NCRC
OPENING DOORS TO ECONOMIC OPPORTUNITY

January 22, 2019

Robert E. Feldman, Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 Seventeenth Street NW
Washington, D.C. 20429

Re: Small Dollar Lending Request for Information, RIN 3064-ZA04

Dear Executive Secretary Feldman:

On behalf of the National Community Reinvestment Coalition (NCRC) and our more than 600 community-based organizations, thank you for the opportunity to comment on the Federal Deposit Insurance Corporation's (FDIC's) Request for Information on small-dollar lending. NCRC's mission for the past 25 years has been to create opportunities for people and communities to build and maintain wealth. NCRC members include community reinvestment organizations, community development corporations, local and state government agencies, faith-based institutions, fair housing and civil rights groups, minority and women-owned business associations, housing counselors, and social service providers from across the nation. NCRC is concerned about the debt trap that can be created by high-cost small dollar loans, and the perpetual long-reaching harms they can cause to families working to build wealth.

NCRC shares the FDIC's goal of greater financial inclusion for low-income consumers and communities of color. We also know too well the harm that unaffordable, high-cost loans cause these communities. NCRC and its member organizations strongly encourage the FDIC to facilitate supervised financial institutions offering responsible and affordable small installment loans, while preventing harmful deposit advance loans and the use of dangerous "rent-a-charter" deals with payday lenders. Banks are in the best position to offer safe and affordable small-dollar loan products and these products are consistent with their obligations under the Community Reinvestment Act. Any guidance by the FDIC should remain consistent with the agency's Affordable Small-Dollar Loan Guidelines, the small-dollar loan pilot program and the FDIC's *Safe*, Affordable and Feasible Template.[1]

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[1] FDIC, *Affordable Small-Dollar Loan Products Final Guidelines* (June 2007)

Background

The FDIC's latest National Survey of Unbanked and Underbanked Households found that 19% of American families are both banked and also turning to alternative financial products, including harmful high-cost payday and auto title loans.[2] The Consumer Financial Protection Bureau (CFPB) research has documented the extent to which these products can be unaffordable debt traps for consumers, finding that 75 percent of all payday loan fees are due to borrowers trapped in more than 10 loans a year, and that 80 percent of all car title loans are due to borrowers trapped in more than seven loans a year.[3]

Consumers spend more than $30 billion in fees and interest each year for high-cost, non-bank small loans.[4] Payday loans typically carry annual percentage rates (APRs) of 300-500% and are due on the borrower's next paycheck, approximately two weeks later, in a lump-sum payment that often consume about a third of the average customer's paycheck, making the loans difficult to repay without borrowing again.[5] Payday lenders continue to rely on their ability to collect from borrowers' checking accounts, leading some bank customers to lose their checking accounts in connection with payday loans. Payday lenders repeatedly charge borrowers fees to renew unaffordable loans, and their business model succeeds because borrowers fail to repay the loans as advertised.

Rather than see their customers leave the bank to borrow payday loans at 400% APR, banks should be encouraged to provide safe, small installment loans directly. Banks should be encouraged to offer safer loans for a fraction of the cost of payday, auto title, pawn, rent-to-own or other high-cost credit that underbanked consumers use today.

Typical Cost of Borrowing $400 for 3 months[6]					
New Bank Small Dollar Loan (e.g. U.S. Bank Simple Loan Product)	**Typical Payday Loan**	**Typical Auto Title Loans**	**Paying 8 Overdraft Fees ($35)**	**Typical Pawn Loan**	**Typical Deposit Advance (discontinued)**
$48-60	$360	$300	$280	$240	$240

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[2] FDIC, 2017 FDIC National Survey of Unbanked and Underbanked Households (October 2018) https://www.fdic.gov/householdsurvey/

[3] Consumer Financial Protection Bureau (CFPB), Payday Loans and Deposit Advance Products: A White Paper of Initial Data Findings (2013), available at: https://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf

[4] Center for Financial Services Innovation, *2014 Underserved Market Size: Financial Health Opportunity in Dollars and Cents* (December 2015), http://www.cfsinnovation.com/Document-Library/2014-Underserved-Market-Size-Financial-Health-Oppo

[5] The Pew Charitable Trusts, *Payday Loan Customers What More Protections, Access to Lower-Cost Credit From Banks* (April 2017) https://bit.ly/2VIrEno

[6] The Pew Charitable Trusts, Presentation, *FDIC Requests Comments on Small Loans from Banks - Opportunity to save millions of American consumers billions of dollars a year* (December 12, 2018).

