



REPORT TO LAW & LEGISLATION COMMITTEE City of Sacramento

915 I Street, Sacramento, CA 95814-2671
www.CityofSacramento.org

CONSENT
August 4, 2011

Honorable Members of the
Law and Legislation Committee

Title: Legislative Position: Oppose AB 1158 (Calderon) California Deferred Deposit Transaction Law (Payday Lending)

Location/Council District: Citywide

Recommendation:

Adopt an Oppose position on AB 1158 (Calderon) California Deferred Deposit Transaction Law (Payday Lending).

Contact: Michelle Heppner, Special Projects Manager, Office of the City Manager, (916) 808-1226.

Presenters: N/A

Department: City Manager's Office

Division: Legislative Affairs

Organization No: 09200

Description/Analysis

Issue: A deferred deposit transaction is defined as a transaction in which a person defers depositing a customer's personal check until a specific date, pursuant to a written agreement for a fee. Under existing law, the California Deferred Deposit Transaction Law (CDDTL), regulates payday loan lenders, and places a number of restrictions on payday loans. For example, the CDDTL requires that payday lenders be licensed by Department of Corporations (DOC) and permits lenders to charge a fee of 15 percent of the face amount of the check which cannot have a face value of more than \$300. The Act also specifies disclosure and notice requirements, including that the annual percentage rate (APR) and any charges and fees be disclosed to the consumer.

AB 1158 proposes to increase the maximum value of a check for a payday loan from \$300 to \$500. This would also increase the 15% fee from \$45 for a \$300 loan to \$75 for a \$500 loan. According to the Department of Corporations' (DOC) 2010 Annual Report,

a total of 12.1 million payday loans were made totaling \$3.13 billion in 2010. Only 1.65 million individuals obtained payday loans which indicate that individuals are repeat customers and DOC's Annual Report also indicated they take out more than one loan at a time from multiple lenders. These figures illustrate the fundamental problem with the payday lending model in that it requires the borrower to repay the entire principal and interest from a single paycheck in just two weeks, hence ensuring that the typical borrower cannot pay back a loan without needing to take out another.

Furthermore, the DOC Annual Report indicated that the APR for these payday loans in 2010 averaged 414%. Federal law restricts the APR for payday loans to military members and their dependents to 36%.

Policy Considerations: Similar legislation, AB 377 (Mendoza) was proposed in 2009 wherein the increase from \$300 to \$500 was added after it passed Assembly and subsequently was held in Committee after hearing testimony on the bill. Opposition to this bill is consistent with previous positions taken with regard to bills for payday loans.

Environmental Considerations: N/A

Sustainability Considerations: N/A

Rationale for Recommendation: Payday Loans are widely used by the public however, individuals use them frequently and from multiple lenders which is contrary to its intended short term use. Setting a higher cap will undoubtedly increase individual's ability to access more cash and keep them in the longer-term lending spiral.

Financial Considerations: None.

Emerging Small Business Development (ESBD): N/A

Respectfully Submitted by: 
Michelle Heppner, Special Projects Manager

Recommendation Approved:


for WILLIAM H. EDGAR
Interim City Manager

Table of Contents:

Pg	1	Report
Pg	4	Attachments

Attachments

1	Pg	4	Draft Position Letter
2	Pg	5	Bill Text
3	Pg	10	Bill Analysis

Draft Oppose Letter

August 4, 2011

The Honorable Charles Calderon
California State Assembly
State Capitol
P.O. Box 942849
Sacramento, CA 94249-0058

RE: NOTICE OF OPPOSITION: AB 1158 California Deferred Deposit Transaction Law

Dear Assembly Member Calderon:

On behalf of the City of Sacramento, and as Chair of the Law and Legislation Committee, I am writing to inform you that we strongly oppose AB 1158 which increases the maximum value of a check for a payday loan from \$300 to \$500. Increasing the maximum value from \$300 to \$500 invariably increases the accompanying 15% fee respectively from \$45 to \$75 for each loan. In addition, an exorbitant Annual Percentage Rate, which according to the Department of Corporations averaged 414% in 2010, is charged on these loans. As a result, it adds to the fundamental problem with the payday lending model in that it requires the borrower to repay the entire principal and interest from a single paycheck in just two weeks, hence ensuring that the typical borrower cannot pay back a loan without needing to take out another.

