that question. One is the traditional installment lending industry has certain characteristics that are different than the other industries and the other products that have been discussed.

With respect to the traditional installment lending industry, again, it is a fixed-rate, fully amortized, small dollar loan paid off equally in monthly installments over a period of time. So that is a different product than what was discussed with respect to payday a loan or a title loan, which in some of the cases you are looking at collateral either being bank account or the vehicle itself. And so that is vastly different.

What I have found in my experience in the community that I come from that I talked about in my testimony is that there are oftentimes where those establishments are not in the community. And what that is simply saying is, in some cases, they may be outside of the ZIP Code that I was discussing with you. I am from 64130 in Kansas City, Missouri.

Interestingly enough, we have a municipal ordinance that does not allow certain products to be in certain places within the community. Kansas City is one of those places that has a municipal ordinance that does not allow payday, title, or installment loan places to locate there if you are not already there.

Mr. CLAY. I see.

Mr. SIMMONS. And so, it cuts that off.

Mr. CLAY. Thank you for your response. Reverend Haynes, if I may, the core of the CFPB small dollar loan proposal is to require a lender to check if the borrower has the ability to repay the loan. This seems like commonsense and standard practice in all other types of lending. Since some lenders seem alarmed by this rule, we can only assume that some of them are not doing this now. Can you share your experience and impact on communities around your churches when loans are given without considering an ability to repay it?

Mr. HAYNES. Yes, thank you very much. First of all, to have—as I shared earlier—some 20 car title and payday loan stores in the last 10 years to literally target and saturate our community and then to see the impact upon members of the community who in a desperate situation applied for such a loan and then found themselves 7 months—I have even seen one for 10 months they were trying to pay back a loan because of rollovers.

And so, of course, that has an impact on the family. It has an impact on the community. And let's be honest, if you were driving through our community and you saw payday loan stores next to each other, and you were looking to invest in that community, it is highly unlikely that you are going to see that as a wise investment.

So in a real sense, the predatory nature of it has a tendency to not only impact in a negative way those families, but worse than that, the community becomes not only a food and job desert, but now it is an opportunity desert.

Mr. CLAY. What does that say about the banking industry? Apparently, there are obstacles here for people to get checking accounts. What does that say about the U.S. banking industry?

Mr. HAYNES. That the banking industry has a lot of work to do to expand options. One of the things that Brother Sherill said was that he had no other options. That is a sad statement on our democracy that he has no other options. And I think that justice is about expanding options, as opposed to narrowing options, especially to options that are the same principles that got us into the financial crisis that we as a Nation just got out of. And the sad reality is, these are the same principles going on, but they are targeting communities that historically have been denied opportunity.

Mr. CLAY. Thank you. My time is up.

Chairman NEUGEBAUER. The time of the gentleman has expired. The Chair now recognizes the gentleman from New Mexico, Mr. Pearce, the vice chairman of the subcommittee.

Mr. PEARCE. Thank you, Mr. Chairman. I appreciate each of you being here.

Dr. Haynes, I found myself earlier in your testimony wondering why you all didn't offer the product yourselves. And so then I was deeply gratified when you got to that point of the discussion that you did expand and go into doing the loans, which is the key to expanding opportunities, is competition.

So my question is, have you seen a decrease in the number of payday lenders in the neighborhood? In other words, you mentioned the 20 in the 5 square miles around the church. Has that decreased as people choose the lower interest and the better service with the church there?

Mr. HAYNES. I can say that the payday loan store that opened 5 years ago down the street from the church is closed now. So that is a good sign for me. As a matter of fact, it is going to be a restaurant now.

Mr. PEARCE. Just how many loans would you say that you are servicing now through your church program?

Mr. HAYNES. Oh, wow.

Mr. PEARCE. A hundred, a thousand, ten thousand? In other words, what kind of expansion of the market have you seen for—

Mr. HAYNES. Again, we are new in the microloan department, and as a consequence, I would say it is in the number of about 100 to 150.

Mr. PEARCE. That is fair enough. That is pretty significant in a new start-up. And I am serious to think other churches should be looking at this as a way—it really is a problem when you start passing laws. You get rid of the good as well as the bad. And when you offer competition, then the bad will go away because there is a better alternative. And so I worry about—you had said that justice is expanding the options, not limiting them, and yet the thing that the CFPB is set on doing is going to limit the opportunities and—so I think that the better option is the competition drives the bad ones out of business. So, again, I compliment you.

Just one small note. I noticed that you talk about the 20 percent annual interest rate. And when you are talking about the payday lenders, you talk in terms of APR. Now, how much is the origination fee that you mentioned there?

Mr. HAYNES. The origination fee?

Mr. PEARCE. Yes, you say there is an administrative fee with your 28 percent. So what would that be?

Mr. HAYNES. Oh, that is very minimal. I don't have that figure with me right now.

Mr. PEARCE. About $20 bucks?

Mr. HAYNES. Pardon me?

Mr. PEARCE. Ten bucks or twenty bucks?

Mr. HAYNES. Ten bucks max.

Mr. PEARCE. Okay. But you see the difference there. Your APR suddenly went from 28 percent to 38 percent if it is $10, and so that is, again, from this side, it could be considered a minor point. But just compare apples to apples, if you would.

Mr. Sherill, you heard earlier in the previous testimony the abusive practices that the one witness kept bringing up. Did you find those abusive practices that tried to string you out if you borrowed $500? I don't know what you borrowed, and I am not really interested. Did that string out to where you ended up paying back $10,000 for a $500 loan? You have heard that kind of—

Mr. SHERILL. Well, those are exceptions. There are a lot of people who use this product responsibly, like myself. You know, I wouldn't be here.

I feel that if you borrow money, it has to be a need. So if you borrow it, you already have the means to an end, because you are thinking, okay, I have to pay it back. So me, I am thinking when I get paid, I am going to pay it back. And that is the only reason I think you should get one.

Now, if you get one with no end in mind, then you are asking for the hiked fees and stuff like that. It is not meant for a long-term way of life. It is meant for a quick fix, you pay it back, and you move on.

Mr. PEARCE. So to an extent, you are saying that personal responsibility says that the product works pretty well if I use it responsibly, but if I don't take care of my obligations, then, sure, it can string out and out and out. But you didn't find it to be some guy sitting there with a green eyeshade on stringing you out and keeping you where you couldn't quite reach the goal.

Mr. SHERILL. I relate that to anything in life. If you use it responsibly, then it is a good thing. But you can abuse anything. We can abuse alcohol. We can abuse whatever—anything that is usable, we can abuse, basically. And this is just one of those things. If you use it responsibly, it will work for you.

Mr. PEARCE. And, by the way, I compliment you on your story, because it is a story that needs to be told to the Nation. We have a lot of people out there who have made mistakes and never recover from it. They don't have your drive and discipline. So my hat is off to you.

Thank you very much. I yield back, Mr. Chairman.

Mr. SHERILL. Thank you, sir.

Chairman NEUGEBAUER. I thank the gentleman. And now, the gentlewoman from California, Ms. Waters, the ranking member of the full Financial Services Committee, is recognized.

Ms. WATERS. Thank you very much. I first would like to take a moment to thank Dr. Haynes for being here. I know how busy you are and how you are in demand all over the country, and that you were in California last night, and you flew in here and you have waited all day. And I want you to know, I truly appreciate that and the work that you are doing with the other ministers in this country who are focused on this issue and who are creating opportunities.

I have been to Dallas. I visited one of your community days. And I saw how you brought all the resources from all over to be at the community day where people can have access to information about services, and I know how hard you work. I am very appreciative for you. Thank you so very much.

Just quickly, when I first started today to talk about setting the tone and helping to create the picture of what we are dealing with, I will just quickly go through again the pain that is being fostered on certain communities and certain people in this country. Predatory lending almost destroyed many communities. And the home foreclosure problem was terrible. And these people who were victims of predatory lending were trying to live the American Dream, only to discover that they had signed on the dotted line for mortgages they could not afford. And when the devil came due, and the interest rates were increased, on and on and on, they lost their homes.

We are still dealing with that. And the hedge funds are coming in and they are buying them up, and now we have a lot of people who are paying 50 percent of their income for rent because a lot of the foreclosed properties have been bought up by hedge funds and speculators. And they are not selling them; they are renting them and raising the rents, et cetera. Homelessness in the Los Angeles area alone increased by 12 percent, and in the overall county, about 20 percent, and it is exploding all over the country.

In addition to that, we are fighting these private, post-secondary schools who advertise on television that you can get degrees and diplomas and they could help people have careers, and people take out these loans only to find out the schools are just ripoffs. We closed down Corinthian. There are a lot of others that we have to go after. But we are confronted with that.

In addition to that, when you pile on top of that, the payday loans that are in targeted communities, the rent-to-owns where people are losing their cars, it is overwhelming almost. And so for each of these, those of us who work very hard on these issues are determined that we are going to create some change.

Now, we never said we were trying to put people out of business. We raised the question, why can't you, Mr. Simmons, have loans at 36 percent, as we are doing with veterans? Why do we have 400 percent, 500 percent, 1,000 percent in these loans? Why can't you do 36 percent?

Mr. SIMMONS. Congresswoman, with the testimony that I provided earlier, when the FDIC had its pilot program with respect to bringing the banking institutions into this particular space, a number of those banking institutions, as you will find with other financial institutions, said the 36 percent was very difficult to lend, given the numerous things that they have to deal with, the cost, the labor issues, a number of those issues. And so, credit unions were in some cases asked to do the same thing. And it was very difficult to do.

Ms. WATERS. Okay, I don't want to cut you off, because I know that story about the overhead being so much that they could not afford to do it. But just as they have done it with the veterans, they are making out. They are making money. And we are experimenting with some credit unions. Kinecta, for example, has joined with payday loan operation in Los Angeles where people get involved. They are banking the people. They are charging less. They are doing some financial literacy, on and on and on.

So I and many others are not saying we want to put you out of business, but we are not going to stand by and allow yet another what I consider unfair ripoff to people who can least afford it. And so I want you guys to think about it. I want you to think about why—for example, you said that in your own community, they don't allow payday loans. Why do you think they don't allow payday loans?

Mr. SIMMONS. Congresswoman, in the community that I come from, the municipal ordinance that was put in place was to stop the proliferation of what the council at that time considered predatory practices.

Ms. WATERS. Okay, that is good. And that is why 15 other States have basically either said you can do no more than 36 percent and if you don't, if you can't live with that, get out, we don't want you at all. But there is a reason why your municipality has prohibited the proliferation, as you would call it, and there is a reason why 15 States are denying payday loans the opportunity to operate in the way that they do.

So with that—

Chairman NEUGEBAUER. The time of the gentlewoman has expired.

Ms. WATERS. My message is, drop the interest rates. Look at 36 percent or so. Pastor is doing it with 28 percent. We believe it can be done. Create the opportunity for this gentleman and don't gouge him.

Chairman NEUGEBAUER. The time of the gentlewoman has expired.

Ms. WATERS. I yield back the balance of my time.

Chairman NEUGEBAUER. I now recognize the gentleman from North Carolina, Mr. Pittenger, for 5 minutes.

Mr. PITTENGER. Thank you, Mr. Chairman. Mr. Shaul, I would just like to get a better handle on the borrower and what must he provide to obtain a loan from one of your associated members? What are the best practice efforts that they have to follow to this potential client?

Mr. SHAUL. It begins with proof of employment. They must have a checking account. They must have a credit history, which is looked up. And basically, that is what is required.

Mr. PITTENGER. So you are talking to people who have an understanding of the practice of credit, who have a credit history, they are aware of what they are doing, these are thoughtful, knowledgeable people who have already been through the credit process before? You are not just—

Mr. SHAUL. That is correct. I would make one addition, that we have increasingly—and partly under regulatory oversight—also looked at the schedule of obligations that the borrower would have so that we know that the ability to repay doesn't crowd out the other obligations like rent, food, et cetera, that he or she has.

Mr. PITTENGER. So the perception, really, in some of the testimony is if you grab people off the street and you have exploited them and taken advantage of them, and they blindly don't even know what they are getting involved in. And on the contrary, they already have a credit history. It has to be a good, solid history. You wouldn't be loaning the money to begin with.

Mr. SHAUL. We have had a very difficult time, Congressman, getting people to understand that this is a business. And if you are loaning money and you don't get it back, you are not in business very long. Contrary to some people's thinking, if you look at the schedule that the CFPB has put out on sequence of loans, there is only about 17 percent of people who are over 6 loans in a year.

That 17 percent I would submit to you is a problem. And it usually is one of two things. Either that person shouldn't have had a loan in the first place, or in the second place, something happened between the time the person took out a loan and the time the payment was due.

Our best practice requires that if a person cannot repay the loan at the third time it is due, then he is allowed to go into a program where he gets no further interest charge and he gets a longer term to pay. I hear these stories, and I am as horrified by some of the outrageous things I hear as anybody else is. The question then becomes, who made that loan? And almost always when we run them down, we find that it is not someone who is a member in our association or anyone reputable.

There is a myth that there are States that don't have payday lending. Every State has payday lending. The question is, is it regulated payday lending? Or is it payday lending that you can take off the net? And if you just go to your home computer and you look up the State of Washington, or Idaho, or whatever State you choose, even including New York State, and you have the patience to go through New York State payday lending, you will see the opportunity to get a loan, even though that is not regulated. Those are dangerous.

And we have for a long time said to the CFPB, you ought to get at this question by requiring universal registration of everybody who makes a loan, and then you ought to ask every State to pass a law that says, if you are not registered, you can't collect. That will put a stop to this illegal lending, and then we will see how many of these anecdotes are left, because I believe that most of these anecdotes stem from illegal vendors.

Mr. PITTENGER. Thank you very much. It is a very good answer.

Mr. Simmons, you have extensive background, experience in economic development and oversight of financial matters. Do you believe that these loan practices are predatory?

Mr. SIMMONS. I can only speak for the traditional installment lending industry. And in answering your question, we believe that there is an opportunity for these loans to be options, additional loans for individuals because we believe that they are safe, they are affordable, they are over a period of time, that an individual would know exactly what their loan payment would be over a period of time in monthly installment loans.

Our position would be that as you look at the potential rule and the proposal, that consider the other options that are available. And we believe that a traditional installment loan and the lending industry that has been around for 100 years, different than other products, is an opportunity to be choice given to individuals that is not predatory in nature.

Mr. PITTENGER. Thank you very much. I yield back.

Chairman NEUGEBAUER. And now the gentleman from Texas, Mr. Green, is recognized for 5 minutes.

Mr. GREEN. Thank you, Mr. Chairman. I thank these witnesses for appearing, as well.

Dr. Haynes, let me thank you for the stellar job that you have done. I want to go beyond this question of payday lending for just a moment and mention your THRIVE program, where you have had over 100 young Black males to work with you between the ages of 16 and 19, paid them not minimum wage, but $10 an hour, and they are getting mentoring and they are getting tutored. And you are doing a good job in helping people to find their way in life. And I want you to take just a moment, if you would, so that people will know who you are and tell us a little bit about the things that you are doing at your church.

Mr. HAYNES. Okay, thank you so much. The THRIVE program was in response to the murder of Treyvon Martin, and the outrage in our community had to be harnessed for good. So on the one hand, we wanted to stand against injustice in the justice system, and at the same time provide opportunities for empowerment.

And so for the last 2 summers, we have partnered with other corporate entities, our church has, and we have recruited, we have trained, and we have mentored young brothers for the purpose of helping them to secure employment in some of the corporations in Dallas.

And the program has gone well. This year, we are going to expand it to include young ladies within that same age range. And so it is our hope always to on the one hand address the injustices in the system, and at the same time to empower those who are powerless.

Mr. GREEN. And you hope to help the Mr. Sherills of the world, people who may find themselves in his position, such that they don't have to go to payday lenders. Is that a fair statement?

Mr. HAYNES. That is a fair statement. I admire his testimony and his strength. And it is my determination that he will have other options other than a predatory loan. Though he has made good on his—and I think that is wonderful—it is just that in many instances, he is the exception to the rule. And so we need to be concerned about those who suffer from the rule.

Mr. GREEN. Mr. Sherill, let me compliment you, as well. I think that you have done well with your life and I wish you the very best. But there are lots of folks who haven't been as successful, and they have been victims. And I speak for the victims.

Those who have been in a position to make it through these payday loans, wonderful. And, by the way, I don't want to put payday lenders out of business, either.

So let's just go through some questions quickly. If you believe, as Mr. Shaul does, that you can regulate payday lenders, raise your hand. So, Mr. Sherill, you don't think that you should regulate payday lenders?

Mr. SHERILL. Well, I don't get into the politics into it, so I really don't understand the question.

Mr. GREEN. I don't want you to get into the politics of it. You got into the politics of it when you decided to come to this hearing, Mr. Sherill, just so you know.

Mr. SHERILL. Yes.

Mr. GREEN. Now, let's try it again. If you believe, as Mr. Shaul does, that you can regulate payday lenders—by the way, they are regulated across the country so that you all know—do you believe you can regulate them? Raise your hand. All right. Everybody has raised their hand. Let the record reflect—I want you to be on the record. The record has reflected that you believe they can be regulated.

If you believe that it was appropriate for the military to be regulated, payday lending to the military to be regulated, raise your hand. So now, Mr. Simmons, you don't think that we should have regulated the military. Mr. Sherill, you don't think that we should have regulated the military. And, Mr. Miller, you don't think we should have regulated the military.

Do you think that the military folks ought to be treated the same way other people are being treated and taken advantage of to the same extent. Is that a fair statement, you don't think they should be regulated? I will ask you again so that you can be on the record. You have to be on the record now. You are talking about the military of the United States of America. If you believe that we should have regulated military payday lending, raise your hand. All right. Let the record reflect again that the same three persons do not believe that this should be done.

Mr. SHAUL. Congressman, can I at least—

Mr. GREEN. There are no halfway answers right now, because I only have 20 seconds left. I apologize, okay? If I had more time, I would work with you. See, here is the problem. And I respect the three of you for taking the positions that you have taken. But here is the problem. A person today not in the military can be victimized by some of these payday lenders. Not all, but some. But if the next day he gets in the military, he can't be victimized. What happened to him to make him a person who shouldn't be a victim overnight?

Chairman NEUGEBAUER. The time of the gentleman has expired.

Mr. GREEN. Thank you, Mr. Chairman.

Chairman NEUGEBAUER. The Chair now recognizes the gentleman from Colorado, Mr. Tipton, for 5 minutes.

Mr. TIPTON. Thank you, Mr. Chairman. I would like to thank the panel for taking the time to be here today and to be able to hear your individual stories. And I know in my district in Colorado—in fact, we have well over 200 letters that have been sent to our office, constituents out of my district who have taken the time to be able to just write in and be able to express their support for having the freedom to be able to go out and meet their financial needs, to be able to have some choices in some very specific circumstances.

A constituent out of Alamosa wrote us saying that they used one of these short-term loans to be able to pay for unexpected car repairs, and another in Monte Vista to be able to catch up on a couple of bills, and yet another for medical bills.

What they are concerned about is the overreaching hand of the Federal Government. And you have had to sit here a long time, so maybe a little exercise is a great idea. How many of you here think that the Federal Government is the sole embodiment of good choices for how to be able to run a business in this country? Let the record show not one person raised their hand.

What we have is our colleagues have pointed out is an industry that is regulated and creates some opportunity in those hometown communities to be able to provide access in a time of some specific need to be able to do that. But, Mr. Simmons, I would like to be able to maybe get a couple of comments from you. When you were giving your testimony, you had talked about a financial service desert in your community.

Mr. SIMMONS. Yes.

Mr. TIPTON. And just really kind of a couple of points. I think that I would like to be able to hear you address on this. The importance of that access and, in your community, when it was effectively outlawed, people were told to go away from providing some of the service to the community, did the need go away, and where did they go?

Mr. SIMMONS. I would like to say that, Congressman, the need is there. The need is great. It is demonstrated by the fact that in the State of Missouri last year, I believe there were 180,000 traditional installment loans that are made.

With respect to small dollar loans made in the entire State, that is well over a million that is made on an annual basis. So there is significant need that is there. My testimony today was to talk about the traditional installment lending and what it is as an option with respect to that need.

And so I commend the gentleman, Dr. Haynes, who talks about giving the options in the community that allows the community to have additional options. I commend him for that. I commend individuals that try to find different ways and different options.

At the same time, I am very familiar with the fact there is still great need and there are at times cracks that often people will slip into, and they won't be able to get one loan versus the other. And so for those that are doing that yeoperson's job like he is doing, we commend them.

At the same time, I think it was said earlier, giving the options where you have the opportunity to say here are other products that are in the marketplace and given competition and given the opportunity to have other products is something that is still needed within the community.

I didn't have that within the community that I grew up in. I see what transpires in a community where there is a financial services desert. That need is still there. If there are not people like Dr. Haynes filling that gap and filling that role or having safe and reliable loans like I talked about with traditional installment lenders, it is very difficult because the banks don't do this.

Mr. TIPTON. And then it will move into a completely unregulated market, which is probably going to be a lot more punitive?

Mr. SIMMONS. I would say that is what we hear in the community often is, I am going to find a way to deal with my needs.

Mr. TIPTON. To be able to help your family.

Mr. SIMMONS. To be able to help.

Mr. TIPTON. I apologize. I am a little short on time, and I did want to get Dr. Miller in. Does it raise concerns for you that we are seeing the CFPB, where it has done no analysis of existing State regulatory structures or practices, now trying to be able to set the bar nationwide?

Mr. MILLER. Yes, it does. I think having 50 States try regulations gives us 50 opportunities to see what works and see what doesn't work. And the States do have various regulatory methods that they have employed in the past.

My question is, on research, let's see independent research that is done that is not a position but it is independent by academics who look at the data and ask questions and draw conclusions and publish the results in peer-reviewed journals.

Mr. TIPTON. Thank you so much. My time has expired.

Chairman NEUGEBAUER. Time has expired. The Chair now recognizes the gentleman from Kentucky, Mr. Barr, for 5 minutes.

Mr. BARR. Thank you, Mr. Chairman. And thanks to our witnesses. And, first, to Dr. Haynes, let me just thank you and commend you for stepping in and providing through your church opportunities for credit, for folks in your community. And I think there is certainly a role for that in the faith-based community to do that.

And also, as we have seen so many times, faith-based institutions and institutions of private society, frankly, doing a much better job than the government in offering financial literacy to the people of this country.

To Mr. Sherill, I wanted to ask you, in your compelling personal story of redemption and accessing a payday loan to build a business and take advantage of a second chance that was given to you in your life and really be the embodiment of the American Dream, at that time in your life, did you have access to a faith-based church or organization that could have given you credit?

Mr. SHERILL. No, I had access to nothing. And that is why I chose to go to the payday lending. There is nothing out there. Like, again, I said, I commend Dr. Haynes for that. If he had one in my city, I am pretty sure there would be a lot of people like me going to see him.

We are looking for something. We have nothing. And that is why I chose to go to payday lending.