The FDIC should encourage only loans that are affordable and responsible

The FDIC's Small-Dollar Loan Pilot program demonstrated that banks can offer alternatives to high-cost loans, emergency credit products, such as payday loans and overdrafts, in ways that build or retain profitable, long term relationships with consumers and also create good will in the community. The CFPB's October 2017 Payday Lending Ruleprovides a strong foundation that protects consumers and leaves the door open for banks to challenge predatory lenders by offering fair products of their own. [7] The Office of the Comptroller of the Currency (OCC) has also taken steps to encourage banks to offer small-loan products.[8] The FDIC should continue to encourage small-dollar bank products that are safe and affordable alternatives to payday loan options. Millions of underbanked consumers stand to benefit by switching to use these lower-cost options and save billions of dollars each year.[9]

The FDIC must require that any bank product is supported by sound underwriting, which focuses on a borrower's ability to repay a loan, based on their circumstances and other outstanding obligations. Banks should be encouraged to make sure all small loans have reasonable safeguards including affordable payments, appropriate terms, and fair prices. We support the affordability and pricing provisions in the FDIC's Affordable Small-Dollar Loan Guidelines, and the agency should continue to encourage lenders to offer small-dollar credit with APRs no greater than 36 percent - a limit that is widely recognized as a safe and responsible, is codified in the Military Lending Act, and is the state interest rate cap in the majority of states. Research also suggests that small-dollar loans are not affordable, on average, if payments take more than 5 percent of a borrower's paycheck.[10] However, to truly ensure affordability, the FDIC must encourage banks to consider the borrower's income and expenses before making the loan. Relying on income-only standards like a "payment-to-income" ratio is not the ability-to-repay, and could result in widespread unaffordable lending. APRs should also decline as loan sizes increase; the relatively high APRs that might be needed to make small loans profitable are not justified for larger loans.

Safe and responsible loan products must also include features such as time to pay, credit building, and blocks on overdraft fees. Borrowers need more than two weeks to repay. One of the important lessons learned from the success of the FDIC's own small-dollar pilot was the importance of longer loan terms, followed by streamlined but solid underwriting. The CFPB also wisely acknowledged this in its Payday Loan Rule by including additional restrictions for loans due back in less than 45 days. Successful repayment should be reported to credit bureaus so borrowers can improve their credit scores and qualify for mainstream products like auto

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[7] https://www.consumerfinance.gov/policy-compliance/rulemaking/final-rules/payday-vehicle-title-and-certain-high-cost-installment-loans/

[8] OCC, Core Lending Principles for Short-Term, Small-Dollar Installment Lending (May 23, 2018).

[9] The Pew Charitable Trusts, *Standards Needed for Safe Small Installment Loans From Banks, Credit Unions* (February 2018) https://bit.ly/2TtnHkm

[10] Pew Charitable Trusts, Payday Lending in America: Policy Solutions (2013) available at: https://www.pewtrusts.org/~/media/legacy/uploadedfiles/pcs_assets/2013/pewpaydaypolicysolutionsoct2013pdf.pdf

loans and mortgages. This is vital aspect for wealth building for consumers, and ultimately benefits the lending institutions by creating a long term, creditworthy borrower. Payments on small loans from banks should never trigger overdraft fees. Harmful overdraft fees drive struggling consumers out of the banking system. Affordable small installment loans products should strive to eliminate the debt trap perpetuated by overdraft fees caused by payday lenders and replace the practice of "borrowing" through over drafting bank accounts. Any fees charged, other than a small application or annual fee, should be charged monthly and spread evenly over the life of the loan. This will prevent borrowers from being penalized for repaying early and avoid encouraging lenders to refinance loans.

These safeguards are critical to ensure that bank loan programs, particularly those designed for financially distressed consumers, promote financial inclusion rather than exacerbate financial distress.