Thank you for your attention to the City of Sacramento's concerns.

Sincerely,

JAY SCHENIRER, Chair
Law and Legislation Committee

cc: Senator Darrell Steinberg
Senator Ted Gaines
Assembly Member Roger Dickinson
Assembly Member Alyson Huber
Assembly Member Richard Pan
Mayor Johnson and Members of the City Council
David Jones, Emanuels and Jones and Associates

Attachment 2

AMENDED IN ASSEMBLY APRIL 13, 2011
AMENDED IN ASSEMBLY MARCH 21, 2011
CALIFORNIA LEGISLATURE—2011–12 REGULAR SESSION

ASSEMBLY BILL

No. 1158

Introduced by Assembly Member Charles Calderon

February 18, 2011

An act to amend Section ~~23027~~ 23035 of the Financial Code, relating to deferred deposit transactions.

LEGISLATIVE COUNSEL'S DIGEST

AB 1158, as amended, Charles Calderon. Deferred deposit transactions; advertising transactions.

Existing law, the California Deferred Deposit Transaction Law, provides for the licensure and regulation by the Commissioner of Corporations of persons engaged in the business of making or negotiating deferred deposit transactions, as defined. Existing law prohibits a licensee from placing an advertisement disseminated primarily in this state for a deferred deposit transaction unless the advertisement discloses that the licensee is licensed by the Department of Corporations. Existing law authorizes the commissioner to require licensees to maintain a file of all advertising copy for a period of 90 days from the date of its use and requires the file to be made available to the commissioner upon request. *Existing law authorizes a licensee to defer the deposit of a customer's personal check for up to 31 days, prohibits the face amount of the check from exceeding \$300, and requires each deferred deposit transaction to be made pursuant to a written agreement. A willful violation of the California Deferred Deposit Transaction Law is a crime.*

AB 1158

- 2 -

~~This bill would prohibit a licensee from placing an advertisement primarily intended to reach California residents, including advertisements on the Internet, unless the advertisement discloses that the licensee is licensed by the department, as specified. The bill would also authorize the commissioner to require licensees to maintain a file of all advertising copy currently in use and to retain that advertising copy for a period of 2 years from the date of its use instead authorize the face amount of a check for a deferred deposit transaction to be up to \$500.~~

~~Because a willful violation of these provisions by a licensee would be a crime under the California Deferred Deposit Transaction Law, the bill would impose a state-mandated local program.~~

~~The California Constitution requires the state to reimburse local agencies and school districts for certain costs mandated by the state. Statutory provisions establish procedures for making that reimbursement.~~

~~This bill would provide that no reimbursement is required by this act for a specified reason.~~

Vote: majority. Appropriation: no. Fiscal committee: yes.
State-mandated local program: *yes/no*.

The people of the State of California do enact as follows:

1 SECTION 1. Section 23035 of the Financial Code is amended
2 to read:

3 23035. (a) A licensee may defer the deposit of a customer's
4 personal check for up to 31 days, pursuant to the provisions of this
5 section. The face amount of the check shall not exceed ~~three five~~
6 hundred dollars ~~(\$300)~~ (\$500). Each deferred deposit transaction
7 shall be made pursuant to a written agreement as described in
8 subdivision (e) that has been signed by the customer and by the
9 licensee or an authorized representative of the licensee.

10 (b) A customer who enters into a deferred deposit transaction
11 and offers a personal check to a licensee pursuant to an agreement
12 shall not be subject to any criminal penalty for the failure to comply
13 with the terms of that agreement.

14 (c) Before entering into a deferred deposit transaction, licensees
15 shall distribute to customers a notice that shall include, but not be
16 limited to, the following:

17 (1) Information about charges for deferred deposit transactions.

1 (2) That if the customer's check is returned unpaid, the customer
2 may be charged an additional fee of up to fifteen dollars (\$15).

3 (3) That the customer cannot be prosecuted in a criminal action
4 in conjunction with a deferred deposit transaction for a returned
5 check or be threatened with prosecution.

6 (4) The department's toll-free telephone number for receiving
7 calls regarding customer complaints and concerns.

8 (5) That the licensee may not accept any collateral in conjunction
9 with a deferred deposit transaction.