Mr. BARR. And I think that spells it out right there. Sometimes, there aren't as many choices as we need. And I think your story demonstrates that the greatest protection for consumers, the greatest consumer protection is competition and choices. And if we had more choices, we would have better opportunities for people to do what you did and achieve the American Dream. And I commend you for that.

Let me just ask you, Mr. Sherill, if you didn't have that opportunity for that payday loan to build that business, where would you be today?

Mr. SHERILL. Possibly back in prison, because we revert back to what we are used to. And if I am used to the streets and getting money from the streets, then I would most likely go back to that, because it is survival of the fittest. If you don't have it, then you have to go get it some type of way.

Mr. BARR. Again, I appreciate the fact that your story is one of redemption and second chances and taking a risk and the hard work that it takes to do what you have done. There has been a lot of talk today in this hearing about predatory lenders and making people victims. Mr. Sherill, do you view yourself as a victim?

Mr. SHERILL. No, sir. Not at all.

Mr. BARR. So if you don't view yourself as a victim of your business partner advance, describe that relationship that you have with your lender?

Mr. SHERILL. Well, my lender—I got to know them. They are basically a pillar of our community in Nashville. They give back a lot. I am here solely because of me and my reasons. But they are—in our community, they give back a lot. And they gave me an opportunity when nobody else would.

Mr. BARR. To Mr. Simmons and Mr. Shaul, I think, Mr. Simmons, you made the point that banks don't do this. And I want to explore that issue, because, again, as I said before, I think competition and choice is the best way to protect consumers, in addition to State-based regulation, consumer protection laws. Kentucky has one of the most advanced consumer protection laws in this area, and unfortunately the Bureau would cancel out what our general assembly and our regulator and our governor have done in that area.

But let me just explore why banks don't do this. The CFPB, the OCC, and the FDIC, they have issued rules that have limited banks' abilities to compete in the overdraft space, in deposit advance, in short-term lending, with only a few banks left even offering such products.

So it looks to me like the regulators in Washington are squeezing both sides of this. And as Mr. Sherill says, they are going to go—you are going to go get a loan—I think your testimony, Mr. Sherill, was I can say that there other places I could have gone for a loan. You don't want me to tell you about those places or those people, but they are out there.

If we are denying the American people access to credit from banks and traditional lenders, and then the Bureau comes in on this side and denies people like Mr. Sherill opportunities here, and there are not great people like Dr. Haynes in the community and the faith-based community, where are these people going to go? Mr. Simmons, Mr. Shaul?

Mr. SHAUL. May I say, Congressman, the Bureau has adopted a policy that is simply this: The easiest way to protect consumers is to deny them credit. There is no problem then with whether there is any misuse. But that is precisely a recipe for disaster, because contrary to what the Bureau seems to be willing to propone, ask yourself how many Americans have advanced economically or socially without the use of credit.

The people to whom we loan money have a more desperate need often for that credit than anybody else does. The failure to appreciate that the reasons that banks have moved out of neighborhoods has a lot to do with simple economics. The cost of complying with the post-2001 disaster in New York City, the cost of that, the compliance cost for most banks has tripled since in that 15 years.

Banks look upon everybody who comes through the door as to whether or not they are a profit center. That means that they have very little interest in those individuals who don't look at that moment in time as though they will continue to be a profit center.

That means that we have a much larger non-depository base than we used to have. Regulating it is very important, but having it there is even more important than the regulation.

Chairman NEUGEBAUER. The time of the gentleman has expired.

Mr. BARR. Thank you. I yield back.

Chairman NEUGEBAUER. The gentleman from Texas, Mr. Williams, is recognized for 5 minutes.

Mr. WILLIAMS. Thank you, Mr. Chairman. And I want to thank all of you for taking time today. It has been a great dialogue. I appreciate it.

I am a small-business owner in Texas. And I may be one of the few on this committee who actually is a lender. I deal in credit. And I just cannot believe, as I go through my life every day up here, how people want to bash and condemn small-business people who are trying to employ people, trying to make things better.

Mr. Sherill, I know that we talked about victims today. And I hope that the victims who are out there, whomever they are, are looking at you as someone they can look up to and get themselves out of that status and get into where you are and own a business and employ people and do great things. And I know everybody is proud of you.

And I want to just say this really quickly to you, Mr. Sherill. Tell me about—we talked about the place you borrowed the money. But I believe that Mike and Tina Hodges own that business. And what kind of people are they?

Because here is the deal. All of us who employ people, who own businesses, we just get hammered by this Administration, just non-stop, every single day. I want to know what kind of people you do business with. These are good people, I bet.

Mr. SHERILL. Yes, they are stand-up, honest people who give people opportunities. Like I said, they do a lot in the community. I could go on and on about the stuff that they do. They are great people. They are wholesome people. They are family people. I have known them for about 4 or 5 years now, and I have built a rapport with them over the years.

It started out as business. And then later on, we created a rapport. Initially it was strictly, hey, I didn't know them, and then as years went to—as years developed, I got to know them personally.

Mr. WILLIAMS. That is the same story across the country about people who invest and try to help folks. And I am glad to hear about that. And just that story in itself, Mr. Chairman, I would say is another story of the American Dream.

Mr. SHERILL. Yes, sir.

Mr. WILLIAMS. And so I hope we don't destroy that, which it seems like we are trying to every single day up here.

Now, Mr. Simmons, my question to you is, after listening to your testimony today, I believe it is safe to say that the need for small dollar lending is real. Now, you note in your testimony that traditional installment lenders make traditional installment loans or to make high-quality small dollar loans. But I don't think the CFPB believes that.

What the CFPB doesn't understand is the importance of providing service to customers. They don't deal in service. They have no idea on how to give service to their customers, which is all of us. Most of the people I deal with in my business, the car business, and the people you are here to represent are folks that we can really make a difference for. We try to improve things, whether they need a new car to drive or a used car to drive to get to work or a small loan to get through a tough month. We are there to support them, because they are valued members of our community. The experience can be personal. And, frankly, again, we get back to the consumer and the people know better than the Federal Government.

So let me ask you, Mr. Simmons and Mr. Shaul, these questions. As we discussed earlier, in 2008 the FDIC conducted a small dollar loan pilot program to see if banks would participate in this space: 31 banks participated, with 446 locations in 26 States. I think what the FDIC program showed was that it didn't save customers any money. In his budget release this week, the President requested $10 million for the small dollar lending program to be administered by community development financial institutions. This, of course, would be funded by the customer, i.e., the taxpayer.

So can you elaborate, either one of you, more on this program and why it will or won't work, to really save the consumer any money at all?

Mr. SHAUL. It won't work. Bluntly put, the FDIC experiment did not work. And it did not work because you cannot subsidize your way or artificially control rates and believe that the market will respond.

This is a problem because, first of all, it will bring to full measure something we have all feared, and that is the CFPB runs always the risk of becoming an allocator of credit, picking winners and losers. And this is the direct attempt to do that.

Second, this is the nose inside the tent. If it is $10 million today, it could be $100 million or $1 billion soon. Third, and most importantly, anyone can make loans, provided they know that their losses are going to be floored by another entity, and that is what is being talked about here.

There is a contingent who believes that you can do away with what is now being offered by the private sector, and you can get at that either by Operation Chokepoint or you can get at by rules that make it impossible for us to operate. Having done that, then the solution becomes to put in an artificial resuscitation effort which would be this kind of program.

Mr. WILLIAMS. Thank you. I have 4 seconds. Does anybody want to comment on the President's request in funding for a loan loss reserves in this year's budget? I am out of time.

Mr. Chairman, I yield back.

Chairman NEUGEBAUER. I thank the gentleman. And I now recognize the gentleman from Missouri, Mr. Luetkemeyer, the chairman of our Housing and Insurance Subcommittee.

Mr. LUETKEMEYER. Thank you, Mr. Chairman. And welcome, Mr. Simmons, a fellow Missourian. It's good to see you again, sir.

Mr. SIMMONS. Thank you.

Mr. LUETKEMEYER. Dr. Miller, kind of a quick couple of questions for you here. Do you know off the top of your head what the average loan loss ratio is, of an average payday loan company?

Mr. MILLER. I do not.

Mr. LUETKEMEYER. Okay. Do you know what the rate of complaints are average across the country for per thousand transactions, something like that?

Mr. MILLER. No, sir, I don't know exactly. I think it is low, but I don't think—I don't know exactly.

Mr. LUETKEMEYER. Mr. Shaul, do you know that number off the top of your head?

Mr. SHAUL. I would like to make two comments about that. Historically, State by State, it is very low. Director Cordray said to us that he would be driven by the complaint data. If you look at the complaint data, two things are apparent. The payday loan complaints are very, very low. They are at either the first or second lowest in all of the categories that are measured by complaints.

Second, when you analyze those complaints, they contain two other kinds of categories within them, loans that are complained about, denominated as payday loans in States that don't have payday lending, which means that people who took a non-regulated online loan are complaining about the fact that they are being serviced poorly, paying too much, one thing or another.

That problem the CFPB has had no willingness, no appetite for tackling at all, although it is obviously one that should be tackled, because it impedes the businesses that do have reputations to protect, and it is disastrous for the consumers.

The second thing about the complaint portal is that it is irrational. If someone writes in and says, I didn't get a loan, that is my complaint, we get a ding as an operator as though there were a legitimate complaint. It is baffling to me that the single exercise that was meant, we were told, to guide the question of examination, compliance and rulemaking shows us to be not a category of problems, but we are the ones that are first out of the box and being set upon by a rule, and yet the rule does nothing about the real complaints that are there and about the real victims who are not being in any way brought to a situation where they will be compensated.

Mr. LUETKEMEYER. In my experience, when I was a financial services chairman back in Missouri for a few years, and actually worked on at that time a landmark piece of payday lending legislation, so it became the model for a while of how you address this issue, I checked every year with our consumer protection folks in the State there. And the payday loan folks per thousand transactions, their rate was always less than banks and credit unions.

Mr. SHAUL. Yes.

Mr. LUETKEMEYER. It was across-the-board. That is not even close.

Mr. SHAUL. That is the nationwide experience.

Mr. LUETKEMEYER. So it tells you that there are a lot of satisfied customers out there. And we have heard some testimony today about some who are not happy. And every industry has that kind of a situation. I don't care whether you are selling cars like Mr. Williams is or whatever your industry is, if you are selling toothpaste. Somebody is not going to be happy with your product and misuse it somewhat.

One of the concerns I have is—it really is kind of interesting, we have—the government took over the student loans, and we continue to increase the student loan data, get more students in debt over their heads than can actually ever get out, and today we are worried about the problem with payday loans when we have hundreds of thousands of dollars that some of our students are getting into and haven't heard a whimper out of the other side on that. It is amazing.

But I would like to talk for just a second about Chokepoint. Mr. Shaul, you brought that up. Obviously, you are probably aware that I am the sponsor of the Chokepoint bill here in Congress, and my colleagues helped me pass that last week and sent it to the Senate to try and stop the nonsense. I have an e-mail address in my office that takes Chokepoint stories. I had one last week, and it was a payday lending one. Two weeks before that, it was a credit bureau in California. And 2 weeks before that, it was a tobacco shop in Florida.

I have about a minute left here. Can you quickly give a couple of stories about Chokepoint?

Mr. SHAUL. I had one in my e-mail today from the State of California, a small operator in a very small town. This has not stopped. We still feel that the examiners have not been given sufficient disciplinary action from the top that they will stop advising people, banks, institutions, to cut off those of us who fall in the category that by their taste they don't like, not by the law, not by any guidance, but by their taste.

And I must tell you, I was extremely disappointed by the President's statement. Evidently, we have come to this point with regard to due process in this country where it is justified to go after those who are regulated and innocent by virtue of the statement he issued because it could interfere with getting at some of those who are actually guilty of crime.

Were we to take that standard into the criminal law or were we to do anything else with it, we would have repudiated most of the Anglo-Saxon and United States history as far as rights go.

Mr. LUETKEMEYER. I appreciate your comments, sir, and I appreciate the indulgence of the chairman. I think this is a key point that your members are being deprived of their livelihood without due process.

Mr. SHAUL. No due process.

Mr. LUETKEMEYER. It is a Constitutionally protected right. Thank you, Mr. Chairman.

Chairman NEUGEBAUER. The time of the gentleman has expired.

The gentleman from Minnesota, Mr. Ellison, is recognized for 5 minutes.

Mr. ELLISON. Let me thank the chairman and the ranking member.

For anybody who might be watching these proceedings, I want to say thank you and welcome for being here today. I would like to point out just as a matter of rule that the reason that of the five people who are offering testimony today, four sound like they are taking a Republican position, is because that is the way the rules work. The Republicans get to choose, well, four—the majority of the witnesses and the Democrats get to pick just one.

So anybody who just doesn't know how it works around here, this is not representative of how people feel about this issue. It is just the Republicans have the majority, so they get to pick four people who agree with them.

Anyway, Dr. Haynes, it is always a pleasure to see you. I want to thank you for your tireless fighting for people all the time. You are always at the forefront of standing with people. And you remind me of some dear friends I have in Minneapolis where I am from. We also have strong faith-based movement working in predatory payday lending in our communities.

And by that, I don't mean all payday lenders are always predatory, but there is predatory payday lending and we should try to stop it. And I would hope everybody on this panel would agree with me about that.

I work with at home friends of mine, Reverend Paul Slack of New Creation Church, Reverend Grant Stevenson, Pastor Billy Russell, Greater Friendship Missionary Baptist Church. I could fill them up with this room, and I guarantee you I would have more people complaining about the way payday loans are abused than people on the other side of the fence, if this were a true representative sample of how people feel about this issue.

Can you tell us why faith-based leaders, yourself and others who you work with, and institutions are involved with this small dollar lending issue? What brings you to it?

Mr. HAYNES. Number one, it is a moral issue in that in our faith tradition, as in most faith traditions, we believe that God is concerned about those who cannot do for themselves. And as a consequence, we have a responsibility to address those structures and systems that reinforce that situation of being dispossessed and left behind.

Mr. ELLISON. Now, Doctor, you don't just preach from the pulpit. You actually go one-on-one with people.

Mr. HAYNES. Right.

Mr. ELLISON. In your experience, do most people understand the terms that they are getting into? Is there sufficient time for them to—do the lenders take time for them to really know what they are getting into? Or are these desperate people in a desperate situation?

Mr. HAYNES. Thank you. They are desperate. And when you are in a desperate predicament, and this is what is marketed to you through the airwaves, and it is all you see on your streets, again, you make choices within the confinement of your options. And so they make those choices out of desperation, and they are not going to take the time to read the whole thing. And most of us don't take time to read our whole loan piece whenever we apply for a loan.

So to judge them I think is inappropriate and unfair. So you are talking about desperate people in desperate situations who want to do the right thing, but they are being set up by predatory practices.

Mr. ELLISON. So one of the things that some of the folks who engage in these predatory payday loans—and, again, by saying—I use the predatory not to modify all payday loans, but the predatory ones—and sadly there are too many. And I would hope that everyone in the industry would want to hold up a high standard.

A lot of times, these folks who advocate for just predatory lenders doing whatever, they say that they have to be allowed to do it or there would be no other alternative. Do you agree with that?

Mr. HAYNES. Not at all. As a matter of fact, again, our microloan fund that we are offering at the church through our credit union is there and it is doing well. The people are paying back well. As a matter of fact—and I meant to correct the gentleman earlier—if you are paying well on the loan, it goes from 28 percent to 19 percent. So we are still doing well. And I believe that there are those out there who would like to offer these kinds of opportunities.

Mr. ELLISON. Yes, and do you find that other congregations are looking into the same thing? I know in Minnesota there are a lot of congregations thinking about this stuff. They would even try to buy back people's payday loans and then set them on a more moral framework.

Mr. HAYNES. Oh, without question. As a matter of fact, there are several churches in the area that I referenced earlier, where we had this inundation of a community targeted by the industry. And as a consequence, there are several of us who are trying to pick up on this model. I am even partnering with the church across town that is a white Southern Baptist Church, because, again, they are against this kind of predatory practice.

Mr. ELLISON. So it is moral and right to stand up for consumers. Your churches offer alternatives. And there are other people around the world in the country doing the same thing.

Mr. HAYNES. No question.

Mr. ELLISON. Thank you, sir. It is an honor to see you again.

Mr. HAYNES. Thank you.

Chairman NEUGEBAUER. The time of the gentleman has expired. I would like to thank our witnesses for their testimony today.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

And with that, this hearing is adjourned.

[Whereupon, at 6:02 p.m., the hearing was adjourned.]

A P P E N D I X

February 11, 2016

I am the Rev. Dr. Frederick Douglass Haynes, III.

I serve as the Senior Pastor of Friendship-West Baptist Church in Dallas, Texas and Chairman of the Board of the Samuel DeWitt Proctor Conference, a nationwide movement of pastors and community activists fighting for spiritual renewal and social justice . I am pleased to represent Friendship-West as well as othe churches in Dallas and across the nation whose communities have been targeted, oversaturated and economically overwhelmed with payday loan and auto title loan stores.

Several of my colleagues in pastoral ministry and I became alarmed as buildings once occupied by thriving restaurants and bank branches were taken over by payday and auto title loan stores. In the last 10 years, 20 payday and auto title loan shops opened within a five mile radius of our churches. Many of these stores are located next door to each other. A community that was already suffering as a food and job desert was and is being overrun by these predatory stores. It appeared that our underserved and under banked community was being intentionally targeted for these high cost, debt trap loans. Our concern was confirmed as we heard from members of our churches and residents in the community who were financially held hostage by these "loans." They confessed that in a situation of desperation they had sought to get a loan that eventually became a trap. They made payments, every other week or monthly, only to get deeper in debt. They were in a financial hole and upon getting a payday or car title loan, received a shovel instead of a rope.

As a pastor my heart went out to many who were victimized by these predatory practices. Here are some of the unfortunate experiences shared by members of our churches and citizens in our communities. A recently widowed 70 year old grandmother took out a $300 loan. She ended up paying $800. She's always been fiscally responsible but "life happened" and she had to take out this loan. She paid back the loan in full but she had to roll the loan over several times, ultimately paying much more in interest than she had borrowed. I'm representing the 23 year old college student, whose parents are deceased, but he was determined to get his education. He needed to purchase books for his classes and what was a $300 loan ended up costing him over $600. I could go on with other heartbreaking experiences that have been shared with me, but suffice it to say all of them were hoping for a life preserver, but they were given shackles.

Payday loans in Texas carry rates of 500% annualized interest. Car title loans are in the range of 250-300% APR range. The Texas Office of Consumer Credit shows that 61% of balloon payday loans are refinance loans that are taken in order to repay the previous unaffordable loan. Every week car title loans result in 847 car repossessions. A resident of our community shared with me that he had a car title loan that began as a $4000 loan. The car was repossessed when he couldn't escape the debt trap but he had paid $8200 in the process.

A coalition of churches and community groups sought to close the loophole in the state usury law in Texas that allows these businesses to charge over 500% in interest but we were unsuccessful and the shackles disguised as a life preserver remain in place. Undaunted and determined to free our community from these predatory practices we petitioned the city government in Dallas to rein in the destructive dealings of the payday and car title lenders. The Dallas City Council enacted an ordinance that established a limit on the number of times a loan can be rolled over and requires significant principal to be paid down with each renewal. More than 30 municipalities in Texas have followed this model of justice and relief, reflecting the serious concerns held by many Texans about payday and car title loans.

Friendship-West has sought to be a solution to this problem, which is symptomatic of a larger problem of greed and economic exploitation which has produced a widening wealth gap that threatens the fabric and future of our nation, by launching a credit union and partnering with another church in our community that held a federal credit union charter. We now have several years of banking experience and we now offer Liberty Loans, microcredit to members in need who are able to afford a small dollar loan. We offer loans of up to $500 for terms of 6 months and 28% annual interest, 19% interest for members, with a reasonable application fee. There has not been one defaulted loan and all of those who are benefitting from this loan are paying the loan back on schedule because they can afford it. It's good business. It has empowered the powerless it is moral.

We have taken a stride toward economic freedom in Dallas, but we still have a long way to go. The City ordinances have been helpful but they can't cap the rates on these burdensome loans. Furthermore, these ordinances in Dallas don't cover all Texans, not to mention citizens throughout our country who find themselves trapped in underserved communities with limited opportunities that are preyed upon and inundated with payday and car title loans as their only options.

I maintain that it is vitally important for this committee to be morally outraged and attend to the devastating harm caused by payday and car title lenders who have preyed upon the vulnerable and in the process they have financially trapped individuals, stressed families while economically crippling communities. This is immoral and an affront to faith that demands that we protect "the least of these" and stand against all forms of usury.

Nationally, in states that permit these loans, payday loans average 322% APR, typically due two weeks later, while auto title loans average 300% APR, usually due in one month. The bait is marketed as a life saver but it is a debt trap. We can't excuse this as the practice of a few bad apples who are greedy; this is the industry standard. Three-fourths of all payday loans are from borrowers with more than 10 loans per year. They are trapped in an economic snare. The average payday borrower spends seven months of the year trapped in these loans that are supposed to be for two weeks. The downward cycle of debt has long term economic harm. Payday borrowers are more likely to lose their checking account due to overdrafts, fall behind on medical and other expenses, and even file bankruptcy. This is immoral and unacceptable. To respond to a desperate person and give them a loan that takes them from bad to worse is a slap in the face to human decency and dignity.

I am especially appalled by the harm done to communities of color that have been historically exploited and suffer from a lack of economic opportunity. Payday loan borrowers are disproportionately African-American. The research reveals, sadly, that payday lenders target these disadvantaged communities. This predatory industry adds to the problem of the racial wealth gap in this nation. I recognize that some have been helped by this industry but they are the exceptions. Too many are imprisoned. If there's not justice for all we don't have justice at all.

The CFPB's proposal protects against loan rollovers that perpetuate the debt trap. These protections are desperately needed because of the very nature of payday and car title loans. Lenders have direct access to the borrower's checking account allowing the lender to be repaid without regard for other responsibilities the borrower may have. This is a depraved business model that cannot go on. L

We want access to credit, but it must be quality credit. Anything less adds to the stress of the desperate and needy. Well-crafted and compassionate legislation can weed out the predators and enable more responsible and reputable lenders to thrive while rendering a helpful service to communities in need. We must end the debt traps, protect the vulnerable and eliminate the predators so that all can experience "life, liberty and the pursuit of happiness."