The FDIC should motivate innovative and credit building products

For small installment products to become competitive in the payday lending marketplace, the FDIC should continue to encourage the use of technology and automated processes so that approval time is quick. In a 2017 Pew survey of 826 borrowers, 8 of 10 borrowers stated they would prefer to borrow from a bank or credit union if they were equally likely to be approved. These borrowers also rated the speed on receiving funds (76%) and the ease of applying (64%) as being "very important".[11] The cost of manually processing applications is too high to offer small loans at scale. A structured, automated "pre-approval" system for all deposit customers could ease approval processing time and cost. This could mean some additional time would be required for banks or credit unions to process loan applications from people who are not already their customers, but the financial institutions may find it worthwhile to do so since it would mean acquiring new accountholders.

In addition to reporting on-time payments to credit bureaus, the FDIC should encourage banks to offer a suite of lending products with a thoughtful approach to credit building for its borrowers. A meaningful suite of products could work to escalate borrowers into better cost products as their creditworthiness improves. Banks should be encouraged to carefully tailor their underwriting criteria for small-dollar installment and other loan products so they can be competitive, while still ensuring they are lending in a safe and sound manner. Implementing underwriting metrics that include factors such as whether the customer is maintaining an account in good standing; the length of the customer's relationship with the bank or credit union; regularity of deposits; and the absence of any warning signs such as recent bankruptcies or major problems with overdrafts. Taking into account underwriting criteria other than credit scores and working with borrowers to build their credit worthiness over time would go a long

[11] The Pew Charitable Trusts, *Payday Loan Customers What More Protections, Access to Lower-Cost Credit From Banks* (April 2017) https://bit.ly/2VIrEno.

way in wealth building for the borrower and creating long term, reliable customers for the financial institution.

Small-dollar lending and CRA

The agencies could use the Community Reinvestment Act (CRA) more effectively to promote safe and sound small dollar consumer lending. The Interagency Question and Answer (Q&A) document provide a few Q&As that encourage banks to make safe and sound loans based on a borrower's ability to repay. The Q&As encourage reporting to consumer reporting agencies and programs that transition borrowers from loans with higher interest rates to lower cost loans.[12] However, these Q&As are not implemented by examiners on a regular basis. One difficulty is that CRA exams do not routinely scrutinize consumer lending and will do so either at the request of a bank or if a substantial majority of an institution's loans are consumer loans.[13] A recent GAO study found that only 25 percent of large bank exams looked at consumer lending while only 3 percent of intermediate small bank and 6 percent of small bank exams evaluated consumer lending.[14]

A plethora of needs for unmet consumer lending exists ranging from the needs for small dollar loans to finance emergency expenses, automobile loans (particularly for rural counties and other parts of the country without regular transit service), credit cards, and student loans. If a bank makes a substantial number of consumer loans, examiners should assess whether these loans are safe and affordable and whether they are serving low- and moderate-income borrowers and communities. In addition, the current treatment of major credit card banks as so-called wholesale and limited purpose banks must end since exams of wholesale and limited purpose banks do not examine consumer lending such as credit card lending.

The FDIC must prevent partnerships that evade State laws and prey on consumers

The FDIC must not sanction so called "rent-a-bank" schemes, where banks partner with state-regulated lenders in order to facilitate high-rate loans that would otherwise be illegal. These schemes threaten existing state laws and will ultimately cause severe harm to our nation's most financially distressed consumers. The longstanding precedent against rent-a-bank schemes has served banks and customers well. The FDIC, OCC, and Federal Reserve effectively ended most rent-a-bank schemes over a decade ago, with then-OCC Comptroller, John D. Hawke, stating that these schemes were "an abuse of national charter."[15] The OCC reaffirmed its position in its May 2018 Guidance stating "[t]he OCC views unfavorably an entity that partners with a bank

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[12] See Q&A to §_.22(a)—1 on page 48536 and §_.22(b)(5)—1:, p. 48539 in Interagency Questions and Answers Regarding Community Reinvestment, Federal Register, Vol. 81, No. 142, July 25, 2016.