10 (6) That the check is being negotiated as part of a deferred
11 deposit transaction made pursuant to Section 23035 of the Financial
12 Code and is not subject to the provisions of Section 1719 of the
13 Civil Code. No customer may be required to pay treble damages
14 if this check does not clear.

15 (d) The following notices shall be clearly and conspicuously
16 posted in the unobstructed view of the public by all licensees in
17 each location of a business providing deferred deposit transactions
18 in letters not less than one-half inch in height:

19 (1) The licensee cannot use the criminal process against a
20 consumer to collect any deferred deposit transaction.

21 (2) The schedule of all charges and fees to be charged on those
22 deferred deposit transactions with an example of all charges and
23 fees that would be charged on at least a one-hundred-dollar (\$100)
24 and a two-hundred-dollar (\$200) deferred deposit transaction,
25 payable in 14 days and 30 days, respectively, giving the
26 corresponding annual percentage rate. The information may be
27 provided in a chart as follows:

28

Amount Provided	Fee	Amount of Check	14-day APR	30-day APR
\$100	XX	XXX	XXX	XXX
\$200	XX	XXX	XXX	XXX

33

34 (e) An agreement to enter into a deferred deposit transaction
35 shall be in writing and shall be provided by the licensee to the
36 customer. The written agreement shall authorize the licensee to
37 defer deposit of the personal check, shall be signed by the
38 customer, and shall include all of the following:

AB 1158

— 4 —

- 1 (1) A full disclosure of the total amount of any fees charged for
- 2 the deferred deposit transaction, expressed both in United States
- 3 currency and as an APR as required under the Federal Truth In
- 4 Lending Act and its regulations.
- 5 (2) A clear description of the customer's payment obligations
- 6 as required under the Federal Truth In Lending Act and its
- 7 regulations.
- 8 (3) The name, address, and telephone number of the licensee.
- 9 (4) The customer's name and address.
- 10 (5) The date to which deposit of check has been deferred (due
- 11 date).
- 12 (6) The payment plan, or extension, if applicable as allowed
- 13 under subdivision (c) of Section 23036.
- 14 (7) An itemization of the amount financed as required under
- 15 the Federal Truth In Lending Act and its regulations.
- 16 (8) Disclosure of any returned check charges.
- 17 (9) That the customer cannot be prosecuted or threatened with
- 18 prosecution to collect.
- 19 (10) That the licensee cannot accept collateral in connection
- 20 with the transaction.
- 21 (11) That the licensee cannot make a deferred deposit transaction
- 22 contingent on the purchase of another product or service.
- 23 (12) Signature space for the customer and signature of the
- 24 licensee or authorized representative of the licensee and date of
- 25 the transaction.
- 26 (13) Any other information that the commissioner shall deem
- 27 necessary by regulation.
- 28 (f) The notice required by subdivision (c) shall be written and
- 29 available in the same language principally used in any oral
- 30 discussions or negotiations leading to execution of the deferred
- 31 deposit agreement and shall be in at least 10-point type.
- 32 (g) The written agreement required by subdivision (e) shall be
- 33 written in the same language principally used in any oral
- 34 discussions or negotiations leading to execution of the deferred
- 35 deposit agreement; shall not be vague, unclear, or misleading and
- 36 shall be in at least 10-point type.
- 37 (h) Under no circumstances shall a deferred deposit transaction
- 38 agreement include any of the following:
- 39 (1) A hold harmless clause.
- 40 (2) A confession of judgment clause or power of attorney.

1 (3) Any assignment of or order for payment of wages or other
2 compensation for services.

3 (4) Any acceleration provision.

4 (5) Any unconscionable provision.

5 (i) If the licensee sells or otherwise transfers the debt at a later
6 date, the licensee shall clearly disclose in a written agreement that
7 any debt or checks held or transferred pursuant to a deferred deposit
8 transaction made pursuant to Section 23035 are not subject to the
9 provisions of Section 1719 of the Civil Code and that no customer
10 may be required to pay treble damages if the check or checks are
11 dishonored.