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TESTIMONY

PRESERVING AND EXPANDING CONSUMER ACCESS TO CREDIT PRODUCTS ALONG THE NONBANK-SUPPLIED SMALL-DOLLAR LOAN LANDSCAPE

THOMAS MILLER, JR.
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Visiting Scholar, Mercatus Center at George Mason University

House Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit
Hearing: Short-term, Small Dollar Lending: The CFPB's Assault on Access to Credit and Trampling of State and Tribal Sovereignty

February 11, 2016

Chairman Neugebauer, Ranking Member Clay, and members of the subcommittee—thank you for the opportunity to appear before you today. Consumer credit has been a hotly debated topic for decades, if not centuries. Historically, banks do not fulfill small-dollar credit needs of subprime borrowers. As a result, the marketplace has responded with an array, or landscape, of nonbank-supplied small-dollar credit. Americans who rely on nonbank-supplied small-dollar loans are not wealthy, and many live from uncertain paycheck to uncertain paycheck. Today, few Americans have rainy day funds big enough to cover unexpected bills, paycheck shortfalls, or unplanned work absences.[1] People who make regulatory decisions on behalf of these borrowers are well intentioned. In many cases, however, they do not fully understand how small-dollar credit products help subprime borrowers who are in difficult financial circumstances.

In my scholarly work on consumer credit, I seek to understand how small-dollar loan markets work and how best to restructure regulation to improve borrower welfare. Access to credit is a fundamental freedom for all Americans. The research that I and others have done shows that regulation along the consumer credit landscape often impinges upon this freedom.

1. See Annamaria Lusardi, Daniel Schneider, and Peter Tufano, "Financially Fragile Households: Evidence and Implications" (Brookings Papers on Economic Activity, Brookings Institution, Washington, DC, Spring 2011).

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My testimony contains three main points:

A. The small-dollar credit market is diverse because consumers' needs are diverse.

B. Eliminating credit supply does not eliminate credit demand.

C. States have a long experience regulating small-dollar credit products—enabling us to judge the performance of regulatory restrictions.

A. THE SMALL-DOLLAR LOAN MARKET IS DIVERSE BECAUSE CONSUMERS' NEEDS ARE DIVERSE

A common form of consumer credit is the personal credit card. Both prime and subprime borrowers use credit cards. Policymakers are likely less familiar with other common small-dollar consumer credit products, which I will focus on. These products have different loan structures in terms of size, length, cost, and repayment.

It is incumbent on anyone legislating, regulating, advocating, or studying any small-dollar credit product to know the differences among these products. There are significant differences among nonbank-supplied consumer credit products. Differences in their structure and underwriting processes mean that these products are not perfect substitutes for one another.

Nonrecourse Credit Products

1. *Pawnbroker loans* "are among the oldest forms of credit, stretching back to antiquity."[2] To my knowledge, pawnbrokers operate in every state. Their products have a simple structure. A consumer who owns something of value, say a stuffed moose head, exchanges the moose head for cash.[3] At the end of the term, generally 30 days, the consumer has three options: a) extend for another term by paying a fee, generally 20–25 percent; b) reclaim the moose head by repaying the loan and the fee; or c) walk away and abandon the property. If the consumer chooses the third option, the pawnbroker has no recourse—the borrower owes nothing and the pawnbroker now owns the moose head. Accordingly, the only thing that matters to the pawnshop is the value of the object presented and the borrower's legitimate ownership of the item.

2. *Vehicle title loans* operate in a manner nearly identical to pawn loans. To my knowledge, these loans emerged in the 1990s and, by law, title lenders operate in only 17 states. In these transactions, a consumer uses a clear car title as collateral. Importantly, the consumer keeps possession of the vehicle during the term of the loan—generally 30 days. The title lender places a lien on the car. The lender may also ask the borrower to provide references and proof of income.[4] At the end of the term, the consumer has the same three options as the consumer who borrows from a pawnbroker. If the consumer chooses to abandon the car, which happens only about 8 percent of the time,[5] the title lender sells the car and keeps the proceeds, but may not pursue the borrower for the difference if the loan exceeds the proceeds from selling the car. State laws governing vehicle title loans vary, but typically govern the maximum amount that can be borrowed and the maximum interest rate.[6]

2. Tom Durkin, Gregory Elliehausen, Michael Staten, and Todd Zywicki, *Consumer Credit and the American Economy*, Oxford University Press, 2014.
3. For more detail on pawn lending, see Marieke Bos, Susan Carter, and Paige Marta Skiba, "The Pawn Industry and Its Customers: The United States and Europe" (Law & Economics Research Paper Number 12-26, Vanderbilt University Law School, September 2012). For a sample pawn statute, see Mississippi's Pawn Shop Act § 75-67-313 (2013), which limits fees to 25 percent of the principal amount of the cash advanced.
4. Jim Hawkins, "Credit on Wheels: The Law and Business of Auto-Title Lending," *Washington and Lee Law Review* 69, no. 2 (2012).
5. Todd Zywicki and Gabriel Okolski, "Potential Restrictions on Title Lending" (Mercatus on Policy, Mercatus Center at George Mason University, Arlington, VA, November 2009).
6. For an example, see Mississippi Code § 75-67-413 (2013).

Recourse Credit Products

3. *Payday loans,* available at brick-and-mortar stores and online, are lump sum loans with interest and principal due at the end of the term, generally 14 days. To my knowledge, these loans emerged in the 1990s and these lenders operate legally in 33 states. These loans have a simple form. Payday lenders typically require the borrower to have a checking account, provide proof of income, show identification, and be at least 18 years old. About 80 percent of those who apply for a loan receive one. Payday lenders collect a signed Automated Clearing House authorization or a postdated check from the borrower in the amount of the principal plus interest. States limit the values of these loans and the fees a lender may charge, and they regulate other aspects of the loans.[7] Although regulations vary, a typical maximum amount lent is $500, with a typical fee of about $20 per $100 borrowed.

4. *Traditional installment loans* are available through finance companies. The history of these loans stretches to the Uniform Small Loan Law of 1916—a model law that emerged from extensive study of small-dollar lending in the early 1900s. To my knowledge, no state bans this credit product, but because of laws capping interest rates, installment lenders only operate in about 32 states.[8] There is a wide range of allowable interest rates. Consumers pay back installment loans with equal payments over time. Each payment consists of principal and interest. These loans amortize; that is, the amount owed decreases over time. Depending on the size of the loan, a typical term is 6 to 24 months. Due in part to this structure, installment lenders must conduct extensive underwriting—that is, assess the borrower's financial condition and gauge their ability to repay the loan. Depending on overall economic conditions, installment lenders turn down 40 to 60 percent of loan applicants.

Consumers generally know how to navigate the small-dollar landscape. I recently surveyed 400 randomly chosen Mississippians.[9] In my study, I asked two questions. The first was, "Do you know where to go to get a loan to suit your needs?," and 53 percent of the respondents strongly agreed, while 11.5 percent strongly disagreed. The second question was, "Do you understand the terms of the loans you have taken out?," and 60.5 percent of the respondents strongly agreed, while 8.3 percent strongly disagreed.

B. ELIMINATING CREDIT SUPPLY DOES NOT ELIMINATE CREDIT DEMAND

Economic research shows that in American history, banning products outright, or effectively banning them through regulatory restrictions, does not eliminate the demand for these products. Instead, the effect is a restriction in the honest supply of these products. The 18th Amendment to the US Constitution is an instructive example of the unintended effects of banning legitimate businesses. Banning the production, sale, and transportation of alcohol drove those businesses underground. People were still (illegally) making and transporting alcohol, but buyers paid a premium to cover the added legal risk that producers and transporters faced.

Recent rigorous academic research documents the importance of keeping nonbank-supplied credit products available to consumers. For example, Zywicki and Okolski conclude: "The bottom line is that restrictions on auto title lending will eliminate an important funding option for many consumers, especially those of lower income, and will incentivize the use of more risky or dangerous credit channels."[10] In addition, Fritzdixon, Hawkins, and Skiba conclude: "Instead of banning title lending, policymakers should foster a market with information that will help customers understand the true cost of title loans."[11] Morse studies the payday loan market and finds that "communities with payday lenders show greater resiliency to natural disasters," and her estimates of welfare measures "suggest that payday lending enhances the welfare of communities."[12]

7. For an example, see Mississippi Code § 75-67-501 (2013). For a list of other types of state regulations, see Alex Kaufman, "Payday Lending Regulation" (Finance and Economics Discussion Series 2013-62, Federal Reserve Board, Washington, DC, August 2013).
8. For an example, see Mississippi Code § 75-17-21 (2013).
9. Thomas Miller, Jr., "Differences in Consumer Credit Choices Made by Banked and Unbanked Mississippians," *Journal of Law, Economics & Policy* 11, no. 3 (2015).
10. Zywicki and Okolski, "Potential Restrictions on Title Lending."
11. Kathryn Fritzdixon, Jim Hawkins, and Paige Marta Skiba, "Dude, Where's My Car Title?: The Law, Behavior, and Economics of Title Lending Markets," *University of Illinois Law Review* 2014, no. 4 (2014).
12. Adair Morse, "Payday Lenders: Heroes or Villains?," *Journal of Financial Economics* 102, no. 1 (2011).

The Consumer Financial Protection Bureau (CFPB), armed with five years of experience, stands ready to make new consumer credit rules. The CFPB has the power to distort or destroy consumer credit markets under the guise of protecting consumers from "unfair, deceptive, or abusive acts or practices." For example, based only on established patterns of use, the CFPB is currently exploring new restrictions on payday loans. Observing that some payday loan customers use payday loan products frequently, the CFPB seemingly concludes that payday loans are "unaffordable." Without exploring other possible reasons why some payday borrowers use the product, or documenting harm to consumers, the CFPB is seeking to limit the number of payday loans made to any consumer in a year to six. My preliminary investigation into this matter suggests that such a limit could eliminate 60 percent of the payday loans made each year. Other research suggests that the comprehensive CFPB proposal will eliminate 80 percent of the number of payday loans made in a year.[13] Where will these borrowers go for credit?

Eliminating payday loans does not mean that borrowers will magically stop borrowing or simply begin to borrow from other legal lenders. Director Richard Cordray has testified to the effect that the CFPB plans to preserve access to some small-dollar loan products. In my opinion, the traditional installment loan makes a good candidate because it has a long history of being a safe and affordable pathway out of debt. Traditional installment lenders, however, do not and will not loan to everyone. Such regulation could force some consumers, already in desperate situations, into the arms of illegal lenders. Loan sharks love credit deserts—places that are uninhabited by legitimate lenders because of ill-considered regulation (see attached figure 1).[14]

Rather than conducting careful research of its own and drawing from the research others have done, the CFPB appears poised to act without adequate independent empirical support. If so, the CFPB could radically alter the small-dollar loan landscape to the detriment of consumers. The CFPB would be wise to base its decisions on compelling academic research—and the CFPB should be actively encouraging such research. These decisions could include leaving regulation entirely to the states. As an academic, I believe in conducting thorough and extensive research before making public policy decisions. In the example above, I want to see considerable rigorous empirical evidence that: a) repeated payday borrowing is, in fact, harmful to consumer welfare, b) such a proposed limit of six loans in a year will do more good than harm, and c) no existing state regulatory structure is adequate to address the perceived overuse problem.

C. THE PERFORMANCE OF STATE REGULATORY RESTRICTIONS ON SMALL-DOLLAR LOANS

The CFPB cannot impose interest rate caps. This power belongs to the states. The various states have made many regulatory choices along the landscape for the last century and have been setting interest rate caps since colonial times. Binding usury laws, since colonial times, reduce credit and economic activity.[15]

The Progressive Era of the early 20th century brought many social reform movements, including efforts focused on temperance, women's suffrage, child labor laws, and credit reform. The credit reform movement, spearheaded by Arthur Hamm of the Russell Sage Foundation, sought to expand credit for workers. Credit reformers understood that the needs of borrowers and lenders had to be satisfied to create a sustainable market-based alternative to illegal loan sharks. These reformers sought to pass state laws allowing licensed lenders to make small-dollar loans at rates above state-imposed interest rate ceilings, which were then typically 6 percent. Loan sharks have no respect for interest rate caps—or sometimes, more disturbingly, for kneecaps.

13. Charles River Associates, "Economic Impact on Small Lenders of the Payday Lending Rules under Consideration by the CFPB" (unpublished manuscript, 2015). This estimate of the reduction is after the application of the comprehensive scheme of debt protection proposed in the rulemaking.
14. For an illustration of a credit desert due to a 17 percent cap on installment loans, see figure 2 in Onyumbe Lukongo and Thomas Miller, Jr., "Some Consequences of the Constitutional Interest Rate Cap in the State of Arkansas" (forthcoming working paper, Mississippi State University, 2016).
15. See Efraim Benmelech and Tobias J. Moskowitz, "The Political Economy of Financial Regulation: Evidence from US Usury Laws in the 19th Century," *Journal of Finance* 65, no. 3 (2010).

In partnership with lenders willing to risk capital by making loans repaid in equal installment payments, reformers framed the model Uniform Small Loan Law of 1916. Through rigorous studies, the reformers determined that the costs and risks of small-dollar lending merited an annual interest rate of about 36 percent. The reformers set this rate to spur "aggressive competition by licensed lenders" and thus "to drive unlicensed lenders out of business."[16]

A traditional installment lender can make money at a 36 percent APR—if the dollar amount borrowed is large enough to generate enough interest income to cover the costs and risks of making the loan. In 1916, regulators declared a small-dollar loan to be $300 or less (about $6,900 in 2015 dollars). A $300, 12-month, 36 percent APR installment loan generates $61.66 in interest income. A $300 installment loan might have been profitable in 1916, but the loan production costs, including wages, benefits, rent, insurance, and utilities have dramatically increased over the past 100 years.

The consumer price index is about 20 times higher in 2015 than it was in 1916 (see attached figure 2). Today, a $300 installment loan is simply not profitable at a 36 percent interest rate. A recent study showed that a $2,100 (in 2013 dollars) loan has a break-even of 42 percent APR.[17] Thirty-seven states currently have rate caps at or below 36 percent (see attached figure 3).[18]

Numbers like 36 percent and 42 percent sound jarring, so it helps to put them into a dollar context. If you go to an ATM that is not connected to your bank on Friday and withdraw $50 for a $3 charge, you are effectively borrowing $50 (of your own money) until Monday, when your transaction and fee hits your account. Your cost is $1 per day, but your APR is a whopper: 730 percent. Now, would you be happy if a well-meaning regulator prohibited you from paying such an exorbitant APR and you were cashless for the weekend?

Consider a 12-month $1,000 installment loan. At a 36 percent APR, the borrower's monthly payment is $100.46. At a 72 percent APR, the payment is $119.28. The difference is $18.82 per month, or about $4.70 per week. This weekly cost is less than the cost of one pack of cigarettes. A two-pack-per-day smoker can finance this higher rate by smoking 13 instead of 14 packs of cigarettes per week. Installment lenders would likely be willing to make loans of this size under this higher rate. More importantly, a would-be borrower might gladly pay an interest rate above any existing interest rate cap if the alternative were no loan at all.

The result of outdated interest rate caps is that legal loan deserts exist in the small-dollar loan landscape. There is demand, but no supply. Policymakers 100 years ago recognized that they might need to update the interest rate cap. The Uniform Small Loan Law of 1916 states that a rate established by legislators "should be reconsidered after a reasonable period of experience with it." Clearly, the succeeding 100 years exceeds "a reasonable period." Policymakers of today would be wise to follow the lead of reformers in the early 1900s and reconsider the outdated 36 percent interest rate cap.

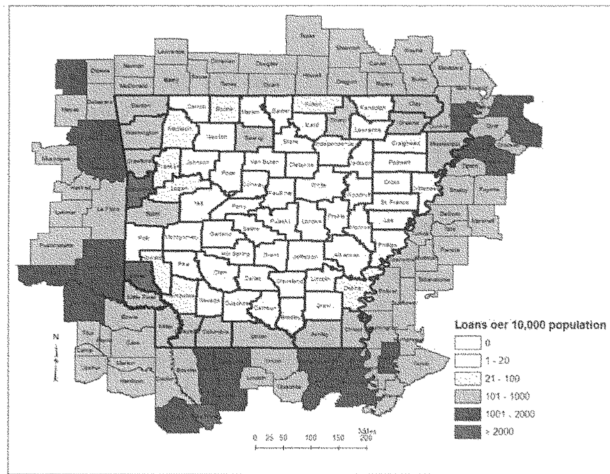
D. CONCLUDING THOUGHTS

Conversations about consumer credit often reflect utopian visions of the world. Many people imagine that a few tweaks to regulations can ensure that everyone has the money needed to feed, clothe, and shelter the family. According to this logic, if households need to borrow money, lenders will treat them fairly, charge little, and always be repaid. But no matter how hard we all try, a well-crafted regulatory framework cannot bring us this utopia. Deliberate, empirically informed regulators, however, can do much to preserve and expand consumers' options along the nonbank-supplied small-dollar loan landscape.

Thank you. I am ready to answer any questions.

16. See F. B. Hubachek, "The Development of Regulatory Small Loan Laws," *Law and Contemporary Problems* 8, no. 1 (1941): appendix C, note 14.
17. Tom Durkin, Gregory Elliehausen, and Min Hwang, "Rate Ceilings and the Distribution of Small Dollar Installment Loans from Consumer Finance Companies: Results of a New Survey of Small Dollar Cash Lenders" (working paper, December 2014).
18. Harold Black and Thomas Miller, Jr., "Examining Some Arguments Made by Interest Rate Cap Advocates" (forthcoming book chapter, Mercatus Center at George Mason University, Arlington, VA, 2016). For a survey of state interest rate caps in effect in 1935, see William Trufant Foster, "The Personal Finance Business under Regulation," *Law and Contemporary Problems* 8, no. 1 (1941).

FIGURE 1. A LOAN DESERT EXAMPLE



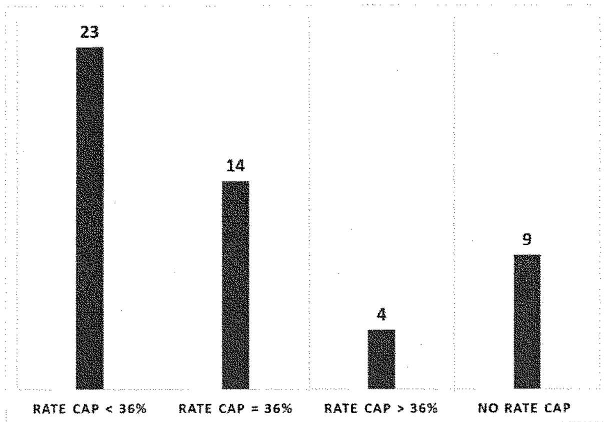
Source: Lukongo and Miller, "Some Consequences of the Constitutional Interest Rate Cap in the State of Arkansas."
Note: Arkansas has a 17 percent interest rate cap. Loan production costs exceed revenue. No traditional installment lenders operate in Arkansas. Arkansas residents have to go to other states to obtain a traditional installment loan. It is too far to go for most Arkansas residents. Number of traditional installment loans (in sample) per 10,000 population, in Arkansas and border counties, September 2013.

FIGURE 2. SOME REPRESENTATIVE PRICES, 1913 VS. 2013

	1913	2013	Annual Growth Rate	Percentage Change
Loaf of Bread	**$0.06**	**$1.42**	**3.2%**	**2436%**
Pound of Coffee	**$0.30**	**$5.90**	**3.0%**	**1874%**
Pound of Sugar	**$0.06**	**$0.68**	**2.5%**	**1078%**
One Dozen Eggs	**$0.37**	**$1.93**	**1.6%**	**418%**
Pound, Sirloin Steak	**$0.24**	**$5.71**	**3.2%**	**2297%**
Hourly Wage Rate, Teamster (1-Horse vs. 18-Wheels)	**$0.21**	**$21.63**	**4.7%**	**10451%**
Typical Rate Cap, Small Dollar Installment Loan (1916 and 2016)	36%	<=36%	**0.0%**	**0%**
Consumer Price Index	**9.9**	**233.0**	**3.2%**	**2258%**

Sources: Tim McMahon, "Food Price Inflation Since 1913," *InflationData.com*, March 21, 2013; Rick Suttle, "Union Truck Driver Pay Scales," *Houston Chronicle*, accessed February 8, 2016.

FIGURE 3. STATE INTEREST RATE CAPS BY SIZE FOR TRADITIONAL INSTALLMENT LOANS, 2016



Source: Black and Miller, "Examining Some Arguments Made by Interest Rate Cap Advocates."

TESTIMONY OF W. DENNIS SHAUL

CHIEF EXECUTIVE OFFICER

COMMUNITY FINANCIAL SERVICES ASSOCIATION OF AMERICA

BEFORE THE HOUSE FINANCIAL SERVICES SUBCOMMITTEE ON

FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

FEBRUARY 11, 2016

Good afternoon, Chairman Neugebauer, Representative Clay, and other members of the Subcommittee. My name is Dennis Shaul, and I am Chief Executive Officer of the Community Financial Services Association of America (CFSA), the national organization for small-dollar, short-term lending, including payday loans. We are pleased to be here today to discuss the Consumer Financial Protection Bureau's rulemaking process for small-dollar, short-term loans.

Your hearing today takes a look at the Bureau's rulemaking from two important perspectives: its effect on state regulation of these practices, and its impact on consumers. CFSA is concerned with both of these elements, especially its potential impact on consumers. Over the last two decades, CFSA members have worked for and embraced reforms at the state level to achieve a range of specific credit products that will serve our customers well by answering their credit needs and affording them better consumer protection. The customer is at the center of everything we do, and we have a vested interest in seeing them succeed with our products. We believe the Bureau's current proposals will do very little in the way of enhancing consumers' financial well-being, and will cut off an important credit source for millions of Americans. Indeed, consumers will be worse off if these proposals were enacted in their current form.

The Community Financial Services Association of America

CFSA was created in 1999 as a national organization for small-dollar, short-term lenders committed to best business practices that balance strong consumer protections with access to short-term credit for millions of Americans. CFSA member companies represent more than half of all non-bank storefronts in the United States offering payday and installment loans and vehicle title loans, among many other valued financial products and services, and serving more than 19 million American households that use small-dollar, short-term credit as a tool to manage their personal and family finances.

CFSA member companies are licensed and regulated, and they adhere to a code of Best Practices (attached to this statement), which include full disclosure; compliance with all applicable laws; truthful advertising; appropriate collection practices; and pledge to take no criminal action against borrowers for bounced checks or failure to repay. Our members display a list of these 13 Best Practices in all their stores, and also provide consumer guides to all customers regarding the responsible use of small-dollar, short-term credit.

CFSA members fill a vital role in Americans' access to financial services. The FDIC estimates that 51 million Americans, or 20% of all households, are underbanked, and not served by traditional banking products. As many as 76% of Americans are living paycheck to paycheck, without resources to cover unexpected expenses or disruptions in income. Small-dollar, short-term loans of the type our members provide are an essential option for these households — one option among several, which may include incurring late fees, bouncing checks, or allowing services to be cancelled and reconnected at a later date. Compared to these alternatives, payday loans are often not only the most convenient but also the least expensive option.

Loans offered by CFSA members are simple, transparent, cost-competitive and regulated. Eliminating or restricting access to our members' products will not encourage new lenders to enter the marketplace, but rather will force consumers into alternatives that are more complex, less transparent, less cost-competitive and potentially unregulated.