[13] See Q&A §_.22(a)(1)—2: on page 48536 of Interagency Q&A

[14] Government Accountability Office, *Community Reinvestment Act: Options for Treasury to Consider to Encourage Services and Small-Dollar Loans When Reviewing Framework*, GAO-18-244: Published: Feb 14, 2018. Publicly Released: Mar 16, 2018, https://www.gao.gov/products/GAO-18-244

[15] https://www.occ.treas.gov/news-issuances/news-releases/2002/nr-occ-2002-10.html

with the sole goal of evading a lower interest rate established under the law of the entity's licensing state(s)."[16]

However, some FDIC-supervised banks are still engaging in this practice, resulting in irresponsible high-cost loans.[17] If sanctioned, these partnerships pose a threat to one of the most significant protections against predatory small dollar loans, state interest rate limits. It is essential the FDIC put an end to these rent-a-bank schemes and prevent new ones from emerging.

The FDIC must prevent harmful deposit advance loans

The FDIC must retain its 2013 guidance against unaffordable bank "deposit advance" loans. The evidence overwhelmingly shows that these were debt-trap payday loans that piled onto bank customers' existing unsustainable debt load. [18] These products are not an alternative to payday loans; they *are* payday loans. FDIC-supervised banks never made these loans, and for the agency to encourage them now would be reckless.

Conclusion

NCRC urges the FDIC to make sure banks are expanding access to affordable credit through proper assessments of the borrower's true ability-to-repay and reasonably priced interest rates. Given that many financially struggling consumers are already overburdened by credit, the FDIC must encourage credit building products and take all needed steps to root out abusive overdraft fees. These initiatives would go a long way toward increasing economic inclusion among our nation's financially vulnerable. With clear guidance and strong consumer safeguards from the FDIC, we're hopeful that consumers who are currently being taken advantage of outside the banking system can gain access to much better, bank-issued small installment loans and collectively save billions of dollars each year.

If you have any questions, please contact Gerron Levi, Director of Policy & Government Affairs at (202) 464-2708 or glevi@ncrc.org.

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[16] https://www.occ.gov/news-issuances/bulletins/2018/bulletin-2018-14.html

[17] *See, e.g.*, Opploans, making 160% APR loans though FinWise Bank; Elevate making 96% APR loans on its Elastice product through Republic Bank & Trust.

[18] CFPB, *Payday Loan and Deposit Advance Products: A White Paper of Initial Data Findings* (April 2013), available at: https://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf and *Supplemental findings on payday, payday installment, and vehicle title loans, and deposit advance products* at 39 (June 2016), available at: https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/Supplemental_Report_060116.pdfDeposit advances had APRs ranging from 152 percent to 456 percent; more than half of deposit account customers had outstanding deposit advances totaling more than $3,000 and about two-thirds of customers had overdrafts. Deposit advance borrowers were seven times more likely to have their accounts charged off than their counterparts who did not take deposit advance loans.

Sincerely,

National Community Reinvestment Coalition
Affordable Homeownership Foundation Inc.
African Career Education and Resource, Inc
CAARMA (Consumer Advocates Against Reverse Mortgage Abuse)
California Coalition for Rural Housing
California Resources and Training
CASA of Oregon
Center for NYC Neighborhoods
City of Toledo
Community Action Association of Alabama
Community Service Network Inc
County Corp
Delaware Community Reinvestment Action Council, Inc.
Edgemoor Revitalization Cooperative, Inc.
Ellendale Community Civic Improvement Association (ECCIA)
Fair Finance Watch
Georgia Advancing Communities Together, Inc.
Harlingen CDC
Hawai'i Alliance for Community-Based Economic Development
Housing Education and Economic Development
JCVision and Associates, Inc.
Jurisdiction-Wide Resident Advisory Board (J-R.A.B)
Kingsley House
Long Island Housing Services, Inc.
Maryland Consumer Rights Coalition
Mass. Assoc. of Community Development Corporations
Metropolitan St. Louis Equal Housing and Opportunity Council
Michigan Community Reinvestment Coalition
National Association of American Veterans, Inc.
NeighborWorks Umpqua
Northwest Indiana Reinvestment Alliance
PathStone Enterprise Center
R.A.A. - Ready, Aim, Advocate
S J Adams Consulting
Texas AgriForestry Small Farmers and Ranchers
Universal Housing Solutions CDC
Urban Economic Development Association of Wisconsin (UEDA)