12 ~~SECTION 1. Section 23027 of the Financial Code is amended~~
13 ~~to read:~~

14 ~~23027. (a) No licensee shall advertise, print, display, publish,~~
15 ~~distribute, or broadcast, or cause or permit to be advertised, printed,~~
16 ~~displayed, published, distributed or broadcast, in any manner, any~~
17 ~~statement or representation with regard to the business subject to~~
18 ~~the provisions of this division, including the rates, terms, or~~
19 ~~conditions for making or negotiating deferred deposit transactions;~~
20 ~~that is false, misleading, or deceptive, or that omits material~~
21 ~~information that is necessary to make the statements not false,~~
22 ~~misleading, or deceptive.~~

23 ~~(b) No licensee shall place an advertisement disseminated~~
24 ~~primarily in this state for a deferred deposit transaction or primarily~~
25 ~~intended to reach California residents, including advertisements~~
26 ~~on the Internet, unless the licensee, in the printed text of the~~
27 ~~advertisement or the oral text in the case of a radio or television~~
28 ~~advertisement, makes the following disclosure:~~

29 ~~—~~
30 ~~"[Insert name of licensee] is licensed by the Department of~~
31 ~~Corporations pursuant to the California Deferred Deposit~~
32 ~~Transaction Law."~~

33 ~~—~~
34 ~~(c) The commissioner may require that rates of charges or fees,~~
35 ~~if stated by the licensee, be stated fully and clearly in the manner~~
36 ~~that the commissioner deems necessary to give adequate~~
37 ~~information to, or to prevent misunderstanding by, prospective~~
38 ~~customers.~~

AB 1158

— 6 —

1 ~~(d) No advertising copy shall be used after its use has been~~
2 ~~disapproved by the commissioner and the licensee is notified in~~
3 ~~writing of the disapproval.~~
4 ~~(e) The commissioner may require licensees to maintain a file~~
5 ~~of all advertising copy currently in use and to retain that advertising~~
6 ~~copy for a period of two years from the date of its use. The file~~
7 ~~shall be available to the commissioner upon request.~~
8 ~~SEC. 2. No reimbursement is required by this act pursuant to~~
9 ~~Section 6 of Article XIII B of the California Constitution because~~
10 ~~the only costs that may be incurred by a local agency or school~~
11 ~~district will be incurred because this act creates a new crime or~~
12 ~~infraction, eliminates a crime or infraction, or changes the penalty~~
13 ~~for a crime or infraction, within the meaning of Section 17556 of~~
14 ~~the Government Code, or changes the definition of a crime within~~
15 ~~the meaning of Section 6 of Article XIII B of the California~~
16 ~~Constitution.~~

SENATE JUDICIARY COMMITTEE
Senator Noreen Evans, Chair
2011-2012 Regular Session

AB 1158 (Calderon)
As Amended April 13, 2011
Hearing Date: July 5, 2011
Fiscal: Yes
Urgency: No
SK:rm

SUBJECT

California Deferred Deposit Transaction Law (Payday Lending)

DESCRIPTION

Existing law permits payday lenders to defer the deposit of a customer's personal check for up to 31 days. The maximum value of a check for a payday loan is limited to \$300, and the maximum fee cannot be more than 15% of the face amount of the check.

This bill would increase the maximum value of a check for a payday loan from \$300 to \$500.

BACKGROUND

Current law, the California Deferred Deposit Transaction Law (CDDTL), regulates payday loan lenders, and places a number of restrictions on payday loans. For example, the CDDTL requires that payday lenders be licensed by Department of Corporations (DOC) and permits lenders to charge a fee of 15 percent of the face amount of the check which cannot have a face value of more than \$300. The Act also specifies disclosure and notice requirements, including that the annual percentage rate (APR) and any charges and fees be disclosed to the consumer.

Recent figures from DOC indicate that, as of December 31, 2010, there were 2,144 licensed payday loan locations in California. In 2010, 1.65 million Californians took out 12 million payday loans worth approximately \$3.13 billion.

(more)

AB 1158 (Calderon)
Page 2 of ?