Payday Loans in the Consumer Financial Marketplace

The typical payday loan is a two-week loan for a fee that varies according to state law, but averages $15 per $100 borrowed. The average amount of a payday loan is $355. These are small-dollar loans, typically used to meet expenses, such as a medical bill, rent, or perhaps a late car payment, when income flow is interrupted or additional expenses make the borrower short on funds.

To obtain a payday loan from one of our members, a borrower needs an active checking account, proof of regular income, and proper identification. The loan application process consists of submitting a simple form that contains Truth in Lending (TILA) disclosures and a personal check for the amount of the loan plus a fee. The lender advances the funds, but holds the check for an agreed-upon period (usually two to four weeks). At the end of that time, the borrower returns to the store with cash to redeem the check, or in some instances, the lender cashes the check.

More than 20,000 payday loan stores operate across the United States, making approximately $38.5 billion in loans annually to borrowers in 19 million households. The majority of these borrowers repay the loans on time, without needing to renew them.

Since payday loans emerged in their current form in the early 1990s, thirty-five states have set up licensing, regulatory and supervisory structures for these products. State laws include limits on the amount of an advance; maximum fees and interest rates; limits on the number of times a borrower can renew a loan; a right of rescission; and various additional disclosure requirements. State and federal laws also govern collection practices. In addition, some states have put structures in place to let customers repay these loans under a no-cost extended payment plan. These structures often mirror CFSA's Extended Payment Plan, as mandated by our Best Practices.

Individual states have taken different approaches to the regulation of payday loans, based on the specific needs of their consumers and markets. As each state has tried to strike its own balance between preserving access to small-dollar, short-term credit and enhancing consumer protections, they have learned from the experiences of other states. For instance, state laws differ in maximum loan amounts: all states set a ceiling, usually under $500, but many also tie the maximum loan amount to a percentage of the borrower's income. Some states limit consumers to one or two simultaneous loans. Indiana prohibits renewals, and requires a "cool-off" period of seven days after five consecutive loans. Florida and 13 other states have a statewide database that keeps track of borrowers. Utah allows loans for terms of up to 10 weeks, with a no-cost payment plan available once every 12 months.

Where states have chosen to effectively ban payday lending through the imposition of a rate cap that makes lending unprofitable, the evidence shows that consumers suffer. A study by the Federal Reserve Bank of New York found that both Georgia and North Carolina saw higher incidences of returned checks, bankruptcy filings and complaints to the Federal Trade Commission about collection practices after those states banned payday lending. Consumers who do not have access to payday loans turn to costlier sources of credit and often to the Internet, where lending may be entirely unregulated.

Payday lenders meet a need in the American economy that traditional lenders are unable or unwilling to provide. Banks that once provided small-dollar, short-term loans no longer do so. Banks find these loans unprofitable and unsustainable largely because bank's personnel and real estate costs, the principal drivers of the cost of a payday loan, are much higher on a unit basis than that of a payday lender. The FDIC's Small Dollar Loan Pilot Program, launched in 2008, set a 36% interest rate cap on small-dollar, short-term loans. However, participating banks quickly found that these loans were not practical or profitable. Furthermore, a recent national study commissioned by the American Bankers Association demonstrated that only one percent of banks surveyed currently offer small dollar loans of $500 or less.

In discussing the role of payday loans in the American economy, it is important to recognize that these loans are demand-driven products, and that the demand for these products reflects fundamental economic shifts. Thirty-one percent of Americans do not have a constant, predictable income source, according to a recent report from the Federal Reserve. The nature of credit in our consumer economy has changed over the past two decades. While credit is still a tool used to advance households socially and economically — through mortgages, car loans, student loans and the like — it is also, increasingly, a financial management tool for households struggling to keep afloat.

Payday loans, perhaps once used more often to meet emergency expenses, are now used to offset income disruptions as well. Households with two incomes may have once provided a financial cushion; today, however, two-earner households may also double a household's financial risk. Tools for managing this uncertainty may include overdrafts, late fees, and, yes, payday loans. The vast majority of funds borrowed through payday loans go directly to pay other debts. The availability of small-dollar, short-term credit is a benefit to the consumer that cannot easily be replaced, if at all.

CFPB Regulation of Short-Term, Small Dollar Loans

The Dodd-Frank Act of 2010 authorized the Consumer Financial Protection Bureau to regulate small-dollar, short-term loans, including payday loans. The Bureau has held several different field hearings on payday lending. The CFPB also opened its consumer complaint portal in late 2013, and more recently began to release monthly complaints reports, including data about payday lending practices. Bureau Director Richard Cordray has said that these complaints are the agency's "compass," helping the Bureau identify prioritize areas for action.

Of the hundreds of thousands of consumer complaints the Bureau has received, only 1.5 percent — 12,193, to be exact — have concerned payday loans. The CFPB's monthly updates also report that payday lending is the only industry area that has seen a regular DECREASE in consumer complaint submissions. Nevertheless, the CFPB is pursuing a course that will decimate the industry and leave consumers in need at the mercy of unregulated lenders. Charged with regulating payday loans, the Bureau released a rule outline of proposals in March 2015 that ignores a long history of legislative and regulatory work at the state level, and opts instead for an end to payday lending.

The CFPB's outline, which is still under review by its small business advisory panel, seems entirely disconnected from the reality of how consumers use payday loans, and how the states currently regulate these products.

The stated goals of the CFPB's proposals are to prevent borrowers from becoming trapped by insurmountable, unaffordable debt — the so-called "debt trap" — and to restrict harmful payment collection practices. While these are laudable goals, the CFPB's objectives are based on assumptions that are not valid and seem based on little to no evidence.

Despite nearly 20 years of experimentation and experience at the state level, the CFPB seems to have conducted no analysis of existing state regulatory structures or practices, and has offered no information about how its proposals would interact with state law. The CFPB's outline leaves no room for continuing state experiments or innovations.

Even more importantly, however, the CFPB seems to have conducted no cost-benefit analysis of payday loan products at all. The Bureau seems unaware that these products emerged because customers have urgent needs, and that those needs will not disappear even if the lenders offering those products do.

Any federal regulatory process should begin with a general welfare analysis that looks at how users of payday loans have been helped or harmed by the products. Field hearings and complaints have provided some anecdotal evidence, but the systemic statistical analyses we have seen, such as the New York Federal Reserve's study, argue against the Bureau's assumptions.

The CFPB seems to assume that the suppliers of payday loans push these products on uneducated and unwary borrowers who do not understand the nature of their obligations. Instead, the academic research on this question shows that the opposite is true. The need for these small-dollar, short-term loans is real. Where people cannot find these loans in their communities, they seek them out online. A majority of the states have recognized that payday loans are a demand-driven product, and have determined that these services ought to be available to their citizens.

The CFPB's duty is to balance access to credit with consumer protection, not cut off all access to credit. This is not the public policy outcome Dodd-Frank envisioned or requires, and it harms the consumer. Because the Bureau has not acknowledged the need for or the benefits of these small-dollar, short-term loans, they cannot effectively weigh the potential harm of fees, interest rates, and payment terms.

Addressing Ability to Repay

CFSA's members make loans with the expectation of repayment, and take steps to make sure that borrowers can repay. In developing and implementing our Best Practices, CFSA's members recognize that payday loans are not appropriate products for all borrowers, and that they can become inappropriate products for borrowers who have used them successfully in the past. Unfortunately, some borrowers do seek loans they will never be able to repay. Others customers borrow wisely, but become victims of adverse circumstances.

CFSA's members acknowledge the obligation to give these borrowers a solution. Where state law permits, CFSA's Best Practices provide for an extended payment plan for borrowers who are unable to repay their loans.

The Consumer Financial Protection Bureau's outline would impose an overly restrictive and unworkable new standard for the ability to repay. No available evidence justifies this new standard, which would require the lender to collect additional information from the borrower and make an underwriting decision that payday loans currently do not involve. These new underwriting requirements, combined with a proposed 60-day cooling off period and limits on additional consumer debt, would effectively end payday lending as it currently exists.

With responsible payday lenders out of the market, who will meet those borrowers' needs? Where will those borrowers go? Experience tells us that they will go online, and to lenders that operate outside regulatory structures and the boundaries of law. Borrowers, and those who seek to protect them, will find themselves in uncharted territory.

Moving Forward on Responsible Reforms

CFSA urges the CFPB to look closely at recent state initiatives to protect consumers while ensuring continued access to small-dollar, short-term credit. State laws in Indiana, Michigan, Utah, South Carolina, Florida and Kentucky, among others, enhance consumer protections while allowing responsible lenders to continue to offer credit. Any federal initiative should not only look to the states as models, but should also preserve the opportunity for states to experiment with new approaches to consumer protection and credit availability.

We also urge the CFPB to make its decisions based on empirical data rather than anecdotal information, and carefully weigh the real benefits of these products against their potential harm.

Since the CFPB opened its doors, the Community Financial Services Association and its members have stood ready to help inform and educate stakeholders about the industry and to assist with the rulemaking process. We remain dedicated to advancing financial empowerment for consumers, while supporting and encouraging responsible lending practices. Thank you for the opportunity to share our views. I look forward to any questions the Committee may have.

CFSA[SM]

COMMUNITY FINANCIAL SERVICES ASSOCIATION OF AMERICA

A COMMUNITY OF RESPONSIBLE LENDERS

BEST PRACTICES FOR THE PAYDAY LOAN INDUSTRY

CFSA Members must abide by the following Best Practices:

1. FULL DISCLOSURE. A member will comply with the disclosure requirements of the state in which the payday advance office is located and with federal disclosure requirements including the Federal Truth in Lending Act. A contract between a member and the customer must fully outline the terms of the payday advance transaction. Members agree to disclose the cost of the service fee both as a dollar amount and as an annual percentage rate ("APR"). A member, in compliance with CFSA guidelines where they do not conflict with applicable federal, state or local requirements, will further ensure full disclosure by making rates clearly visible to customers before they enter into the transaction process.

2. COMPLIANCE. A member will comply with all applicable laws. A member will not charge a fee or rate for a payday advance that is not authorized by state or federal law.

3. TRUTHFUL ADVERTISING. A member will not advertise the payday advance service in any false, misleading, or deceptive manner, and will promote only the responsible use of the payday advance service.

4. ENCOURAGE CONSUMER RESPONSIBILITY. A member will implement procedures to inform consumers of the intended use of the payday advance service. These procedures will include the placement of a "Customer Notice" on all marketing materials, including all television, print, radio and on-line advertising, direct mail and in-store promotional materials.

5. ROLLOVERS. Members shall not allow customers to rollover a payday advance (the extension of an outstanding advance by payment of only a fee) unless expressly authorized by state law, but in such cases where authorized the member will limit rollovers to four (4) or the state limit, whichever is less.

6. RIGHT TO RESCIND. A member will give its customers the right to rescind, at no cost, a payday advance transaction on or before the close of the following business day.

7. APPROPRIATE COLLECTION PRACTICES. A member must collect past due accounts in a professional, fair and lawful manner. A member will not use unlawful threats, intimidation, or harassment to collect accounts. CFSA believes that the collection limitations contained in the Fair Debt Collection Practices Act (FDCPA) should guide a member's practice in this area.

8. NO CRIMINAL ACTION. A member will not threaten or pursue criminal action against a customer as a result of the customer's check being returned unpaid or the customer's account not being paid.

9. ENFORCEMENT. A member will participate in self-policing of the industry. A member will be expected to report violations of these Best Practices to CFSA, which will investigate the matter and take appropriate action. Each member company agrees to maintain and post its own toll-free consumer hotline number in each of its outlets.

10. SUPPORT BALANCED LEGISLATION. A member will work with state legislators and regulators to support responsible legislation of the payday advance industry that incorporates these Best Practices.

11. EXTENDED PAYMENT PLAN*. Each member will provide customers who are unable to repay a payday advance according to their original contract the option of repaying the advance over a longer period of time. Such an extended payment plan will be offered in compliance with any requirement in state law to provide an extended payment plan or, in the absence of such a requirement in state law, in compliance with the Best Practice "Guidelines for Extended Payment Plans." A member will adequately disclose the availability of the Extended Payment Plan to its customers in compliance with any requirement in state law for such a disclosure or, in the absence of such a requirement in state law, in compliance with the Best Practice "Guidelines for Extended Payment Plans."

12. INTERNET LENDING. A member that offers payday advances through the Internet shall be licensed in each state where its payday advance customers reside and shall comply with the disclosure, rollover, rate, and other requirements imposed by each such state, unless such state does not require the lender to be licensed or to comply with such provisions, or the state licensing requirements and other applicable laws are preempted by federal law.

13. DISPLAY OF THE CFSA MEMBERSHIP SEAL. A member company shall prominently display the CFSA Membership Seal in all stores to alert customers to the store's affiliation with the association and adherence to the association's Best Practices.

SUPPLEMENTAL GUIDELINES FOR MEMBER COMPANY IMPLEMENTATION OF CFSA BEST PRACTICES ARE INCORPORATED HEREIN BY REFERENCE AND ARE AVAILABLE UPON REQUEST.

** LAWS IN SOME STATES DO NOT PERMIT IMPLEMENTATION OF CFSA'S EXTENDED PAYMENT PLAN (EPP). CFSA IS WORKING WITH REGULATORS IN THESE STATES TO OBTAIN APPROVAL OF CFSA'S EPP AND WITH LEGISLATORS TO PROMOTE ITS ADOPTION INTO STATE LAW.*

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Good afternoon Mr. Chairman and members of the Committee.

My name is Robert Sherrill and I thank you for letting me come here today to tell you about my life and how payday and title loans have helped me when I had nowhere else to turn. I have been told that the type of small loans that I got may no longer be available to me under new regulations coming from Washington.

My story is simple. When I was young no one taught me about money and finances. I didn't know what I was doing and I made mistakes. I got into trouble. When I needed money I sold drugs and I went to prison.

I was in prison for several years. My offenses were not violent. I am not proud of this but my time in prison made me a better man.

When I got out of prison the deck was stacked against me. I could not get a job, no matter how hard I tried. No one would give me a loan. No bank would give me an account. Since no one would give me a job I decided to try to start my own business.

I turned to a local company in Nashville near where I am from. This company was a payday lender called Advance Financial. When I told my story to Advance, they agreed to make me a loan. I also used Advance Financial to cash my checks, buy money orders and pay bills. I used Advance for payday loans and title loans.

When I got my loans, I knew I had to pay them back. The loans were explained to me. When someone is lending you their money they make sure you know you have to pay it back, and when. And how much it costs.

The payday loan I got from Advance was a lifeline. It enabled me to start a business. I started a janitorial business. Advance also gave me the opportunity to some work for them, cleaning the stores.

Today, my business is growing. I am a minority certified business. I belong to the Chamber of Commerce and the Better Business Bureau.

I have continued to use payday and title loans from Advance. Where I am from many people use the services of Advance Financial. When I am on a job, the people on that job don't think about going to a bank when they get paid. They think about going to Advance.

Some of you are probably going to ask me whether I would like for these loans to be cheaper. My answer is there are a lot of things in life that I wish were cheaper. I don't see the government stepping in anywhere else to tell a business what it can charge for their products.

I understood what a payday loan cost me. I understood when it had to be paid back. The loan worked for me. I can also say that there are other places that I could have gone for a loan. You do not want me to tell you about those places or those people. But they are out there. Since Advance was there I had an established place to go. Everything was open and up front.

Thank you.

Testimony of David Silberman
Acting Deputy Director and
Associate Director of Research, Markets, and Regulations
Consumer Financial Protection Bureau
Before the House Committee on Financial Services
Subcommittee on Financial Institutions and Consumer Credit
February 11, 2016

Chairman Neugebauer, Ranking Member Clay, and Members of the Subcommittee, thank you for the opportunity to testify today about the Consumer Financial Protection Bureau's (Bureau or CFPB) extensive and ongoing work related to payday lending. My name is David Silberman, and I serve as Associate Director for Research, Markets, and Regulations at the CFPB, a position I have held since 2011. Last month I also was named as Acting Deputy Director.

In November 2010, I joined the Bureau as part of the implementation team. Prior to the Bureau, I served as General Counsel and Executive Vice President of Kessler Financial Services, a privately-held company focused on creating and supporting credit card and other financial services to membership organizations. My involvement in consumer financial services began when I was Deputy General Counsel of the AFL-CIO. While at the AFL-CIO, I helped to create an organization to provide financial services to union members and the first AFL-CIO credit card program. I began my career as a law clerk to Justice Thurgood Marshall.

As you know, the CFPB is the nation's first federal agency with a sole focus on protecting consumers in the consumer financial marketplace. Through fair rules, grounded on evidence-based findings and stakeholder input, consistent oversight, appropriate enforcement, and broad-based consumer engagement, the Bureau is working to restore consumer trust in the financial marketplace and to level the regulatory playing field for honest businesses. To date, our enforcement actions have helped secure approximately $11.2 billion in relief for millions of consumers victimized by violations of Federal consumer financial laws.

Since 2011, I have led the Research, Markets, and Regulations Division. The division is responsible for articulating a research-driven, evidence-based perspective on consumer financial markets, consumer behavior, and regulations, informing Bureau thinking on priority areas, identifying areas where Bureau intervention may improve market outcomes, and supporting efforts to reduce outdated, unnecessary, or unduly burdensome regulations. Where our research and analysis suggests the need for regulatory intervention, the Bureau seeks to develop regulations which will protect consumers without unintended consequences or unnecessary costs. As part of the rulemaking process, the Bureau carefully assesses the benefits and costs that the regulations we consider may have on consumers and financial institutions. Balanced regulations are essential for protecting consumers from harmful practices and ensuring that consumer financial markets function in a fair, transparent, and competitive manner.

Since the subject of today's hearing is the Bureau's work with respect to short-term, small dollar lending, let me begin by tracing the Bureau's work in this area.

When the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) was enacted, payday loans were a particular area of concern to Congress. Indeed, the Dodd-Frank Act gives the Bureau plenary authority to supervise any entity that offers payday loans regardless of size. As a result, when the Bureau began supervising non-depository institutions in 2012, payday lending was the first industry that was brought into our supervisory program. To that end, the Bureau developed examination procedures for small dollar lenders that were published as part of the Bureau's Supervision and Examination Manual,[1] which is available on our website, consumerfinance.gov.

Bureau examiners use the examination procedures in the Manual to make sure payday lenders – depositories and non-depositories – are complying with Federal consumer financial law. Specifically, the Short-Term, Small Dollar Lending Procedures describe the types of information that the agency's examiners will gather to evaluate payday lenders' compliance management systems (CMS), assess whether lenders are in compliance with Federal consumer financial laws, and identify risks to consumers throughout the lending process. The procedures track key payday lending activities, from initial advertisements and marketing to collection practices.

At the same time, the Bureau decided to begin the process of fact gathering to assess whether there was a need for federal regulations to prevent unfair, deceptive, or abusive acts or practices. In January 2012, the Bureau held a field hearing in Birmingham, Alabama to hear directly from stakeholders and the public about actual consumer experience with small dollar loans, including both loans offered by non-depository institutions and loans offered by certain banks and credit unions. Alabama is a state with one of the highest number of payday lenders per capita in the country. The field hearing included testimony from consumer and civil rights groups, industry representatives, and members of the public and provided the CFPB with insight into the payday lending market. The Bureau invited the Alabama Congressional delegation to that event and was honored to have Congresswoman Terri Sewell attend and participate in the event as well.

During the year that followed the Birmingham field hearing, the Bureau obtained data from a number of payday lenders and banks making short-term, small-dollar loans and engaged in an in-depth study of the market. Based on that study, in April 2013 the Bureau issued a report entitled, *Payday Loans and Deposit Advance Products - A White Paper of Initial Data Findings* (White Paper).[2] The White Paper was one of the most comprehensive studies ever undertaken of the market. It was an important step toward bringing more clarity to the complicated markets for payday lending and deposit advance products. The White Paper also provided market participants with insight into Bureau concerns based on our findings as of that time.

The White Paper found that most payday loans are for several hundred dollars and have finance charges of $15 or $20 for each $100 borrowed. For the two-week term typical of a payday loan, these fees equate to an Annual Percentage Rate (APR) ranging from 391 percent to 521 percent.

[1] *Available at* http://www.consumerfinance.gov/guidance/supervision/manual/.
[2] *Available at* http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf.

If a consumer does not repay the loan in full by the due date or agree to extend the loan for an additional two weeks, the loan agreement typically permits the lender to directly access the consumer's deposit account, such as with the consumer's post-dated check or Automated Clearing House (ACH)[3] authorization, to obtain repayment.

Typically, a consumer's ability to repay the loan while meeting other debts and ordinary living expenses is not taken into account. Eligibility to qualify for a payday loan generally requires proper identification, proof of income, and a personal checking account. No collateral is held for the loan, although the consumer does provide the lender with a personal check or authorization to debit her deposit account for repayment. Credit score are also generally not taken into account. The median borrower studied in the Bureau's analysis reported $22,000 in income.

The White Paper showed that making these short-term loans to low and moderate income consumers without any assessment of the consumer's ability to repay put many consumers at risk of turning short-term, emergency loans into a long-term, expensive debt burden. Additionally, the Bureau found that payday loans and the deposit advance loans offered by a small but then-growing number of depository institutions were generally similar in structure, purpose, and the consumer protection concerns they raise.

Specifically, the White Paper traced over a period of 12 months the experience of borrowers who had a payday loan in the first month covered by the data. It found that the median borrower took out 10 loans over the course of the year and was in debt for 199 days out of the year. The median borrower thus paid over $150 in fees for every $100 borrowed. Moreover, almost a third of the borrowers took out more than 20 loans, paying twice that amount.

During the year following the publication of the White Paper, the Bureau continued its research and analysis as well as its supervisory activities. Also in 2013, the Bureau announced two important updates to its Supervision and Examination Manual. The Bureau informed supervised entities that Bureau examiners may examine a range of products offered by the supervised entity, including title loans, installment loans, and money services. Additionally, the Bureau released guidelines for examiners to identify consumer harm and risks related to Military Lending Act (MLA) violations when supervising payday lenders.[4]

In November 2013, the Bureau took another important step to gain insight into the payday loan market by beginning to take consumer complaints regarding payday lending. Consumer complaints can be an important source of information about problems consumers experience with different financial products and thus play a vital role in the Bureau's work, especially in targeting its supervisory and enforcement activities to companies that appear to pose the greatest risk to consumers. As of January 1, 2016, the Bureau has handled approximately 37,000 complaints related to payday lending, 12,000 were identified by the consumer as payday

[3] ACH stands for Automated Clearing House, which is an electronic network for processing credit and debit transactions, such as direct deposits and consumer payments, such as those pre-authorized when a consumer applies for a payday loan.

[4] Available at: http://files.consumerfinance.gov/f/201309_cfpb_payday_manual_revisions.pdf.

complaints and 24,000 were identified by the consumer as debt collection complaints related to a payday loan.