The following information was obtained from DOC's "2010 Annual Report: Operation of Deferred Deposit Originators under the California Deferred Deposit Transaction Law" (2010 Annual Report):

	2006	2007	2008	2009	2010
Total dollar amount of payday loans made	\$2.55 billion	\$2.97 billion	\$3.1 billion	\$3.19 billion	\$3.13 billion
Total number of payday loans made	10.05 million	11.15 million	11.8 million	11.88 million	12.1 million

Total number of individual customers who obtained payday loans (repeat customers counted once)	1.43 million	1.61 million	1.67 million	1.57 million	1.65 million
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In addition, the 2010 Annual Report provides the following information with respect to individual payday loans made:

	2006	2007	2008	2009	2010
Average dollar amount of payday loans made	\$254	\$266	\$262	\$262	\$258
Minimum dollar amount of payday loans made	\$10	\$10	\$6	\$8	\$4
Maximum dollar amount of payday loans made	\$300	\$300	\$300	\$300	\$300
Average annual percentage rate	429%	424%	416%	414%	414%

AB 1158 (Calderon)
Page 3 of ?

(APR)					
Average number of days of payday loan transactions	16	16	17	17	17

In 2008, DOC released two reports, "California Deferred Deposit Transaction Law, California Department of Corporations, December 2007" (DOC Report) and "2007 Department of Corporations Payday Loan Study" (AMPG study).

The DOC report was based upon a survey of payday lenders and DOC's annual report for 2005-06. The AMPG study was based on an online survey of payday lenders, a telephone survey of borrowers, and five customer focus groups. AMPG's study was conducted between August and December 2007, for the 18-month period between April 15, 2006 through September 11, 2007. Both reports highlighted that, while a payday loan is intended to be a short-term, one-time loan to meet emergency financial needs, a large number of Californians use payday loans on a regular, on-going basis and find that establishing a payday loan account "opens the door to a repetitive cycle of borrowing that is difficult if not impossible to end" (AMPG study). The DOC report also found that 2.4 percent of payday loan borrowers took out more than one loan at the same time from multiple lenders.

In 2009, AB 377 (Mendoza), among other things, proposed to increase the amount of a payday loan check from \$300 to \$500. That increase was added to the bill after it passed the Assembly. This Committee held the bill after hearing testimony.

Like AB 377, this bill would increase the maximum value of a check for a payday loan from \$300 to \$500.

CHANGES TO EXISTING LAW

Existing federal law imposes a 36% APR on consumer credit, including payday loans, extended to members of the military and their dependents. (10 USC Sec. 987.) Existing state law gives DOC the authority to enforce these protections under the CDDTL. (Fin. Code Sec. 23038.)

Existing law regulates, under the CDDTL, deferred deposit transactions, defined as a transaction in which a person defers depositing a customer's personal check until a specific date,

AB 1158 (Calderon)
Page 4 of ?

pursuant to a written agreement for a fee. (Fin. Code Sec. 23000 et seq.)

Existing law places the following restrictions on payday lenders:

- limits the maximum value of the check to \$300;
- permits payday lenders to defer the deposit of a customer's personal check for up to 31 days; and
- limits the maximum fee to 15% of the face amount of the check. (Fin. Code Secs. 23035(a), 23036(a).)

Existing law prohibits payday lenders from entering into a payday loan with a customer who already has a payday loan outstanding. (Fin. Code Sec. 23036(c).) —

This bill would increase the maximum value of a check for a payday loan from \$300 to \$500.

COMMENT

1. Stated need for the bill

The author writes that "California currently allows the lowest maximum limit for deferred deposit transaction in the country. This bill aims to correct this discrepancy and allow California customers the ability to address real needs in a difficult economic time."

Representatives of the payday lending industry, the California Financial Service Providers' Association and the Community Financial Services Association support the bill, writing:

Quite simply, the current payday advance limit is outdated; it was put into effect nearly 16 years ago when short-term loans were established in California. As you know, California is one of the most costly states in which to live, and yet the state has one of the lowest advance limits in the nation. The \$300 limit does not always meet the needs of families who have run out of financial resources, especially in these tough economic times.

— Supporter California Hispanic Chambers of Commerce writes that a payday loan is a "convenient, short-term financial option [that] provides a fix for families faced with the prospect of bouncing checks, shutting off utilities or worse, skimping on basic needs such as medical emergencies."

AB 1158 (Calderon)
Page 5 of ?