The next step in the Bureau's study occurred in March 2014 with the publication of a second report, entitled *CFPB Data Point: Payday Lending* (Data Point),[5] which further analyzed the data used in the White Paper. In response to feedback about the methodology used in the Bureau's first report, the Data Point looked at consumers at the start of a borrowing cycle and traced their experience until they paid off their loan and went two weeks without reborrowing. The Bureau found that only 35 percent of borrowers were able to repay the loan when due without quickly reborrowing, and that 15 percent of borrowers took out 10 or more loans in rapid succession. Indeed, the Bureau found that 50 percent of all loans went to consumers in these lengthy loan sequences.

Looking at payday consumers who receive their incomes on a monthly basis, the Data Point found one out of five who took out a payday loan remained in debt for the entire year of the Bureau's study. Payday consumers who fell into this category include elderly Americans and those persons receiving Supplemental Security Income and Social Security Disability.

The Bureau also found that very few consumers managed to reduce the amount they owed over the course of the loan sequence. The more typical pattern was that consumers paid only the fees due and reborrowed the full amount of the principal time after time. Indeed, over 80 percent of consumers owed at least as much on the last loan as they had borrowed initially.

In states with mandated cooling-off periods, where lenders are not permitted to immediately re-lend to consumers paying off a prior loan, the Bureau found that the 14-day renewal rates are nearly identical to the rates in states without these limitations. In other words, these short cooling off periods did not have any material effect in breaking the cycle of indebtedness.

Finally, the Bureau found that over the course of a sequence of loans, 20 percent of consumers ended up defaulting and thus became the object of collections activity. While most of the defaults occurred early in a sequence of loans, a significant percentage of consumers defaulted after having paid substantial fees to continue to roll over or renew their loans.

The Bureau released its second report in conjunction with a second field hearing on payday lending, this one in Nashville, Tennessee. Like the Birmingham hearing, the Nashville hearing gave Bureau staff the opportunity to hear first-hand from consumers, lenders, advocates, and faith leaders about consumer experiences with these products.

Shortly after the release of the Data Point and the Nashville hearing, the Bureau released an edition of its periodic *Supervisory Highlights,* which described findings that the Bureau had made in its payday lending examinations.[6] Specifically, the Bureau reported that examinations had found that a number of payday lenders had not implemented effective compliance

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[5] *Available at* http://files.consumerfinance.gov/f/201403_cfpb_report_payday-lending.pdf.
[6] *See* Supervisory Highlights: Spring 2014, *available at* http://files.consumerfinance.gov/f/201405_cfpb_supervisory-highlights-spring-2014.pdf.

management systems. Generally, CMS concerns covered a range of issues, including lack of oversight of compliance management, ineffective oversight of third-party service providers, inadequate complaint management, failure to adopt appropriate written policies and procedures, failure to adequately train staff, and lack of effective compliance audit programs. At several short-term, small-dollar lenders, Bureau examiners found inadequate compliance management systems for collection activity. Lenders did not adequately monitor collections calls, attempt to understand the root causes of complaints arising from collections practices, provide training for collectors, and properly oversee third-party service providers. As a result of poor record-keeping, some payday lenders have been unable to fully respond to Bureau information requests or examiner inquiries on-site.

Bureau examinations have also found deceptive practices at payday lenders. Upon a borrower's default, payday lenders frequently will initiate one or more preauthorized ACH transactions pursuant to the loan agreement for repayment from the borrower's checking account. At one or more lenders, the Bureau cited a deceptive practice when communications with consumers threatened ACH transactions that were contrary to the agreement, and that the lender did not intend to initiate.

Finally, in October 2014, the Bureau held a government-to-government Tribal Consultation with tribal leaders interested in the subject of small-dollar lending to hear their input as the Bureau was in the process of formulating its proposals. This Consultation, as well as the Bureau's other engagements with tribal nations, are discussed later in this testimony.

All of this brings me to the outline of proposals under consideration which the Bureau released in March 2015, as the first formal step in the rulemaking process.

As outlined above, over the course of three years the Bureau engaged in intensive analysis of the short-term and longer-term credit markets for personal loans. The Bureau considered the history of the demand for such loans and the conditions that create such demand. The Bureau focused carefully on how people are affected by the kinds of credit products that have evolved to meet this demand. After much study and analysis, in March 2015, the Bureau outlined the proposals under consideration[7] designed to protect borrowers from the risks the Bureau's research has identified. The proposals released for consideration would cover payday, vehicle title loans, deposit advance products, and certain high-cost installment loans and open-end loans.

To collect feedback on the approach from small lenders, the Bureau published the outline of the proposals under consideration in preparation for convening a Small Business Review Panel, and obtaining feedback from Small Entity Representatives pursuant to Regulatory Flexibility Act. The proposals under consideration cover both short-term and longer-term credit products that are marketed heavily to financially vulnerable consumers. The Bureau recognizes consumers' need for affordable credit, and is concerned that the practices often associated with these products, such as failure to underwrite for affordable payments, repeatedly rolling over or refinancing

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[7] *Available at* http://files.consumerfinance.gov/f/201503_cfpb_outline-of-the-proposals-from-small-business-review-panel.pdf.

loans, holding a security interest in a vehicle as collateral, accessing the consumer's account for repayment, and performing costly withdrawal attempts, can trap consumers in debt. These debt traps can also leave consumers vulnerable to deposit account fees and closures, vehicle repossession, and other financial difficulties.

The core of the proposals under consideration is aimed at ending debt traps with a requirement that, before making a covered loan, lenders would be obligated to make a good-faith, reasonable determination that the consumer has the ability to repay the loan. That is, the lender would have to determine that after repaying the loan, the consumer would have sufficient income to pay major financial obligations, including a rent or mortgage payment and other debt, and also to pay basic living expenses, such as food, transportation, childcare or medical care, without the need to reborrow in short order.

Until recently, a bedrock principle of all consumer lending was that before a loan was made, the lender would first assess the consumers' capacity to repay the loan. In a healthy credit market, both the consumer and the lender succeed when the transaction succeeds - the consumer meets his or her need and the lender gets repaid. This proposal seeks to address consumer harm caused by unaffordable loan payments due in a short period of time.

The proposals under consideration to require lenders who make short-term, small dollar loans to assess a prospective borrower's ability to repay and avoid making loans with unaffordable payments parallels a rule adopted by the Federal Reserve Board in 2008, in the wake of the financial crisis. That rule requires lenders making subprime mortgages to assess the borrower's ability to repay. The proposals under consideration also parallel ability to repay requirements that Congress enacted in the Credit Card Accountability Responsibility and Disclosure Act (CARD Act) in 2009 for credit card issuers, and in the Dodd-Frank Act in 2010, for all mortgage lenders.

As an alternative to the basic prevention requirements of assessing a borrower's ability to repay, the proposals under consideration also contain what we have called protection requirements. These requirements would allow lenders to extend certain short-term loans without conducting the ability to repay determination outlined above, so long as the loans satisfy certain screening requirements and contain certain structural protections to prevent short-term loans from becoming long-term debt. Under this proposal, lenders would have the option of either satisfying the ability to repay requirements or satisfying the alternative requirements.

The protection requirements the Bureau outlined for consideration would allow lenders to make up to three loans in succession, with a maximum of six total loans or a total of 90 total days of indebtedness over the course of a year. The loans would be permitted only if the lender offers the consumer an affordable way out of debt. The Bureau is considering two options for paths out of debt either by requiring that the principal decrease with each loan, so that it is repaid after the third loan, or by requiring that the lender provide a no-cost "off-ramp" after the third loan, to allow the consumer to pay the loan off over time without further fees. For each loan under these alternative requirements, the debt could not exceed $500, carry more than one finance charge, or require the consumer's vehicle as collateral. After a sequence of three loans, a lender could not take advantage of the protection requirements again for a period of 60 days.

The Bureau's proposals under consideration raised the question of whether offering such an alternative for lenders, including small lenders that may have difficulty conducting an ability to repay determination with a residual income analysis, may be helpful in providing access to credit to consumers who have a genuine short-term borrowing need, while still protecting consumers from harms resulting from long-term cycles of debt. This alternative would also reduce the compliance costs for lenders.

Stakeholders on all sides of the issue have provided valuable feedback on the proposals under consideration. Consumer advocates, for example, have argued that the Bureau should not permit any lending which does not meet the basic ability to repay standard. They argue that consumers need prevention *and* protection - not either, or. Industry stakeholders, on the other hand, argue that the protection requirements under consideration are too restrictive because those requirements would allow no more than three loans in a row and no more than six loans per year. Industry stakeholders want to be able to continue making many more loans to consumers without regard to their ability to repay. State policymakers have urged the Bureau to both protect consumers across all small dollar lending markets and to seek feedback from the states on their regulation of small dollar lending products. Tribal governments have urged the Bureau to consider the impact of any regulation on the revenue the tribes receive from these products.

The Bureau released the outline of the proposals under consideration at a field hearing held in Richmond, Virginia. Like the prior two field hearings on this subject, the Richmond event provided the Bureau with a rich and wide-ranging set of perspectives from consumers, lenders, advocates, and faith leaders.

In over 10 months since the Bureau formally released the outline of proposals under consideration, the Bureau has engaged in further outreach and engagement with a wide variety of stakeholders. That process began by convening a Small Business Review Panel and meeting with 27 Small Entity Representatives, including not only storefront payday and vehicle title lenders, but also banks and credit unions, tribal lenders, and online lenders. The Small Business Review Panel submitted its report to the Bureau last June, and the Bureau is continuing to consider those recommendations.

In addition to participating in the Small Business Review Panel, the Bureau has continued to seek input through formal meetings between Bureau staff and various stakeholders and through many more informal meetings and discussions. From October 14, 2014 to September 15, 2015, the Bureau conducted over 30 meetings on consumer lending with nonprofit groups, including consumer advocacy, faith-based, and civil rights organizations. In the same period, the Bureau met to discuss consumer lending with state, municipal and Tribal officials a total of 17 times, and with representatives from industry and trade associations and over 30 times. A group of lenders and advocates also joined together to discuss areas of agreement, and the Bureau met with this group three times to obtain its consensus recommendations as well as to hear areas of discussion.

Additionally, the Bureau has taken special care to acknowledge and respect the unique legal relationship between the federal government and tribal nations. This relationship is a critical one, and its importance is reflected in the Bureau's Tribal Consultation Policy,[8] as well as the Bureau's extensive outreach and engagement with the tribes.

The Bureau finalized its Tribal Consultation Policy in April 2013. Since the Policy went into effect, the Bureau has conducted two Tribal Consultations on the CFPB's potential rulemakings for payday, vehicle title, and similar loans and welcomes input on ways that we can improve our Tribal Consultation Policy. In both the drafting of the Tribal Consultation Policy and the execution of the two Consultations, the Bureau conferred with other federal agencies, including the U.S. Department of Interior, to draw on their experiences and incorporate their best practices for effective Tribal Consultation. The Bureau is committed to ensuring that our Tribal Consultation policy provides a meaningful opportunity for the Bureau to consult with tribes on policies that affect them.

Specifically, the Bureau invited all 566 federally recognized tribes[9] to two Consultations related to the Bureau's small-dollar lending rulemaking proposals. These Consultations were frank discussions that allowed tribal leaders to share their views about the proposals with the Bureau. The first of these Consultations took place in November 2014, before the Bureau had formulated the outline of proposals under consideration. The second took place in June 2015 to discuss the Bureau's outline. The Bureau also has held a number of other meetings with tribes at the Bureau's headquarters and across the country.[10] The tribe's feedback is being considered as the Bureau moves forward on a Notice of Proposed Rulemaking.

The Bureau also spoke directly to state and federal regulators and policy makers at field hearings and in other settings across the country. In June 2015, the Bureau's Office of Consumer Advisory Board and Councils, which is charged with managing the Bureau's advisory groups and serving as the liaison between advisory group members and the Bureau, held meetings and field events associated with the Bureau's Consumer Advisory Board (CAB) in Omaha, Nebraska about payday, vehicle title, and similar loans. The CAB advises and consults with the Bureau in the exercise of its functions under the Federal consumer financial laws, and provides information on emerging practices in the consumer financial products and services industry, including regional trends and other relevant information. The events included a community roundtable, welcome reception with community leaders and representatives, an industry and community engagement panel, a community tour including a visit to a payday lending store, CAB committee meetings, and a day-long public session, which focused on the Bureau's proposals under consideration, trends in payday and auto-title lending, and mortgages. In addition to the Omaha

[8] *Available at* http://files.consumerfinance.gov/f/201304_cfpb_consultations.pdf.

[9] The Bureau is aware that the U.S. Department of the Interior recognized a 567th tribe on July 2, 2015 and intends to include this additional tribe in all future tribal engagements. *See* Interior Department Issues Final Determination for Two Federal Acknowledgement Petitioners, Dept. of Interior, July 2, 2105, *available at* www.indianaffairs.gov/cs/groups/public/documents/text/idc1-030832.pdf.

[10] Associate Director Zixta Martinez addressed a plenary session of the 2014 National Congress of American Indians (NCAI) Annual Meeting, and Bureau leadership met with the NCAI Executive Committee during that event. In addition, the Bureau has partnered with tribes on key consumer education and engagement programs related to K-12 financial education and the Bureau's *Your Money Your Goals* initiative.

meetings, the Consumer Advisory Board convened six discussions on consumer lending, the Community Bank Advisory Council held two discussions, and the Credit Union Advisory Council conducted one discussion.

Since October 2014, Bureau staff has held meetings and roundtables with over 40 entities from industry, including 13 national trade associations and over 30 of their member businesses. The entities represented small dollar lenders operating in communities and online, vehicle/title lenders, installment lenders, retail banks, community banks and credit unions. The meetings were open forums for industry groups to share their knowledge of small dollar lending operations, underwriting processes, state laws, and anticipated regulatory impact.

The Bureau's Office of Research has reviewed numerous industry-sponsored, advocate-sponsored and independent research reports on payday, auto title and similar lending in the United States. It has invited several of the authors to share their methods and data via follow-up teleconferences or in-person visits here in Washington.

Bureau leaders, including Director Cordray, have also spoken at events and met with industry representatives. In February 2015, Bureau leaders met with the Board of Directors of the Community Financial Services Association of America. These meetings have provided the Bureau with opportunities to hear the industry's insight and suggestions for how to craft a proposed rule that would preserve access to small dollar lending in underserved communities.

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The Bureau continues to receive feedback from Congress, State, Local and Tribal officials, consumers, industry, and others on its proposal under consideration. The Bureau's next step will be to formally issue a proposed rule. Once the proposal is issued, the public will be invited to submit written comments. The Bureau will carefully consider those comments before final regulations are issued. The Bureau will move as quickly as reasonable, recognizing the importance and the complexity of the subject, and will be thoughtful and thorough as we continue this work.

In the end, the Bureau intends for consumers to have a marketplace that works both for short-term and longer-term credit products. For lenders that sincerely intend to offer responsible options for consumers who need such credit to deal with emergency situations, the Bureau is making conscious efforts to keep those options available. There should be opportunities available for loans with affordable payments that will enable the consumer to repay the loan and still meet their other obligations and pay their living expenses. Lenders that rely on fees and profits from consumers in long-term debt traps, however, will not be able to continue business as usual. Consumers should be able to meet their needs without finding themselves stuck in an extended debt trap.

Chairman Neugebauer, Ranking Member Clay, and Members of the Subcommittee, thank you for helping us to achieve that goal and for the opportunity to testify today. I look forward to your questions.

Protecting Credit Since 1916
American Financial Services Association

United States House of Representatives
Subcommittee on Financial Institutions and Consumer Credit

Hearing on:

Short-term, Small-Dollar Lending: The CFPB's Assault on Access to Credit and Trampling of State and Tribal Sovereignty

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Thursday, February 11, 2016

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Statement for the Record

by the

American Financial Services Association

Good Afternoon, Mr. Chairman, Ranking Member Clay, and Members of the Subcommittee. My name is Kelvin Simmons I am here today on behalf of the American Financial Services Association (AFSA) and the millions of traditional installment loan (TIL) customers that AFSA's member companies have served over the last 100 years.

Thank you very much for this opportunity to talk to you today about the Consumer Financial Protection Bureau's (Bureau) proposal for small-dollar loans and the impact that it will have on deserving consumers.

I ask that my full statement be submitted for the record so I can focus on three basic issues: (1) the need for small-dollar credit; (2) the fact that depository institutions are not equipped to address that need; and (3) the demonstrated ability of traditional installment lenders to offer safe and affordable access to small-dollar loans. This ability has been recognized by the Center for Financial Services Innovation, the National Black Caucus of State Legislators (NBCSL) and the National Hispanic Caucus of State Legislators. But first, let me paint a picture of my own experience and how I see the issue from the perspective of the community where I was born and raised – Kansas City, Missouri.

I am a former state director of economic development in Missouri. During my tenure as the director, the state's banks, credit unions and financial services divisions were under my executive authority. I was President/CEO of one of the largest community development corporations in Missouri and I was twice elected to the Kansas City Council in the very community where I was born and raised. The zip code where I was born and raised (64130) lies in Missouri's 5^{th} Congressional District. My parents and I lived and owned homes in that zip code for over 50 years.

A study done between 2006 – 2012 by Dr. Rickey Keys for NBCSL in key urban cities across the United States, including Kansas City, showed that in that same zip code there were no banks, one credit union, a substantial numbers of check cashing outlets, and a significant number of payday loans and title loan stores. There were no locations that offered a choice for safe, reliable and affordable small-dollar loans. I characterized this as living in a community that had a financial services desert.

To further illustrate my financial services desert point, I served as Commissioner of Administration for the state of Missouri from 2009 – 2012. In that role, I had dual signatory authority with the Missouri State Treasurer to issue all checks on behalf of the state of Missouri. My name appeared on every check issued by the state. Even though my name appeared on all the state checks, there was not a bank where I could deposit that check in my hometown zip code.

In that same zip code, the average credit score was 606, which meant it was harder to obtain credit for car loans, mortgages, and items for which credit was needed. As you may have concluded, a number of citizens in this community were unbanked or underbanked. It is an understatement to say that in a financial services desert it is very difficult to obtain safe and affordable small-dollar loan products. It is concerning because it is inevitable that a car will break down, children will need school supplies, and emergencies will happen. The need for a safe, affordable small-dollar loan product is significant.

Last year in Missouri, there were over two million small-dollar loans made to Missouri citizens. Missouri has a population of just over five million people. The need is definitely demonstrated. These loans come in a variety of products, but after reviewing a number of those products, I believe one of the safest and most affordable small-dollar loan products is a TIL. I fear that if the TILs are not available because they become harder to obtain, the community will struggle with more predatory products or be left with no choices at all. This could be an unintended consequence to a well-meaning proposal.

I believe that there is a very obvious need that my former community and others like it have for high-quality, small-dollar credit products. The national need has been recognized by the Director of the Bureau, Richard Cordray, who testified last fall about preserving the ability of installment lenders and others to continue to make responsible loan products. Additionally the Federal Deposit Insurance Corporation (FDIC) undertook a pilot program to get banks to lend in this space.

However, despite years of effort, the FDIC has found that banks do not see small-dollar loans as a profitable business line. To illustrate my point even further, Liberty Bank, one of the nation's largest African-American owned banks, and one which has a location in Kansas City, participated in the FDIC pilot program. I worked with Liberty Bank in Kansas City and they do a terrific job of lending in the community. But in the pilot program, they concluded that despite their desire to meet the small-dollar lending need, it was difficult to make those loans work over time without some form of a subsidy. I commend them for their attempts to work with their customers because this is difficult.

So the obvious question is – who is best suited to meet the need for high-quality, small-dollar loans? The answer is traditional installment lenders making TILs. What are TILs? TILs are fixed-rate, fully-amortizing, small-dollar loans repaid in equal monthly payments or installments. The industry average loan is for $1,500. The average monthly payment is $120 and the average term is 15 months. The average loan amount, monthly payment, and average term vary by lender. TILs are affordable to each borrower's monthly budget. They are "plain vanilla" loans with transparent, easy-to-understand terms, due dates and payment amounts. Installment lenders underwrite loans based on consumers' credit reports and other factors. At the time of origination, each and every loan is made with the highest confidence and expectation that it will be paid back in full and on time.

As I mentioned earlier, the Center for Financial Services Innovation has published a Compass Guide to Small Dollar Credit that I have included in my full statement, which outlines high quality characteristics that reflect TILs.

A high-quality small-dollar loan as one that:

1. Is made with a high confidence in the borrower's ability to repay;
2. Is structured to support repayment;
3. Is priced to align profitability for the provider with success for the borrower;
4. Creates opportunities for upward mobility and greater financial health;

5. Has transparent marketing, communications, and disclosures;
6. Is accessible and convenient; and
7. Provides support and rights for borrowers.

In 2014, the Missouri legislature passed SB 866 to separate and distinguish TILs as a high quality product distinct from payday and title loans. In December of 2015, the NBCSL adopted a resolution, also in my full statement, endorsing the development of responsibly underwritten small-dollar installment loans. The resolution identifies the key structural qualities of safe and affordable loans as being a schedule for repayment in substantially equal installments, and the lenders' assessment of the borrower's stability, ability, and willingness to repay.

The resolution also addresses the issue of the cost of the loan, pointing out that the annual percentage rate (APR), a required disclosure to borrowers, is not always the best indicator of actual cost. It affirms the importance of ensuring consumers' access to low-cost, rather than low-rate, loans. Historically, APR rate caps have been a favored means of regulation, despite not differentiating between loan types.

The resolution states that lenders should examine factors such as a borrower's credit history, monthly disposable income available to service the debt, employment and existing debt as a condition of making a loan. It also recommends that lenders be community-based, licensed and audited by the state, and actively participate in community and charitable activities, particularly those relating to financial literacy.

The Bureau's stated objective of the small-dollar proposal is to protect consumers from the harmful characteristics of payday, title loans, and similar short-term loans. These types of loans all have repayment schedules that are typically three months or less consisting of one to three payments and may include a balloon payment.

We understand the Bureau's concerns about these loans. We agree that some loans may trap borrowers in a cycle of debt. And we agree that the Bureau should enact common sense protections to ensure that consumers have access to credit that helps, not harms them. As I have pointed out, TILs are safe and affordable loans that serve many purposes, including helping consumers out of debt traps.

Unfortunately, the proposal is so broad that it covers all payday, title loans, and many TILs. How are TILs different from payday loans? Unlike payday loans, TILs do not have prepayment penalties or large, one-time balloon payments. They are fully-amortizing loans. TILs are paid off through equal monthly payments of principal and interest that provide a clear roadmap out of debt.

If the Bureau does not limit the rulemaking to payday and title loans, lenders may choose not to make loans above 36% all-in APR. This will cut-off access to loans below $4,000 for two main reasons.

First, traditional installment lenders have worked tirelessly to distinguish themselves from payday lenders. They cannot afford the reputational risk of being associated with payday lenders.

To avoid being seen as anything resembling payday or title, they may choose not to offer a product that is labeled by the Bureau as a "covered loan" under a payday and title rule. This will leave consumers with limited options. Consumers will have to borrow more to stay under 36% all-in APR set by the Bureau, provided they qualify. Or, more likely, consumers will go to disreputable "lenders" (or loan sharks) to get the money they need.