2. Increasing the maximum value of a payday loan check from \$300 to \$500

Existing law provides that a payday loan check cannot have a face value of more than \$300. This bill would increase that amount to \$500. These amounts include the fee that payday lenders may impose. In the case of a payday loan check for \$300, that fee is \$45. In the case of a \$500 payday loan check, that fee is \$75. This increase was included in the DOC report as a policy option (not recommendation), and was based on the premise that payday loans will continue to be available to help Californians meet short-term emergency cash needs, but that longer-term installment products will be available for those

consumers unable to pay back the full amount of their payday loans on their due dates.

The author and industry supporters argue that California's loan limit of \$300 should be increased to \$500 because the current limit is insufficient to meet the emergency cash needs of payday loan customers, has not been adjusted since it was implemented 15 years ago, and is out of line with the limits in other states. Despite those contentions, any increase in the loan limit must be evaluated not in terms of years since the last increase, but, instead, on the collateral effects of that increase on struggling consumers and whether any increase makes it even harder for them to pay off their debt. Previous concerns about the risks posed by payday loans are reflected in the Legislature's decision to place a cap on loan amounts.

a. Whether current limit is sufficient to meet borrower's needs

With respect to whether or not the current limit is sufficient to meet borrower's needs, DOC attempted to evaluate unmet demand due to loan limits by focusing on the number of customers who obtained more than one loan at the same time from different licensees. The sample survey, which analyzed transactions of 72.2% of California's payday loan customers, found that just 2.4% of the total customers in the sample obtained more than one loan at the same time from different licensees. DOC concluded that for this 2.4% of borrowers, "the loan amount was not sufficient to meet [their] emergency credit needs. This may be due to the loan limit being too low or the licensees not willing to lend the amount needed by the borrower."

AB 1158 (Calderon)
Page 6 of ?

When the AMPG survey asked borrowers whether the amount they had borrowed was the amount needed, over 60% of respondents indicated that the amount they borrowed was what they needed when reporting the minimum amount borrowed (79%) and the maximum amount borrowed (63%). Opponent Center for Responsible Lending (CRL) argues these findings demonstrate that most payday loan borrowers are satisfied with the amount they received and that borrowers do not need more than the law currently allows.

_____ Interestingly, as noted in the Background, the average dollar amount of payday loans has actually decreased over the last several years, also suggesting that payday loan customers actually do not need additional funds.

From a policy standpoint, the cap on payday loans represents a decision by the Legislature that the product should only be used for a short term loan of no more than \$300 (arguably due to the risks involved in higher loan amounts). If, in fact, the intent in enacting the CDDTL was to provide consumers with sufficient funds to meet all emergency credit needs, there would be no cap on the amount of the loan. Accordingly, the policy choice represented by this bill is not whether the current payday loan amount is sufficient to satisfy all short-term credit needs, but whether the increase would exacerbate the recognized risks associated with payday loans. Opponent consumer groups, labor, and community organizations argue that this bill would in fact aggravate the risk to struggling consumers. (See Comment 2(b).)

b. Effect of increasing loan limit to \$500

As noted above, the AMPG study indicated that "Although most borrowers report turning to payday lenders as a one-time solution to an immediate financial need, most report that the establishment of a payday loan account opens the door to a repetitive cycle of borrowing that is difficult if not impossible to end."

Payday lending has even been called a "business model that

encourages chronic borrowing." (Michael Stegman, "Payday Lending: A Business Model that Encourages Chronic Borrowing," Economic Development Quarterly, Vol. 17 No. 1, February 2003.) Because borrowers often cannot repay a loan and meet other expenses, they must pay off their current loan with their paycheck and then very soon afterwards, sometimes immediately,

AB 1158 (Calderon)
Page 7 of ?

take out another loan. The California Budget Project notes, "Yl]less than 4 percent of payday loans went to Californians who took out just a single loan during the entire year. More than 170,000 Californians took out 13 or more payday loans. Nearly half (48 percent) of payday loan borrowers in California take out payday loans at least once per month. . . ."

As a result, the public policy question raised by this bill is whether increasing the loan limit to \$500 will harm payday loan consumers by ensuring that they are caught in a repetitive cycle and by making it even more difficult for them to pay off their debt. A borrower who has a hard time paying off a \$300 loan within two weeks is very likely to be unable to repay a \$500 loan within that timeframe.