The second reason that lenders may decide against offering covered loans is that they simply will not be able to make small-dollar loans, especially with onerous and unnecessary income verification standards, at 36% all-in APR. According to a study done by three academics using industry data, in order to make a break-even loan at 36% APR, the loan would have to be made for at least $2,600. For a loan to be made profitably at 36% all-in APR, the loan would have to be for around $4,000. In a Bureau field hearing on military lending, almost all the panelists told Bureau staff that it was impossible to make such loans. As I mentioned previously, the FDIC pilot study on small-dollar loans also showed that banks could only make these loans as loss-leaders.

In conclusion, I hope that I have shown the members of the subcommittee that: (1) there is a great need for high-quality, small-dollar loans in many communities, like the one in which I was raised; (2) TILs meet the definition of high-quality, small-dollar loans and are meeting the need in many of these communities; and (3) most importantly, the Bureau must be careful to preserve the ability of installment lenders to offer these responsible loan products as Director Cordray indicated in his testimony before this committee last September.

Thank you and I look forward to answering any questions the Subcommittee members may have.

APPENDIX I

BUSINESS AND ECONOMIC DEVELOPMENT
Resolution BED-16-21

A RESOLUTION PROMOTING SAFE AND AFFORDABLE LENDING PRACTICES

WHEREAS, the National Black Caucus of State Legislators (NBCSL) has always been committed to financial empowerment through improved access to capital as well as a marketplace that offers safe and affordable lending products and services;

WHEREAS, in 1998, the United Nations defined poverty as the lack of access to certain essential goods and services, including access to credit;

WHEREAS, the need for small-dollar closed end credit exists in every community throughout the country;

WHEREAS, not all loan types are equally safe and affordable, and the structure of certain loans significantly increases the likelihood of borrowers falling into a cycle of debt;

WHEREAS, responsibly structured credit is essential to support a household's ability to save, build a sound credit history, and facilitate crucial investments that can provide a foundation for other wealth-building activities;

WHEREAS, the key structural qualities of closed end loans that are safe and affordable are that the lender makes a good faith effort to assess the borrower's ability to repay the loan and that the loan is repayable in substantially equal installments, with no balloon payments;

WHEREAS, it is the intention of this body to ensure access to loans that are low cost rather than low rate, since consumers buy goods with dollars and cents and not with annual percentage rates;

WHEREAS, NBCSL passed Resolution BFI-13-14, "PROMOTING SAFE AND AFFORDABLE LENDING PRACTICES," among the 2013 Ratified Resolutions and that resolution promotes adequate safeguards to protect the general community from abusive financial services;

WHEREAS, this resolution maintains that responsibly structured credit is an essential part of the wealth-building ecosystem, that includes building a sound credit history, as well as saving and wise investment;

BUSINESS AND ECONOMIC DEVELOPMENT
Resolution BED-16-21

WHEREAS, all small-dollar closed end credit should be "fully amortized," meaning that the Total of Payments defined under the Federal Truth in Lending Act, is repaid in substantially equal multiple installments at fixed intervals to fulfill the consumer's obligation;

WHEREAS, small-dollar closed end credit, when used prudently by consumers, may help establish, re-establish or improve credit scores;

WHEREAS, all small-dollar closed end credit should be reported to at least one of the three major credit agencies: Equifax, Experian and TransUnion;

WHEREAS, all small-dollar closed end credit should provide that the Total of Payments as defined in the Truth in Lending Act be repaid over at least a 120 day period in substantially equal payments; and

WHEREAS, Traditional Installment Loan Lenders offering amortizing small-dollar closed end credit, may prevent cycle of debt issues inherent with non-amortizing balloon payment loans.

THEREFORE, BE IT RESOLVED, that the NBCSL supports small-dollar closed end credit in the form of traditional installment loans;

BE IT FURTHER RESOLVED, that Traditional Installment Loan Lenders should be reasonably protected;

BE IT FURTHER RESOLVED, that the NBCSL supports the expansion of Traditional Installment Loans as an affordable means for borrowers to establish and _secure small dollar closed end credit while preventing cycle of debt issues inherent with non-amortizing balloon payment loans; and

BE IT FINALLY RESOLVED, that a copy of this resolution be transmitted to the President of the United States, Vice President of the United States, members of the United States House of Representatives and the United States Senate, and other federal and state government officials as appropriate.

SPONSOR: Representative Karla May (MO)

Committee of Jurisdiction: Business and Economic Development Policy Committee

Certified by Committee Co-Chairs: Senator Jeffery Hayden (MN) and Representative Angela Williams (CO)

Ratified in Plenary Session: Ratification Date is December 4, 2015

Ratification is certified by: Senator Catherine Pugh (MD), President

APPENDIX II

COMPASS PRINCIPLES

The Compass Guide to Small-Dollar Credit

CFSI Center for Financial Services Innovation

www.cfsinnovation.com

Table of Contents

1. ACKNOWLEDGEMENTS

This Guide was developed by CFSI, with the support of the Ford Foundation and the Omidyar Network, and in consultation with a wide range of advisors from industry, consumer advocacy organizations, nonprofits and academia. These include:

Appleseed
Aspen Institute
BillFloat
Brundage Management Company
Capital One
Center for Responsible Lending
Clarifi
Community Development Finance
Consumer Federation of America
Consumers Union
Core Innovation Capital
Corporation for Enterprise Development (CFED)
Credit Builders Alliance
Enova
Float Money
Ford Foundation
Guaranty Bank
KeyBank
Kinecta Federal Credit Union
L2C, Inc.
LendUp
LexisNexis Risk Solutions
MasterCard
MetaBank/Meta Payment Systems
MetLife Foundation
Mission Asset Fund
National Consumer Law Center
National Council of La Raza
National Federation of Community Development Credit Unions
National Urban League
Neighborhood Housing Services of Greater Cleveland
NetSpend
New America Foundation, Asset Building Program
North Carolina State Employees' Federal Credit Union
Omidyar Network
One PacificCoast Bank
One PacificCoast Foundation
Progreso Financiero
Regions Bank
San Francisco Office of Financial Empowerment
Self-Help Federal Credit Union
Sunrise Banks
Texas Appleseed
The Leadership Conference on Civil and Human Rights
The Pew Charitable Trusts
Think Finance
UNC Center for Community Capital
Urban Institute
Visa
ZestFinance

We are grateful for the wisdom and guidance of our advisors in this process. However, the Guide does not necessarily reflect the individual views of these advisors. CFSI takes full responsibility for the end product, and all comments, questions or suggestions should be directed to CFSI.

2. OVERVIEW

Why a Guide on Small-Dollar Credit?

Access to high-quality small-dollar credit is a key component of a successful financial life for many Americans. Millions of people use small-dollar credit products every year; in 2012, consumers spent an estimated $41.2 billion on such products (see Box 1). Having the ability to borrow relatively small sums, on reasonable terms, can help individuals weather a financial shock, smooth income fluctuations, build a positive credit history, and facilitate a wealth-building purchase. However, millions of Americans do not have access to small-dollar credit or only have access to high-cost, low-quality small-dollar credit products that too often lead them into a cycle of repeat usage and mounting debt.

The Center for Financial Services Innovation (CFSI) believes the opportunity and need are great to improve the marketplace for small-dollar credit. Well-designed products have the potential to help people turn a momentary credit need into an opportunity to improve their financial well-being. Voluntary standards for quality in the small-dollar credit marketplace can facilitate innovation by providing a roadmap for lenders who seek to meet consumers' credit needs in a responsible and sustainable way. With the support of the Ford Foundation and the Omidyar Network, CFSI convened a network of expert advisors to develop this set of specific guidelines and best practices for high-quality small-dollar credit as part of our Compass Principles program.

BOX 1 *There is no one universally-accepted definition of what constitutes "small-dollar credit." Broadly speaking, the term typically refers to consumer loans of less than $5,000 with terms ranging from as little as two weeks to as long as three years.*

According to CFSI's 2012 Financially Underserved Market Size Study, consumers spent an estimated $41.2 billion on small-dollar credit products in 2012; these include deposit advance, refund anticipation checks, pawn loans, payday loans, overdraft protection, secured and subprime credit cards, auto title loans, installment loans and rent-to-own. The study also includes revenue estimates for subprime and Buy Here Pay Here auto loans, but as these tend to be larger loans with longer terms, they are not considered "small-dollar credit" for the purposes of this Guide.

The practices in the Guide are generalizable to all types of small-dollar credit, except where it is indicated that the practice refers specifically to closed-end loans or lines of credit. The Guide does not suggest guidelines for overdraft protection, as it is sufficiently different from other types of short-term credit that it falls out of the scope of this Guide. The guidelines do, however, apply to overdraft lines of credit.

2012 Financially Underserved Market Size Study. Center for Financial Services Innovation, December 2013.

Background on the Compass Principles

The Compass Principles are aspirational guidelines to assure quality innovation and execution in financial services – services that enable people to transact, borrow, save and plan in ways that are beneficial to the consumer and profitable for industry. The Principles reflect the belief that the U.S. financial services marketplace can actively contribute to improving people's lives, and deliver sustainable value to all consumers and providers.

The four Compass Principles are:

- ***Embrace Inclusion: Responsibly expand access.*** Consumers, including those from traditionally underserved groups or communities, are creatively reached and well-served with a relevant suite of quality, affordable financial services that promote consumer choice and are provided in a safe, dignified and convenient manner.

- ***Build Trust: Develop mutually beneficial products that deliver clear and consistent value.*** Consumers can clearly understand and derive value, without pitfalls or unwelcome surprises, from financial products designed to align provider and consumer goals.
- ***Promote Success: Drive positive consumer behavior through smart design and communication.*** Consumers are empowered to make wise money choices via smart product design and guidance that is relevant to their specific concerns and financial situations, coincides in a timely fashion with key life events or decisions, and is immediately actionable.
- ***Create Opportunity: Provide options for upward mobility.*** Consumers have appropriate options that create opportunities for increased financial prosperity, and they are encouraged to pursue those opportunities.

The Compass Principles are guided by the following six values:

- ***Profitability and Scalability:*** The Compass Principles provide a framework that is pragmatic, achievable, financially sustainable and scalable.
- ***Deep Customer Knowledge:*** The Compass Principles are formulated and must be implemented with a solid understanding of real consumer needs.
- ***Safety:*** The Compass Principles support and build upon consumer protections.
- ***Variation and Choice:*** The Compass Principles allow for judgment on the part of individual providers, because there is no one right way to meet all customer needs.
- ***Relationships:*** The Compass Principles focus on success for both consumers and providers and encourage viewing each customer interaction as an opportunity for a long-term relationship.
- ***Cross-Sector Participation:*** The Compass Principles incorporate the perspectives of a range of practitioners and experts.

For additional information on the Compass Principles, please visit www.compassprinciples.com.

Scope of the Guide

This Guide seeks to define characteristics of a high- quality small-dollar credit product. **It does not assume, however, that credit is the answer for every consumer.** For most people, the ability to borrow is an essential tool – along with the ability to transact, to save and to plan – for successfully managing their financial lives. Access to credit can help weather a financial shock, smooth income fluctuations, build a positive credit history, and facilitate a wealth-building purchase – all of which are keys to overall financial health.

For some people, however, access to credit might only worsen their financial situation. When people who face a chronic income shortfall or who already have debts they cannot manage use credit to meet their basic needs, they put themselves at risk of falling into a dangerous cycle of debt. Absent some significant change in their short-term financial situation, they will likely need to borrow again to repay the loan while still meeting their basic needs and other financial obligations in the next period. Mounting fees and interest can quickly spiral out of control, creating a new financial strain on the individual who is already struggling.

This Guide emphasizes responsible underwriting as a key component of a high-quality small-dollar credit product. As lenders' underwriting capability improves, due in part to the increased availability and utility of new data sources, some consumers who are currently accessing credit may no longer qualify.

It is difficult to estimate with certainty how many consumers might no longer qualify with more responsible underwriting. Research shows that some current small-dollar credit borrowers have expenses that regularly exceed their income; these are likely many of the same borrowers who find themselves in a destructive cycle of debt when they cannot repay their loans.[1] For these individuals, non-credit solutions such as job training, income support programs, budgeting help or savings tools might be more

1 CFSI's research suggests that approximately 30% of small-dollar credit borrowers have expenses that regularly exceed their income, according to their self-reported reasons for seeking credit. Regression analyses also found that borrowers who report this reason for seeking credit are more likely than other borrowers to rollover or extend their payday, pawn, auto title or deposit advance loan. "A Complex Portrait: An Examination of Small-Dollar Credit Consumers." Center for Financial Services Innovation, August 2012.

appropriate. Adequate consumer protections are also needed to shield vulnerable individuals against lending practices that are harmful or deceptive. While finding ways to support and protect the most vulnerable consumers is critically important, it is outside of the scope of this Guide.

Definition of Quality

This Guide defines a high-quality small-dollar loan as one that:

1. Is made with a high confidence in the borrower's ability to repay
2. Is structured to support repayment
3. Is priced to align profitability for the provider with success for the borrower (see Box 2)
4. Creates opportunities for upward mobility and greater financial health
5. Has transparent marketing, communications, and disclosures
6. Is accessible and convenient
7. Provides support and rights for borrowers

BOX 2 *At the heart of the Compass Principles is a commitment to mutual success in the customer-provider relationship. By reframing each customer interaction as a source of many future engagements, and aligning company culture and incentives accordingly, providers can successfully and profitably offer, structure, and sell products and services that promote a positive customer relationship. In the case of small-dollar credit products, it means designing business models and products such that the lender's profitability depends on borrowers' success with the product (i.e. high rates of on-time repayment, low default rates, etc.) without re-borrowing and while still meeting basic needs and other financial obligations; a high default rate should never be accepted as just another cost of doing business. It also means that employees should be incentivized based on success of the loan portfolio, not on the number of loans booked, and that borrowers should never be encouraged to refinance their loans as a way for the lender to generate additional revenue. Providers are encouraged to identify and track progress against specific consumer-focused Key Performance Indicators (KPIs) along with traditional financial metrics.*

While some of these characteristics are straightforward, others imply clear trade-offs. For example, assessing ability to repay requires that the lender gather and verify information about the borrower, including but not limited to his or her identity, income, credit history and other obligations, which may slow down the loan approval process, making the loan less convenient for some borrowers. Fortunately, consumers report a variety of needs for small-dollar credit, and therefore a one-size-fits-all solution is not the goal (see Box 3).

Much of the debate about small-dollar credit has heretofore focused on price, as expressed in Annual Percentage Rates (APR), as a primary determinant of quality. While affordable prices are certainly one aspect of high-quality small-dollar loans, what is "affordable" to any given borrower depends on many factors, including the loan's size, repayment period, interest rate and fees, as well as the individual borrower's unique financial

BOX 3 *CFSI's research identifies four primary need cases in the small-dollar credit market: Unexpected Expense borrowers, Misaligned Cash Flow borrowers, Planned Purchase borrowers and Exceeding Income borrowers. The distinct profiles of the first three need cases suggests that different types of products (e.g. lines of credit versus installment loans, or loans of various sizes or with different distribution mechanisms) might meet those borrowers' needs. However, for Exceeding Income borrowers, access to credit might only worsen their financial situations.*

Because this Guide emphasizes making loans with a high confidence in the borrower's ability to repay, lenders have a responsibility to use the best tools available to determine whether an applicant falls into this category, and if they do, not to extend credit to them. These consumers should be the target of interventions by policy-makers, governments and nonprofits designed to protect them from harmful or deceptive lending practices and to improve their financial situations. There may also be opportunities for financial institutions to devise other non-credit products, such as small-dollar savings, that can meet the needs of these consumers.

"Know Your Borrower: The Four Need Cases of Small-Dollar Credit Consumers." Center for Financial Services Innovation, December 2013.

situation. *CFSI defines an affordable small-dollar loan as one for which the loan amount, repayment period, interest rate and fees are such that the borrower can successfully repay the loan without re-borrowing and while still meeting basic needs and other financial obligations* (see Box 4). In other words, whether a loan is affordable or not depends on underwriting, structure and pricing – not on price alone.

Whether a loan is affordable or not depends on underwriting, structure and pricing – not on price alone.

Underwriting. As discussed earlier, loans should be made with a high expectation that the borrower will repay them, on-time and without renewing the loan. This means that lenders must invest in their underwriting capabilities, rather than accepting a high default rate as a necessary cost of doing business or relying on high fees from borrowers who are in a cycle of debt. As lenders' underwriting capabilities improve, they ought to be able to distinguish higher-risk borrowers from lower-risk borrowers, and price their loans accordingly. Credit should become much more affordable for the many consumers who use it responsibly.

Structure. Structure is just as important as price in determining whether a small-dollar loan is affordable. For example, for borrowers who struggle financially, a two-week loan with a balloon payment structure is often very difficult to repay, even at very low prices. In most cases, loans should be structured in fully-amortizing installment payments; the amount of the loan and the repayment period are variables that should be adjusted to ensure that the borrower can afford to make the regular payments while still having enough left over to meet basic needs and other financial obligations.[2] Borrowers should have the option to repay the loan early without penalty, preserving needed flexibility for those who wish to get out of debt more quickly. (However, lenders should not encourage borrowers to pay off early simply by refinancing or taking out another loan, a practice called loan flipping.)

Pricing. Lenders must be able make a profit in order to offer consumers lasting, high-quality solutions at scale. However, small-dollar credit products should not benefit the lender at the borrower's expense; in other words, the business model should rely on successful repayment, not high probabilities of default. Pricing should be designed to incentivize and reward positive behavior, lowering costs for consumers as they demonstrate creditworthiness over time. Lenders should not rely on punitive rates and fees as profit centers, and borrowers should not be penalized for good behavior. Over time, lenders should leverage improved underwriting capabilities and operational efficiencies to lower prices and extend credit to more qualified borrowers.

CFSI's vision for the future of the small-dollar credit marketplace is that consumers will have a variety of high-quality options that meet their small-dollar credit needs and support them on a path to long-term financial health. For this vision to become reality, lenders will need to develop and pilot new models for delivering small-dollar credit that meet the standards outlined in this Guide. As they do so, CFSI believes that competition for the small-dollar customer will increase, leading to lower prices, more diverse product structures, more innovative features and better customer service – all of which mean more and better choices for consumers.

BOX 4 *Throughout the Guide, we say that an affordable loan is one that the borrower can repay without re-borrowing and while still meeting basic needs and other financial obligations. By "basic needs and other financial obligations," we are referring to necessities such as food, shelter and medical care, as well as debt service for other loans, including mortgage, student, credit card and other small-dollar loans. By "without re-borrowing," we are making a distinction between borrowing again at some future date because a new credit need arises (which does not necessarily indicate that the original loan was unaffordable) and re-borrowing immediately or shortly after repaying the original loan (which strongly suggests the borrower could not afford to pay back the loan while still meeting basic needs and other financial obligations in the next period).*

2 We stop short of saying that loans should be made in installments in all cases. A loan with a balloon payment might still be considered high-quality if the loan is small enough that repayment in one lump sum remains affordable to the borrower.

3. HOW TO USE THE GUIDE

Purpose and Audience

The Compass Guide to Small-Dollar Credit is a tool for improving the quality of small-dollar loans through guidelines for their design and delivery. Lenders can use it to review or improve existing offerings, or to design new ones. Other actors in the small-dollar credit marketplace, such as investors, technology providers, consumer advocates or government agencies, can use the Guide to inform their own assessment tools for small-dollar loans.

Structure of the Guide

The following sections outline each of the seven guidelines with a corresponding list of recommended practices. The practices are divided into three categories:

Core Practices: These are the standards for a high-quality small-dollar credit product. A loan should not be considered high-quality unless it meets these practices.

Stretch Practices: These are additional best practice ideas for providers looking to stretch beyond the basic requirements.

Next Generation Practices: These practices are for providers that have met the standards for quality, challenged themselves to stretch beyond the basics, and are considering the next step in high-quality product design. These practices are called "next generation" to emphasize the need for new models for delivering small-dollar credit that may not yet exist today. We need additional customer-focused innovation, research and testing for these new models to emerge.

Please note that the examples are simply for illustrative purposes and should not be used as a checklist. Many of the practices in this Guide entail distinct business strategy decisions that are at the provider's discretion, and there is no one-size-fits-all approach to a high-quality small-dollar credit product.

How Not to Use the Guide

This Guide is intended as a tool to help lenders design high-quality small-dollar credit products. **It cannot function as a "seal of approval" for any product or company, as CFSI does not monitor how individual lenders use this Guide or evaluate the extent to which they adhere to its principles.**

This Guide is not intended to provide advice about regulatory compliance. Users should seek legal counsel to ensure compliance with all applicable laws and regulations.

4. COMPASS GUIDELINES AND PRACTICES FOR SMALL-DOLLAR CREDIT

Alongside each guideline, the Compass Principle(s) most fully embodied by the guideline are identified. For each of the Core, Stretch and Next Generation practices, examples are provided to illustrate how a company might apply the practice.

This Guide defines a high-quality small-dollar loan as one that:

1 Is made with a high confidence in the borrower's ability to repay.

✓ EMBRACE INCLUSION
✓ BUILD TRUST
✓ PROMOTE SUCCESS

CORE PRACTICES

Use the best available underwriting techniques to ensure a borrower's ability to repay without re-borrowing and while still meeting basic needs and financial obligations.

Examples:

- Consider the borrower's overall relationship and history with the financial institution.
- Collect and analyze information about the borrower's other outstanding debt.
- Collect and analyze information about the borrower's total monthly income and expenses.
- Safely incorporate data not captured by traditional credit reporting.
- Analyze the borrower's deposit account inflows and outflows, either through the lender's own institution or through a third-party API.
- Develop a secondary scorecard that enables the institution to consider borrowers without a traditional credit profile.

Do not make loans that rely solely on collateral for repayment.

Example:

- If collateral is accepted (e.g. preauthorized ACH or payroll deduction), use additional underwriting techniques to ensure the borrower's ability to repay.

Offer an appropriate loan product and amount based on each individual borrower's financial situation and the lender's risk.

Examples:

- Offer "starter" loans in smaller amounts to borrowers for whom there is less available information (e.g. no traditional credit scores) and therefore for whom the risk to the lender is greater.
- Balance the amount borrowed and loan term to ensure that individual payments are affordable while minimizing the total cost of the loan to the borrower.
- Consider offering loan products (e.g. secured credit cards) that minimize risk to the lender while expanding access to borrowers seeking to build or re-build their credit.

Monitor portfolio performance to ensure that most borrowers are using the product as designed, without defaulting or re-borrowing.

Example:

- Set target rates for indicators of borrower success, such as the frequency of defaults, late payments or repeated use, and proactively adjust underwriting standards when these indicators suggest that borrowers are not succeeding with the product as designed. Tolerate only low rates for such indicators, even if high rates would not impair profitability.

2 Is structured to support repayment.

✓ BUILD TRUST
✓ PROMOTE SUCCESS

CORE PRACTICES

Design repayment timing and other product features to support and encourage successful on-time repayment.
Examples:
- For closed-end loans, include repayment of principal with each payment (fully amortizing) and no prepayment penalty.
- For lines of credit, set default minimum payments to include both principal and interest, and encourage borrowers to pay more than their minimum payment each month.
- Balance the amount borrowed and the length of repayment to ensure that individual payments are affordable while minimizing the total cost of the loan to the borrower.
- Allow reasonable grace periods, enabling borrowers to avoid late payment fees and penalty interest rates.
- Enable borrowers to opt out of or reschedule automatic repayments within a reasonable grace period.

Create meaningful safeguards to prevent harmful misuse or overuse of the product.
Examples:
- For closed-end loans:
  - If a borrower takes out more than one loan at a time, ensure that total payments on all loans do not exceed the borrower's ability to repay.
  - Do not encourage borrowers to pay off their loans early simply by refinancing or taking out another loan.
  - Consider limits on the number of loans in a given period as means to prevent harmful misuse or overuse of the product.
- For lines of credit:
  - Periodically monitor and reevaluate the borrower's creditworthiness, reducing or increasing credit lines as needed to respond to changes in the borrower's financial situation.
  - Consider requiring that borrowers periodically reduce their balance to zero to prevent harmful misuse or overuse of the product.
  - Do not allow borrowers to exceed their credit limit.

Provide support to borrowers when they have trouble repaying.
Examples:
- Accept partial payments when a borrower has trouble repaying.
- Design flexible repayment plans for responsible borrowers facing difficult financial circumstances.
- Allow borrowers to put payments temporarily on hold when facing difficult financial circumstances.

STRETCH PRACTICES

Allow flexibility in setting repayment schedules that match income schedules.

Examples:

- Set loan payment due dates to correspond with the borrower's pay schedule or receipt of other income.
- Allow borrowers to choose their own loan payment due dates and/or to reschedule them (within a reasonable grace period) at any time.

Allow borrowers to customize the amount borrowed, loan term and payment amount up front in order to design a loan that fits their budgets, within ranges that underwriting suggests the borrowers can afford.

Example:

- Provide an interactive online tool that shows prospective borrowers how much they will have to pay (both in individual payments and over the life of the loan) for various possible loan amounts and durations. Set defaults that encourage borrowers to pay off the loan as quickly as they can afford to do, to help them get out of debt faster.

NEXT GENERATION PRACTICES

Provide customizable alerts and tools that help borrowers manage their debt responsibilities effectively.

Examples:

- Allow borrowers to choose to receive alerts before automatic payments are withdrawn, providing the option to approve the payment or reschedule it (with a reasonable grace period).
- Allow borrowers to choose to receive alerts when their loan balance reaches certain thresholds (e.g. when they have paid off X% of their loan, or they have $X left to pay before their loan is fully paid off), or when they have paid a certain amount in total fees.
- Offer online or mobile budgeting and personal financial management tools and/or access to third-party providers for those purposes.

3 Is priced to align profitability for the provider with success for the borrower.

✓ BUILD TRUST
✓ PROMOTE SUCCESS

CORE PRACTICES

Price loans to incentivize and reward positive behavior, lowering costs and/or increasing benefits for borrowers as they demonstrate creditworthiness over time.

Examples:

- Incentivize automatic loan repayments from transactional accounts, while allowing the borrower the option to opt out at any time.
- Reduce rates over time for borrowers who demonstrate consistent repayment.
- Refund fees on a pro-rata basis when loans are paid back early.

Do not rely on penalty fees and interest rates or fees earned from refinancing as profit drivers.

Examples:

- Minimize late payment fees and penalty interest rates.
- Allow reasonable grace periods, enabling consumers to avoid late payment fees and penalty interest rates.
- Minimize upfront fees and use accounting methods that accrue interest over the life of the loan, to reduce loan officers' incentives to encourage borrowers to refinance.
- Actively help borrowers avoid penalty fees and interest rates through smart communication (e.g. alerts, targeted advice from customer service representatives, etc).
- Place a cap on the total amount of interest and late fees a borrower can pay on the loan to prevent rapidly accumulating costs in the event the borrower has trouble making payments.

Ensure borrowers receive the most appropriate and lowest-priced loan for which they qualify.

Examples:

- Provide opportunities to graduate to lower-cost products.
- Provide opportunities to refinance other high-cost debt at more favorable rates.
- Proactively monitor borrowers' use of the product to identify opportunities to graduate them to lower-cost products.

NEXT GENERATION PRACTICES

Provide additional benefits to borrowers who demonstrate positive behavior.

Example:

- Offer appropriate additional financial service products to regular borrowers in good standing, such as reloadable prepaid cards with savings and budgeting tools.

4 Creates opportunities for upward mobility and greater financial health.

✓ BUILD TRUST
✓ CREATE OPPORTUNITY

CORE PRACTICES

Help the borrower leverage successful repayment into better credit opportunities in the future.

Examples:

- Report repayment to major credit bureaus to help borrowers establish or build credit scores.
- Provide a clear path of graduation based on successful repayment, such as from a secured credit card to an unsecured credit card, or from one product to another with better terms and lower prices.

If a borrower does not qualify for a loan today, provide actionable and specific advice that can help him or her work towards qualifying in the future.

Examples:

- Provide referrals to credit counseling services that can help the borrower learn how to improve his or her score in the future.
- Offer information about other services, such as government benefits, job training or social services, which can help the borrower improve his or her financial situation.

Leverage teachable moments to provide guidance about how to use the product successfully.

Examples:

- Use key moments such as loan application, approval and servicing as opportunities to provide proactive advice to the borrower about how to avoid fees and qualify for better credit opportunities in the future.
- Allow borrowers to avoid a late payment fee or receive an interest rate discount by completing online financial education modules.

STRETCH PRACTICES

Provide borrowers with information about their credit reports and credit score at key moments over the life of the loan so they can observe in real-time how repayment behavior affects their credit profiles.

Examples:

- Provide access to a credit score for all applicants, regardless of decision.
- Provide borrowers with free access to credit report monitoring services.
- Incorporate clear, easy-to-understand information about the borrower's credit score into periodic statements and/or an online dashboard.

NEXT GENERATION PRACTICES

Combine small-dollar loans with savings opportunities and incentives, helping borrowers improve their ability to manage future emergencies or cash shortfalls.

Examples:

- Continue to direct automatic payments into a savings account after the loan has been fully paid off.
- Require that the borrower open a savings account as a condition of the loan and make a nominal contribution to the account as an incentive for the borrower to begin using it.
- Credit the application fee into the borrower's savings account if he or she pays the loan on time.
- Direct a portion of the loan amount into savings, and do not charge interest on that portion of the loan.
- Provide a bonus that gets deposited into the borrower's savings account when the loan is fully repaid.
- Allow the borrower to refinance higher-cost debt, and direct a portion of the savings from the lower payments into a savings account.

5 Has transparent marketing, communications and disclosures.

✓ BUILD TRUST
✓ PROMOTE SUCCESS

CORE PRACTICES

Disclose the full cost of the loan to the borrower in simple, clear and easy-to-understand language, with no hidden fees, industry jargon, misleading information or fine print.

Examples:

- Prominently disclose, with equal weighting, the periodic and total cost of the loan, both in dollar terms and as an Annual Percentage Rate (APR) inclusive of all fees.
- Ensure that all disclosures comply with the requirements of the Truth in Lending Act's Regulation Z.
- Design the format and visual design of the price disclosure to be useful and easily understandable.
- Offer add-on products separately, once the loan has been funded, and on an opt-in basis only, with no hidden fees, industry jargon, misleading information or fine print.
- Provide prospective borrowers with information about the likely terms of their offer prior to submitting an application, especially if credit scores will be pulled as part of the underwriting.

Provide borrowers with information about the loan product in a manner and language they can understand so that they can make better and more informed decisions.

Examples:

- For closed-end loans, provide borrowers with a full payment schedule that shows the dates and amounts of all payments, including the amounts applied to interest and principal until the loan balance reaches zero.
- Use affirmative statements to enable borrowers to affirm that they understand the full cost of the loan and the consequences of late or non-payment, e.g. "I recognize that I will pay $X, and will pay $X extra if I do not do Y..."
- Provide periodic loan statements that clearly demonstrate success towards paying off the loan (and, if applicable, progress towards savings goals).
- Provide marketing collateral, loan applications, disclosures, statements and account information in multiple languages.
- Communicate decline decisions in a manner that is easy to understand and in compliance with the Fair Credit Reporting Act.
- Clearly communicate to prospective borrowers that their repayment behavior will be reported to major credit bureaus.
- Clearly market information about the risks to borrowers before they apply for the loan (e.g. that their credit reports will be pulled and employment verified, that they will be liable for making payments, the consequences of non-payment, etc.)

STRETCH PRACTICES

Clearly illustrate to borrowers in real time how much the loan will cost and how long it will take to pay off given actual or anticipated payment behavior.

Example:

- Include a section in periodic statements and/or online dashboards that shows borrowers how much more quickly they will be able to pay off the loan if they increase payments by a given amount over their actual repayment behavior.

6 Is accessible and convenient.

✓ EMBRACE INCLUSION
✓ BUILD TRUST

CORE PRACTICES

Make loan decisions in a timely fashion, balancing the borrower's desire for quick access to funds with the lender's commitment to responsible underwriting.

Examples:

- Leverage existing third-party platforms to enable borrowers to verify more of their information on the spot.
- Set clear expectations up front for prospective borrowers about how quickly they will receive a loan decision.
- Develop underwriting techniques that allow for prequalification for loans up to a certain limit, based on a preexisting relationship with the borrower.

Ensure that loan application, decision, disbursement and servicing processes are convenient and culturally relevant.

Examples:

- Allow applications to be accessed and submitted through multiple channels, such as in-person, by mail, by phone, online, via kiosk or via mobile device.
- Allow payments to be made through multiple channels, such as ACH, in-person, by phone, online, via kiosk or via mobile device.
- Provide the option of receiving funds distributions through multiple channels such as by paper check, direct deposit, wire transfer or payment directly to a third-party provider.
- Provide a loan dashboard online, via mobile platforms and/or through Interactive Voice Response (IVR) systems so that borrowers can easily access account information and make payments.
- Provide marketing collateral, loan applications, disclosures, statements and account information in multiple languages.
- Allow customers to use multiple forms of identification when applying for a loan (e.g. foreign identification).
- Allow customers to request mailed paper statements at a reasonable cost.

STRETCH PRACTICES

Use nontraditional delivery channels to increase access for the borrower, facilitate timely loan approval and minimize risk to the lender.

Examples:

- Allow borrowers to submit applications and make payments at retail locations where they frequently shop, such as supermarkets.
- Tie loan approval and disbursement to the payment of a particular vendor, such as utility companies or auto mechanics.
- Work with employers to facilitate access to loans as an employee benefit.

7 Provides support and rights for borrowers.

✓ BUILD TRUST

CORE PRACTICES

Ensure that borrowers can obtain customer support easily and are treated respectfully and helpfully.

Examples:

- Provide customer support through multiple channels, such as in-person, by phone, online, via kiosk or via mobile phone.
- Provide customer support in multiple languages.
- Develop Interactive Voice Response (IVR) systems that are available in multiple languages, easy to navigate, and make clear how to access a live agent.
- Provide contact information for the relevant state or federal regulatory body in the event the borrower wishes to register a complaint or seek additional guidance.
- Assign borrowers to individual relationship managers who are primarily responsible for providing them with customer support.

Design dispute resolution and collection practices that are reasonable and fair to the consumer.

Examples:

- Ensure that collection practices comply with the Fair Debt Collection Practices Act and all applicable regulations.
- Before initiating collections, reach out to the borrower and consider designing a repayment plan, waiving late fees or back interest, or other measures to assist with repayment.
- Provide an independent ombudsman process to resolve disputes.
- Do not use collections tactics that employ harassment or intimidation under any circumstances.
- Provide a process for borrowers to easily dispute errors in their credit reports.
- Develop and disseminate a Borrower's Bill of Rights.

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United States House of Representatives
Committee on Financial Services

Short-Term, Small Dollar Lending: The CFPB's Assault on Access to Credit and Trampling of State and Tribal Sovereignty

February 10, 2016

Statement of Sherry Treppa
Chairperson, Habematolel Pomo of Upper Lake

Chairman Neugebauer, Ranking Member Clay, and Honorable Members of the committee, thank you for the opportunity to testify at this important hearing on short term lending and tribal sovereignty. My name is Sherry Treppa and I am the chairperson of the Habematolel Pomo of Upper Lake, a federally-recognized Indian Tribe located in rural Upper Lake, California. I have represented the Tribe's interests as an elected leader for the past eleven years, and held the position of chairperson for the last seven. I also serve as the Vice-Chairperson of the Native American Financial Services Association (NAFSA), an intertribal organization formed in 2012 to advocate for tribal sovereignty and responsible business practices in e-commerce.

As a vital part of our economic development strategy, our Tribe owns and operates several online small-dollar lending businesses that operate on our Trust lands. I am here today to provide you with information on how our Tribe regulates and supervises these businesses and the considerable tools we have available to protect consumers. I would also like to share my thoughts and feedback on the efforts the Consumer Financial Protection Bureau (CFPB) has taken to restrict the short-term, small dollar credit marketplace and preempt State and Tribal rights, and what that will mean to American consumers and Indian tribes.

To first understand these critical issues, it is important to understand our tribe's people, our long and arduous history, and the sovereign authority that we have worked so hard to safeguard.

Our ancestors have called the Clear Lake region of California home from as early as 6,000 BC. Our people flourished until significant migration and settlement brought conflict and disease that, in one generation, decimated our numbers by 95%. The flawed federal policies that ensued subjected Pomo Indian tribes to enslavement, internment, horrific abuse, and slaughter. Notably, the U.S. Cavalry in 1850 nearly eradicated my Tribe's ancestors, predominantly elderly, women and children, in an aggressive military operation known as the "Bloody Island Massacre." The only survivor of that attack was a 6-year old girl who survived by hiding underwater and breathing through a tule reed.

Our Tribe and our lands were first federally recognized in 1907 eventually amassing over 560 acres through piecemeal acquisitions. In 1956 the federal government passed the California Rancheria Act, which terminated the Tribe's federal recognition.[1] We lost not only our recognition, but also our land, which is fundamental to our way of being. Despite efforts to destroy our tribe and our identity, we persevered. In 1975, the Tribe began the arduous task of reestablishing its identity and restoring its dignity by filing a court action alleging that the Tribe's termination was illegal. Although the suit took nearly 10 years to litigate, we prevailed. After restoration in 1983, the Bureau of Indian Affairs (BIA) refused to recognize our Tribe's 1941 Constitution which required the Tribe to reorganize under federal law, and impeding our efforts to restore our land-base. In 1998, we began reorganization, working with the BIA to reestablish our government, finally succeeding in 2004 in adopting our current Constitution. After this long and onerous process, the Department of the Interior accepted into trust a small, 11.24 acres tract of land for the benefit of our Tribe. These achievements, gained through years of effort and raw human will, are our legacy.

As elected leaders of our Tribe, I and other members of our Tribal Council honor that legacy through our unrelenting efforts to improve the general welfare of our citizens through self-development, education and other opportunities for advancement. E-commerce and lending provides those opportunities.

Before I go into the specifics of our Tribe's lending practices and the strong regulatory framework that undergirds them, I believe it is important that I provide an overview of tribal sovereignty and the rights that Tribes have to legislate and regulate business activities occurring within their jurisdictions.

Tribal Sovereignty and Self-Regulation

The inherent sovereign power of Indian Tribes predates the United States Constitution. Indian Nations appears twice in the Constitution, each time in Article I, treated as separate and existing sovereign nations. Nearly every piece of modern legislation dealing with Indian tribes explicitly affirms the protective trust relationship between tribes and the federal government. The federal trust responsibility to Indian tribes underlies both the "government-to-government relationship" with Indian tribes and the imperative that federal agencies not actively impede the economic development and self-determination of Indian tribes, and that they engage in meaningful consultation when any federal undertaking might impact tribes in a significant way. The sole power to diminish tribal sovereignty rests with Congress. Whatever Congress has not expressly diminished by legislation remains for the exercise of tribal governments like the Habematolel Pomo of Upper Lake.

Tribal Regulation of Consumer Lending Activity

From our sovereign power springs the right to legislate and regulate the operations of business activities within our jurisdiction. Consistent with our commitment to improve our members' economic prospects, in 2010, the Tribe began to explore e-commerce and online small dollar lending as a viable economic opportunity. After a thorough review of the industry and related opportunities, our tribal

[1] See, the California Rancheria Termination Act of 1958, Public Law 85-671 (72 Stat. 619) found at http://www.gpo.gov/fdsys/pkg/STATUTE-72/pdf/STATUTE-72-Pg619.pdf.

council, consistent with our inherent power, constructed a regulatory framework using the model that has proven successful in the tribal gaming industry.

We enacted a lending ordinance that sets forth the parameters of legal operation of consumer lending from our Trust land. This lending ordinance prohibits tribal licensees from engaging in unfair, deceptive, or fraudulent practices, or engaging in any consumer financial services other than those expressly permitted under that ordinance.[2] Tribal lending entities that issue loans within our trust land must comply with that legislation.

We created a regulatory commission and charged it with oversight of the tribal lending businesses, and gave it the power to enforce our laws. This regulatory commission is a separate division of the Tribe's government, which means that it operates independently of our tribal government. The commission has the autonomy to exercise its enforcement authority should a lending business violate the consumer protection laws that we established.

Sovereignty at Work: Collaborating to Protect Consumers

My Tribe has exercised its sovereign power in other ways beyond our robust legal and regulatory framework. We have actively sought opportunities to enter into cooperative agreements or compacts with states as a means to coordinate the exercise of authority in this area and promote a collaborative government-to-government regulatory environment. By way of example, our Tribe successfully entered into a Memorandum of Understanding with the State of New Mexico in December, 2014, which explicitly memorialized our Tribe's sovereign authority to engage in online short-term lending and acknowledged that the legislation enacted by our Tribe effectively regulates transactions between consumers and licensed lenders that occur on Trust land, adheres to best practices, and does not violate federal or tribal law.

The California Department of Business Oversight's Information-Sharing Pilot program offers another example of the initiatives our Tribe has undertaken to foster government-to-government cooperation with states. Our Tribe, along with other tribal members of NAFSA, collaborated with the Department of Business Oversight to explore opportunities to develop a framework that facilitates information exchanges between regulatory authorities. The experience was positive and we continue to pursue open dialogues and additional Memoranda of Understanding with other states, ever eager to work cooperatively and communicate openly with states as co-regulators to achieve shared goals of consumer fairness and protection. Indeed, these efforts are consistent with the regular practice of many Tribes throughout the country to collaborate with state authorities on tribal-state relations in areas as wide-ranging as law enforcement, environmental protection, hunting and fishing, public lands management, and education.

Another enforcement power available to Tribes in regulating financial services businesses, as the CFPB itself admits, is the ability to bring legal actions under the Dodd-Frank Act, just as States can. Indeed, the Navajo Nation and the CFPB brought an enforcement action together against a tax refund business in mid-2015 under this authority. While we have not seen the need to rely upon anything more

[2] See, Ordinance at §7.3.

than our own laws and regulatory commission to handle consumer complaints and other regulatory issues, my Tribe (and others operating small dollar lending businesses) are aware of this significant power, and are certainly prepared to exercise it should the need to do so arise. This Committee should make no mistake – ample power already exists for Tribes to protect consumers and regulate businesses within its jurisdiction.

What Tribal E-Commerce Offers Consumers

To fully illustrate what my Tribe has developed to meet the needs of consumers and our tribal members, I would like to go into more detail regarding my Tribe's lending operations and their obligations under Tribal law.

The Tribe's lending businesses must be licensed by our Tribal regulatory commission before they may engage in lending. They may not charge consumers an application fee or penalize them for early payment of their loans. Tribal lending entities must maintain a compliance management system to ensure compliance with Tribal law, promulgated regulations and applicable federal law.[3] This system must include a full suite of written policies that cover all aspects of lending. Each lender must also have internal controls and processes that allow it to monitor its operations to ensure that its procedures follow those policies.[4] As an additional control, our regulatory commission audits these businesses regularly. If deficiencies are identified during an audit, or if a lender fails in any way to satisfy their compliance obligations, then the commission is empowered to take corrective action. This includes imposing fines and penalties, as well as suspending and revoking the lender's license, which would terminate the lender's ability to extend credit. This regulatory framework is what our tribal lending entities operate under, and it ensures that their practices are responsible and based on principles of consumer protection.

The loans that our Tribe's businesses offer are not payday loans; they are unsecured loans that are repaid in installments, which means our lenders have no real remedies if a customer defaults. Consequently, a robust underwriting process is an operational imperative. Our Tribe's lending businesses use computer algorithmic waterfalls and data analytic tools to assess a consumer's application. The amount of a customer's credit request is compared against their income and existing credit obligations because it is a strong factor in determining their *ability to repay*. An applicant's repayment history is checked because it is the strongest factor in assessing their *willingness* to repay. If a customer's ability to repay or willingness to repay do not meet the lending company's underwriting requirements, or if the identity verification portion fails, then the application will be denied. Data from the Tribe's lending businesses illustrate the rigor and effectiveness of our underwriting. From all of the applications received in 2015, 4 only 3.1% were accepted. Of those accepted for review, less than 2% were approved and funded. Put another way: **98.3% of new customers are rejected in underwriting**. This commitment to responsible lending helps to prevent customers from taking loans they are unable to repay.

[3] See, Ordinance at 7.4. Federal laws that our Tribal businesses adhere to include, as applicable, the Truth in Lending Act, Equal Credit Opportunity Act, Electronic Fund Transfer Act, Fair Credit Reporting Act, Gramm-Leach-Bliley Act, Fair Debt Collection Practices Act, Telephone Consumer Protection Act, the Telephone Sales Rule, and Section 5 of the Federal Trade Commission Act which prohibits unfair, deceptive or abusive acts or practices.

[4] See, the Habematolel Pomo of Upper Lake Tribal Consumer Financial Services Regulatory Ordinance, §7.1

The typical customer that our tribal lenders approve for credit is approximately 45 years old with a median income of $45,000. The typical customer rarely reports public assistance or other benefits as an income source. The median loan amount is $700, and, although the installment contract is structured on a ten-month payment schedule, customers are encouraged to pay extra toward the principal or pay off the loan early without penalty. We have significant data that shows customers frequently repay their loans in less than four months. Data also shows that our customers have moderate borrowing patterns: when measured over two years, our customers have an average of 1.6 loans.

The Benefits of Tribal Lending for Us and Our Consumers

The decision to enter into the small-dollar credit marketplace has been transformative for our Tribe in that **all** net revenue derived from consumer lending is used to fund essential Tribal governmental services such as: cultural programs to promote the Tribe's language, heritage, and community; an Honored Elders Assistance Program, which provides monthly stipends for members 65 and older; a school clothing allowance for K-12 children, and scholarship programs to help with the costs of higher education; and a Community Care Program for members to receive violence and suicide prevention counseling, and other vital social services. Without tribal lending, these programs would be impossible.