In a joint opposition letter, 35 consumer, labor, and community organizations write that "the high cost of payday loans, together with the short two-week repayment term, virtually ensures that cash-strapped borrowers will not be able to meet their basic expenses and pay off their loan at their next payday. . . . Borrowers get caught in a cycle of debt, leaving them worse off. It costs a typical borrower \$570 to pay back a single \$255 loan; with a larger loan, the same borrower would typically pay at least \$950 for a \$425 loan."

The California Budget Project argues that the bill would have a disproportionate impact on low-income women of color, writing:

A 2007 survey of payday loan borrowers conducted for the DOC revealed that well over half (59.8 percent) of borrowers in California are women and three-quarters of borrowers (74.1 percent) have annual household incomes under \$50,000. The survey also showed that disproportionate shares of payday loan borrowers are black or Latino.

According to CRL, a study recently released by the group found that 76% of borrowers, after repaying one payday loan, must take out another loan before their next paycheck. The study, entitled "Phantom Demand: Short-term Due Date Generates Need for Repeat Payday Loans, Accounting for 76% of Total Volume," found that half of all new loans are opened at the borrower's first opportunity (immediately or after a 24-hour or more waiting period where required). The study, which was largely based on data from Florida and Oklahoma-both states with a

AB 1158 (Calderon)
Page 8 of ?

\$500 loan limit-also found that 87% of new loans are opened within two weeks, or generally before the next payday, and only six percent of subsequent payday loans are taken out longer than a month after the previous loan was paid off. CRL notes:

This rapid, widespread re-borrowing indicates that most payday borrowers are not able to both repay one of these loans and clear a monthly billing cycle before having to borrow again. In essence, the bulk of payday loan demand comes from borrowers who are taking out a payday loan to

repay a payday loan.

The City and County of San Francisco opposes the measure, writing that "Yijn response to the proliferation of payday lenders in San Francisco . . . San Francisco acknowledged the need for short-term loans without predatory lending rates. It established Payday Plus SF, a micro-lending program with six local credits. San Francisco has demonstrated that better alternatives to usurious payday lending rats are available and therefore AB 1158 is unnecessary."

Increasing the payday loan limit from \$300 to \$500 also has the effect of significantly increasing the fee imposed on borrowers. Current law limits the face amount of a payday loan check to \$300 and the maximum fee to 15% of the face amount. As a result, under existing law, the maximum fee imposed is \$45. Under this bill, increasing the payday loan limit to \$500 would result in a maximum fee of \$75. Assuming a lender would charge, and a borrower would take, the maximum amount, that fee is 67% higher than allowable under current law. With respect to the fee, Community Housing Works writes:

Last November, after a landslide vote, Montana joined 15 other states and the District of Columbia in placing double-digit limits on the annual interest that payday lenders can charge. With shrinking profits in other states, payday lenders are trying to preserve their profit margins on the backs of struggling Californians, by seeking to increase the allowable loan amount from \$300 to \$500.

Opponents also note that while California has one of the lower limits on the amount of a payday loan, other states that have higher loan limits also have restrictions on the number of loans that may be taken out.

AB 1158 (Calderon)
Page 9 of ?

Given the concerns expressed above, DOES this bill's increase of the loan limit to \$500 ensure that payday loan consumers are caught in a repetitive cycle of re-borrowing which may be difficult if not impossible to end?

c. Amendments to address above concerns

The opposition suggests amendments to address its concerns, writing:

The fact that families are struggling to make ends meet does not justify gouging these families with 459% interest on two-week loans that leave families trapped in a cycle of repeat borrowing. AB 1158 is not about whether to preserve or eliminate payday lending; it is about whether we are going to expand an already risky and dangerous product, or whether we are going to do something to better protect California families in need. The current version of AB 1158 would expand payday lending and exacerbate the dangers. Instead, we recommend that AB 1158 be amended in ways that would truly help struggling families. _

Those suggested amendments do the following:

adopt the FDIC's six-loans per household annual loan limit in an effort to "Ymjake sure that extremely high cost payday loans are addressing short-term emergencies, rather than longer term debt;"

extend the minimum loan term to 31 days. This amendment is based on a DOC policy option that would "Yg]ive families more time to repay a payday loan without the need to borrow again;" and

adopt a requirement that lenders evaluate each borrower's ability to repay, modeled on underwriting provisions contained in the Pilot Program for Affordable

Credit-Building described in Comment 2. This amendment is intended to ensure that borrowers can repay the loan.