For American consumers, our credit products offer options for meeting financial obligations without fear of defaulting on an obligation, failing to pay a bill, or overdrawing their checking account. The CFPB may consider small dollar lending to be a scourge of the credit industry; our customers tell a different story. In 2015, our total complaint rate was only1.6%. This number likely drops to 1% when considering that some of those complaints are likely due to loan applications we denied. That number is significant and it illustrates the quality and the legitimacy of our operations.

My tribe agrees that consumer protection should be a primary concern of this industry, because responding to consumer demand in a regulated, compliant, and helpful manner is the essence of consumer protection – and that is what we do. Much of the reason we have been successful is the strong commitment we have made to ensure that tribal lending businesses adhere to fair and responsible lending practices that protect consumers. That is why we question the need for new CFPB rules. Efforts to impose additional regulations would significantly obstruct access to credit and reduce or eliminate consumer choices for meeting unexpected financial obligations.

Before the CFPB seeks to impose new regulations, I would first like them first to acknowledge the robust regulatory framework that our Tribe, and other tribes, have created, and that our lending businesses are operating within. In contrast to our experience working with other federal agencies as well as state and local governments, the CFPB has refused to engage in a meaningful dialogue about our shared interests and so far has shown little interest to work together, where necessary, as co-regulators.

The CFPB's refusal to work with tribes in a government-to-government manner is not consistent with the federal government's trust responsibility to tribal governments nor does it respect the inherent sovereignty of Indian tribes. I remain concerned that the CFPB is developing its proposed action in a vacuum without consulting with tribes to learn about the innumerable tools that we have developed to ensure that we conduct business in a manner that is fair, responsible, compliant and benefits our tribal members and the American consumer.

We respectfully urge Congress to take an approach that respects the historic government-to-government relationships of federal entities and sovereign tribes, and one that takes account of both consumer need and the robust self-regulation that sovereign Tribes such as the Habematolel Pomo of Upper Lake have established.

U.S. House Subcommittee on Financial Institutions and Consumer Credit
Thursday, February 11, 2016
1:00 PM ET

Testimony of Indiana Attorney General Greg Zoeller
Re: Preemption of State lending laws

Thank you Mr. Chairman and members of the committee. I am Greg Zoeller, the Attorney General of Indiana. I appreciate the invitation and it is an honor to be in front of you today to talk about this important matter of preserving states' rights, and to raise awareness of an ongoing barrage of federal government overreach.

Over the years, Indiana, and other states, have crafted meaningful regulation and consumer protections for their citizens, including small loan lending. Indiana established consumer friendly protections for all borrowers, while providing solutions for those who need additional help. In the past year, the Consumer Financial Protection Bureau has proposed a rule creating a regulatory framework that defies the very goals my state has strived to achieve for consumers to maintain access to credit while not inadvertently driving them to unregulated, unsafe loan products. Like other states, we have worked hard to strike this balance between access to credit and protections against predatory lenders. The proposed federal regulations would throw this balance off and reduce access to short-term loans for the people in my state and others who need this type of financial assistance the most and who need it from reputable lenders.

This policy area has historically been left to states and as Attorney General I defend my state's authority. Indiana has extensive experience in crafting these regulations to protect consumers. For example, currently in Indiana, lenders are prohibited from making a small loan to a borrower if the total of the principal amount and the finance charges of the small loan to be issued, combined with any other small loan balances that the borrower has outstanding with any lender, exceeds 20% of the borrowers' monthly gross income. Indiana also requires certain disclosures about the nature of this financing option. These and other regulations promulgated under Indiana law provide Hoosier-specific protections which would be pre-empted under the proposed Bureau rules.

Moreover, the regulatory framework proposed by the Bureau is extraordinarily broad. It covers not only payday loans, but short- and medium-term loans which can be made by community banks and credit unions as a service to customers. The new rule would create an environment that discourages this type of lending by these already heavily regulated institutions. Without this legitimate source of short-term lending, consumers who need these types of funds will be forced to turn elsewhere… likely to unscrupulous lenders where they are at higher risk for abuse.

Many of my attorney general colleagues across the country have raised these concerns with the CFPB to little avail. Since the creation of the Bureau in 2010, attorneys general have continued to express concern that the Bureau's goals to help consumers have conflicted directly with the authority of states to balance the interests of financial institutions and organizations with the protections of its citizens from fraud.

As Attorney General, I take my role as protector of consumers seriously. I have been a strong advocate on behalf of consumers, especially those most vulnerable in our society. When seniors and veterans were increasingly becoming victims of scam artists, I successfully worked with the legislature to increase penalties against those who targeted these victims. We've also worked to educate and defend consumers struggling with debt and similar issues, for example refusing to tolerate unfair debt collection tactics, and funding foreclosure prevention services and debt counseling to Hoosiers. My attorney general colleagues and I are on the ground working with consumers, assisting victims and tackling these important issues. The progress we've made to advance strong consumer protections that work best for our states should not be undermined. One-size-fits-all, blanket regulations from a federal bureaucracy will only wipe out years of thoughtful, state-specific efforts to assist and protect our citizens.

So at issue is not simply whether the regulatory framework that the CFPB has proposed is best for the consumers in my state but whether the rules that provide for both access to credit and protection from predatory lending are best done in Washington for the nation or by each individual state.

Thank you for your time. I am available for any questions.

CYNTHIA H. COFFMAN
Attorney General
DAVID C. BLAKE
Chief Deputy Attorney General
MELANIE J. SNYDER
Chief of Staff
FREDERICK R. YARGER
Solicitor General

STATE OF COLORADO
DEPARTMENT OF LAW

RALPH L. CARR
COLORADO JUDICIAL CENTER
1300 Broadway, 10th Floor
Denver, Colorado 80203
Phone (720) 508-6000

Office of the Attorney General

October 15, 2015

The Honorable Richard Cordray
Director
1700 G Street, N.W.
Washington, D.C. 20552

Dear Director Cordray –

I write regarding the Consumer Financial Protection Bureau's (CFPB) consideration of rules regarding short-term loans. While I share certain concerns voiced by other Attorneys General, I am not writing to critique the CFPB. Instead, I am asking that you pay close attention to how the states, especially Colorado, have managed the small-dollar lending industry and consider incorporating those lessons into regulations you may promulgate.

U.S. Chief Justice Louis Brandeis is famously quoted as describing a state's right to manage its own affairs without federal interference as a laboratory, a place he said to "try novel social and economic experiments without risk to the rest of the country." *New State Ice Co. v. Liebmann*, 285 U.S. 262, 311 (1932). In 2010 Colorado addressed concerns about abuses in the payday lending industry and had what all sides would agree was an energetic debate on a new regulatory approach. The result of that debate has proven to be a success. Indeed, we consider it a success for the consumer, for the state as a regulator and also for the industry. Industry abuses (as measured by enforcement actions) are down; consumer complaints are down; and the industry itself is profitable and able to offer its products responsibly to consumers who choose to engage in that market. In light of the successes we've enjoyed in Colorado, I strongly encourage you to not only study how we regulate the industry and to consider adoption of our approach, but I offer my office's assistance as you continue to consider application of regulations nationwide.

Many of the CFPB's proposals attempt to keep consumers from falling into a "debt trap" wherein, for example, short-term *single payment* loans can place consumers in a cycle of debt and may cause financial harm rather than assist consumers. CFPB appears to be moving towards proposing rules to address the consumer's ability to repay; possible payment plans ("no-cost off ramp"); establishing cooling off periods; and limiting the lender's access to the consumer's accounts or vehicles.

Colorado's extensive experience with these types of measures tells us such proposals will not work in the real world if the intent is to preserve access to credit products for the financially strapped. Analysis has clearly shown that longer term loans, even if they involve small dollar amounts, are a benefit to consumers from the standpoint of affordability. Colorado's experience with our Act and regulations, which create a six-month repayment *minimum*, have helped reduce the risk that consumers will suffer from continuous indebtedness and constant reborrowing from these type of loans. Large one-time payments have proven to be the source of the problem. Rather, having an affordable payment is key to successful repayment of the loan for both the consumer and the lender. A properly structured loan, based on the results of the underwriting process, will rarely result in a single payment loan. As such, I encourage the CFPB to explore the option of requiring lenders to originate multiple installment loans that will amortize over several consumer income cycles.

There is little doubt that your agency's current proposals, if implemented, will have an impact on the high interest rate lending industry, especially smaller lending entities. This will likely result in less competition among lenders and decreased access to credit for low-income consumers. Given the experiences and data collected after the significant changes to the Colorado payday lending law in 2010,[1] and the success we've enjoyed since it was amended, we believe our input would be extremely beneficial as the CFPB attempts to enter this field of regulation.

We ask you to consider what the states have done and where they have succeeded in working with the lending industry to reach a model that works. Too often this administration has attempted to overlay its prerogatives onto the states despite the states having already adequately solved the problem. I hope you agree that this is an opportunity to work together and get it right.

We look forward to you contacting our office so we can begin a productive dialogue. Please feel free to contact Ms. Julie Ann Meade, First Assistant Attorney General for our Consumer Credit Unit at 720-508-6109 or julie.meade@state.co.us.

Sincerely,

Cynthia H. Coffman

CYNTHIA H. COFFMAN
Attorney General

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[1] Please see the Pew Charitable Trusts' report entitled "Payday Lending in America: Policy Solutions" for data on Colorado's successes in this area. http://www.pewtrusts.org/en/research-and-analysis/reports/2013/10/29/payday-lending-in-america-policy-solutions

Faith for Just Lending

a coalition to end predatory payday lending

February 11, 2016

The Honorable Randy Neugebauer
Chairman
Subcommittee on Financial Institutions and
Consumer Credit
House Financial Services Committee
United States House of Representatives
2129 Rayburn House Office Building
Washington, D.C. 20515

The Honorable William 'Lacy' Clay, Jr.
Ranking Member
Subcommittee on Financial Institutions and
Consumer Credit
House Financial Services Committee
United States House of Representatives
2129 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairman Neugebauer and Ranking Member Clay:

We write as a diverse and non-partisan group of religious leaders, practitioners, and social service providers who are working together to end the predatory practices of payday lending. We are uniform in our belief that usurious and deceptive debt trap lending is a moral issue that calls for a government response. Our churches and members have been working at the local, state and federal level to reform this practice. While some states have effectively reined in the worst abuses of this industry, many have not, leaving households ensnared in the vicious cycle of debt that is part of the business model for some engaged in the payday lending industry.

We appreciate the subcommittee's interest in the payday loan industry, but we are concerned that today's hearing does not reflect an urgency to help constituents trapped in predatory loans. The so-called short-term loans involved in payday lending, with initial terms of two weeks, often result in long-term debt. According to a survey of payday borrowers conducted by the Pew Charitable Trusts only 14% of borrowers can afford to pay off the average payday loan out of their monthly budget. This leads to a pattern of re-borrowing and long-term debt such that 76% of all loans are renewals or quick re-borrows. By setting their customers up in this debt trap, lenders increase fees and profits, while making their customers more likely to lose their bank accounts, fall behind on expenses, and file for bankruptcy.

We urge this subcommittee to offer ideas and work towards a positive solution. For our ministers and congregations these are not just statistics, they are the faces of their congregants and community members who have come to them for help. One reform that has proven effective in many states is limiting loans to 36% APR. Likewise, in 2006, Congress limited the rates on loans made to members of the military and their families to 36% APR. Some payday lenders claim they cannot stay in business under such regulations. However, these experiments demonstrate that small dollar lending remains viable and families fare better with reasonable terms of credit.

We agree that individuals should manage their resources responsibly, save for emergencies, and help others in need. In fact, we often ask our churches and institutions to teach responsible stewardship and assist neighbors in times of crisis. We also believe lenders should extend loans at reasonable interest rates based on ability to repay within the original loan period, taking into account the borrower's income and expenses. This is a basic, common sense requirement of traditional lending and one that should be employed in small, short-term loans as well.

Our nation can do better than putting the entire burden on desperate people to ensure they are not being preyed upon by unethical business practices. Lenders should not be able to take advantage of those who are most vulnerable and who have little or no resources at their disposal. Indeed, short-term loans should help borrowers get out of a financial crisis, not become more deeply entrenched in one.

We are confident effective legislation is possible. We offer ourselves and our expertise to you as you seek a real solution that helps those with immediate financial needs while prohibiting usury and deceptive lending practices and request that this letter be entered into the public record.

Sincerely,

Southern Baptist Ethics & Religious Liberty Commission
United States Conference of Catholic Bishops
National Association of Evangelicals
National Latino Evangelical Coalition
National Baptist Convention, USA, Inc.
Cooperative Baptist Fellowship
Center for Public Justice
Ecumenical Poverty Initiative
PICO National Network

cc: The Honorable Jeb Hensarling, Chairman
cc: The Honorable Maxine Waters, Ranking Member

"Short-term, Small Dollar Lending: The CFPB's Assault on Access to Credit and Trampling of State and Tribal Sovereignty"
Subcommittee on Financial Institutions and Consumer Credit

February 11, 2016 1:00 PM
Questions for the Record
for Robert Sherill [signature]
Submitted by Representative Keith Ellison

I appreciate your willingness to provide testimony before the Financial Services Committee. I also greatly appreciate your efforts to better your life. Please provide answers to the following questions about your loan from Advance Financial.

- When did you take the loan – month and year? 10/28/14
- How much did you borrow? 1105
- How long was the loan term? 30 days
- Were there any prepayment penalties? no
- Were there any fees other than interest? If so, what were they? 22% interest per month
- Was there an origination fee? no
- After taking this loan from Advance Financial, did you take additional loans from them? If yes, how soon after you took the first loan did you take additional loans? Had you paid off the first loan before taking the second loan or did you roll the first loan into the second and/or subsequent loans? I renewed the loan 4 times I paid in full on the fifth month
- Did you take another loan with another small dollar lender within the next two months? I don't remember but I did get a loan from another place. I don't know if it was 2 months or not.
- How did you repay the loan? Was it a lump sum payment due in a couple of weeks or installment payments over several months? I believe you said you did not have a bank account at the time so did you pay by cash or money order or did you use some other method? I paid in cash and with a credit card. I paid 4 smaller payments then paid off.
- I believe you said your employees use loans from small dollar lenders like Advance Financial. What is the hourly wage you pay your employees? Do they feel this salary is adequate to meet their financial needs? Why do they seek loans from Advance Financial or other lenders? Have you tried to establish a banking relationship for your employees where they can have direct deposit and small dollar loans? Are you familiar with the income advance loans that other employers provide to their workers such as the Working Bridges in Chittenden County, Vermont. Details here: http://www.unitedwaycc.org/files/galleries/Working_Bridges_Profile_FINAL.pdf?

See back →

I pay my employees $9.50/hr, a fair wage for cleaning service. Everybody thinks they want to make more money. My employees get loans because they spend more than they make. They don't want bank acounts. Stores like AF are open 24/7, have free bill pay and free money orders, and cheap check cashing. I am not interested in making loans to my employees. I'm in the cleaning business not the lending business.

[illegible]

House Committee on Financial Services
Subcommittee on Financial Institutions and Consumer Credit
Short-term, Small Dollar Lending:
The CFPB's Assault on Access to Credit and Trampling of State and Tribal Sovereignty
Questions for the Record
February 11, 2016

Questions for Acting Deputy Director David Silberman, Consumer Financial Protection Bureau, from Congressman Keith Ellison:

Question 1

I strongly support your efforts to rein in harmful payday loan practices. But I'm concerned about the ability for banks and credit unions to offer affordable alternatives at scale. Is the CFPB considering streamlined guidelines for banks and credit unions? If so, will they be clear enough to foster the development of new small loan alternatives that could better serve the millions of people who use payday loans today?

Response

The Consumer Financial Protection Bureau is committed to fulfilling the dual purposes set out in the Consumer Financial Protection Act of 2010 of pairing access to consumer financial products and services with fair, transparent, and competitive markets. In crafting a proposed regulation of payday, vehicle title, and similar loans, the Bureau is carefully considering the costs and benefits of such regulation to consumers and lenders and is seeking to balance the need for important consumer protection in these markets with access to credit for consumers. In general, the Bureau's proposals under consideration would require lenders to determine a consumer's ability to repay a payday, vehicle title, or similar loan; the proposals would also permit lenders to make certain loans meeting clear structural and other criteria without reaching a determination of ability to repay. The alternatives that the Bureau is considering to the ability-to-repay requirement would be available to all lenders making loans covered by the regulation, including banks and credit unions.

Question 2

During last fall's House Financial Services Hearing on the CFPB's semi-annual report to Congress, I asked Director Cordray about the longer-term alternative sections of the SBREFA framework, and more specifically the 5% payment-to-income alternative section, and offered my support. Does the CFPB still have the goal of including a longer-term "alternative" option that sets clear rules for affordable payments and reasonable durations?

Response

The Bureau continues to refine the proposed approach to regulation in the markets for payday, vehicle title, and similar loans. As part of this framework for regulation, the Bureau continues to believe that permitting lenders some underwriting flexibility when making certain carefully-structured covered longer-term loans may be one important component and continues to develop options for doing so.

House Committee on Financial Services
Subcommittee on Financial Institutions and Consumer Credit
Short-term, Small Dollar Lending:
The CFPB's Assault on Access to Credit and Trampling of State and Tribal Sovereignty
Questions for the Record
February 11, 2016

Questions for Acting Deputy Director David Silberman, Consumer Financial Protection Bureau, from Congresswoman Kyrsten Sinema:

Question 1

The proposal currently being considered would apply to payday loans, vehicle title loans, deposit advance products, and certain high-cost installment and open-end loans. Please provide clarification as to why the Bureau has chosen to combine these loans into one rulemaking.

Do you anticipate that these products will be linked together in the final rulemaking, or have you considered issuing separate rulemakings?

Response

In March 2015, the Consumer Financial Protection Bureau released the outline of proposals under consideration, including payday, vehicle title, and similar loans. While the precise structure and certain features of these products vary to some degree, the markets that would be covered by the Bureau's proposals under consideration share important similarities in both product structure and lender practices. The Bureau is concerned that certain lender practices are causing substantial consumer harm throughout the markets, and that such practices may be best addressed through the same rulemaking. After releasing the proposals under consideration, the Bureau convened a Small Business Review Panel, which included representatives from each potentially affected market to obtain feedback on the proposals under consideration. The Bureau is continuing to develop a proposed rulemaking on these products.

Question 2

It is my understanding that the Bureau is considering a proposal that would generally cover longer-term credit products with a contractual duration longer than 45 days and an all-in annual percentage rate in excess of 36 percent where the lender holds either (1) access to repayment through a consumer's account or paycheck, or (2) a non-purchase money security interest in the consumer's vehicle.

Additionally, the Bureau is considering a proposal to allow lenders to offer covered longer-term loans without conducting the full ability-to-repay determination, as long as the loan has payments below a specified payment-to-income ratio and meets certain other requirements.
I would like to learn more about how the CFPB determined the all-in annual percentage rate of 36 percent, as well as why the CFPB is considering setting the payment-to-income ratio at 5 percent?

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Response

The cost threshold for coverage under the proposals under consideration would focus the Bureau's regulation on those longer-term loans that the Bureau believes pose the greatest risk of harm to consumers. The Bureau has considered various ways of calculating the cost threshold, including considering the Military Annual Percentage Rate under 32 CFR part 232, which would permit lenders to determine whether their loans would be covered under the Bureau's regulation by using the same calculation that a lender would use to determine the costs of loans made to servicemembers and their families under the Military Lending Act.

One proposal under consideration as part of the framework for regulation of covered longer-term loans would permit lenders to make a covered longer-term loan without undertaking the proposed ability-to-repay determination if, among other criteria, the loan has periodic payments that are not more than five percent of the consumer's gross income during the same period. The payment-to-income approach would permit lending without satisfying the requirements of an ability-to-repay determination, while imposing important structural and other requirements for such loans. The Bureau continues to refine the proposed approach to regulation in the markets for payday, vehicle title, and similar loans. As part of this framework for regulation, the Bureau continues to believe that permitting lenders some underwriting flexibility when making certain carefully-structured covered longer-term loans may be one important component and continues to develop options for doing so.

Question 3

Please provide information about the data that informed the vehicle title component of the forthcoming *Rulemakings for Payday, Vehicle Title, and Similar Loans.*

Did the Bureau compile and refer to research on the existing processes and procedures used by title lenders nationwide to determine a borrower's ability to repay (including non-traditional methods)?

Response

In developing proposals for regulation in the market for vehicle title loans—along with payday and similar loans—the Bureau has examined information from a wide variety of sources, including the agency's market monitoring, enforcement, and supervisory activities. The Bureau has carefully looked at state laws and regulations on vehicle title lending and met with representatives of state, local, and tribal governments, industry, and consumer advocates to hear their views on practices and regulation in the market for vehicle title loans. In addition, during the Small Business Review Process, the Bureau heard from Small Entity Representatives about their processes for making vehicle title loans.

House Committee on Financial Services
Subcommittee on Financial Institutions and Consumer Credit
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The CFPB's Assault on Access to Credit and Trampling of State and Tribal Sovereignty
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Question 4

With no readily accessible alternative sources of short-term credit, I am concerned about the everyday implications of the Bureau's forthcoming rulemaking.

In particular, does the CFPB have data highlighting: (1) current product usage (specifically as relates to title loans), both nationwide and in Arizona; and (2) the impact the rulemaking will have on such product usage and the availability of credit to consumers, including the specific impact on Arizona.

Response

The Bureau is using loan-level data from several large lenders that offer a range of vehicle title loan products to analyze consumers' current use of the products and the likely impacts of any proposed regulation on product usage and the availability of vehicle title credit. The Bureau is also reviewing publicly available information, such as data and publications from state regulators and research published by academic and other researchers, to supplement its own analysis. The Bureau will publish the results of its analysis prior to, or contemporaneously with, a proposed rulemaking covering vehicle title loans.

Question 5

It is my understanding that the Bureau is considering proposals that would require lenders to determine that a consumer has the ability to repay a loan.

Will the Bureau's ability-to-repay determination requirements be principles-based or specifically prescribed guidelines? How will the Bureau measure outcomes to determine if access to credit is impacted?

Response

At the core of the proposals under consideration that the Bureau is considering is a requirement that lenders take into consideration a consumer's income and major financial obligations to determine a consumer's ability to repay the loan without reborrowing. During the Small Business Review Process and in outreach with numerous stakeholders, including industry, consumer groups, representatives from state, local, and tribal governments, Members of Congress, and other financial regulators, the Bureau has received substantial feedback on the ability-to-repay approach, the potential costs to lenders and consumers of that approach, and the potential impact on consumer access to credit. The Bureau continues to refine the proposals under consideration and will look forward to continuing to receive feedback on the proposed set of requirements for determining ability to repay, the costs of the regulation, and the impact on access to credit following publication of a notice of proposed rulemaking.