Should the Committee desire to pass this measure, the Committee should consider the above amendments, or similar alternatives, in order to better regulate and control high-cost payday loans so that working families are protected.

GIVEN THE CONCERNS RAISED ABOVE REGARDING THE IMPACT OF

AB 1158 (Calderon)
Page 10 of ?

INCREASING THE PAYDAY LOAN LIMIT FROM \$300 TO \$500, SHOULD THE BILL BE AMENDED TO PROVIDE BETTER CONSUMER PROTECTIONS TO HELP STRUGGLING FAMILIES?

3. Is there an alternative? Recent legislative and private-sector efforts aim to help provide a market for reasonably priced small dollar loans

Proponents of payday lending argue that many borrowers have no alternative but to take out a payday loan. According to the Community Financial Services Association of America (CFSA), an association of payday lending companies, other options are too costly when compared with the fee for one payday loan. For example, borrowers may be charged late fees on credit cards or a non-sufficient funds fee if they bounce a check. Late payments on utility bills also may be costly to the consumer, particularly if they involve a reconnection fee.

As described below, however, new and emerging credit solutions are entering the marketplace both through legislative and private sector efforts. Many of these are directly focused on creating an alternative to high-cost payday loans.

SB 1146 (Pilot Program for Affordable Credit-Building) As noted in the DOC report, small, unsecured installment loans

entities licensed under the California Finance

Lenders Law (CFL). DOC notes that the rates and fees on these loans are limited, however, to an APR of about 30%, compared to the average APR of 429% for a payday loan. According to DOC, "This by itself is a strong inducement to make small, unsecured loans under the payday loan law as opposed to the CFL." may be made by

In an effort to address this lack of incentive to make small dollar loans under the CFL, last year, the Legislature passed and the Governor signed SB 1146 (Florez, Ch. 640, Stats. 2010) which created the Pilot Program for Affordable Credit-Building. That program is an effort to "increase the availability of affordable credit-building opportunities to underbanked individuals seeking low-dollar-value loans and to help those individuals move into the financial mainstream." (Fin. Code Sec. 22348.)

The pilot program, which sunsets January 1, 2015, is intended to provide a less costly alternative to payday loans by creating a market for reasonably priced small loans and, at

AB 1158 (Calderon)
Page 11 of ?

the same time, help loan recipients build credit. Under the program, participating lenders may charge a higher interest rate and fees than under the current CFL. In March 2011, DOC issued regulations implementing the program which contains the following components:

the loan has a minimum principal amount upon origination

of \$250 and is not more than \$2,500, as specified;
the interest rate of each loan is capped at 30% for the unpaid balance of the loan up to and including \$1,000 and 26% for the unpaid balance of the loan in excess of \$1,000;

origination fees are capped at 5% of the principal amount of the loan or \$65, whichever is less. Licensees are prohibited from charging the same borrower more than one origination fee in any six-month period;

the term of the loan is: (1) 90 days for loans whose principal balance upon origination is less than \$500, (2) 120 days for loans whose principal balance upon origination is at least \$500, but is less than \$1,500; and, (3) 180 days for loans whose principal balance upon origination is at least \$1,500;

licensees must report each borrower's payment performance to at least one of the three major credit bureaus; and,

a licensee must underwrite each loan and may not make a loan if it determines that the borrower's total monthly debt service payments exceed 50% of the borrower's gross monthly income. In underwriting the loan, the licensee must assess the borrower's willingness and ability to repay and must validate a borrower's outstanding debt obligations, as specified.

The pilot program created by SB 1146 contains two critical elements that are not a part of the payday loan product. First, the program requires licensees to report borrowers to at least one of the three major credit bureaus, unlike payday loans which are not reported. The intent of this requirement is to help those borrowers who do not have a credit history to establish one, and to help those borrowers who do have a credit history to improve their credit scores. Second, unlike payday loans, the program requires licensees to underwrite the loan and ensure that the loan is affordable to the borrower. In order to avoid the possibility of lax underwriting, this provision was intended to ensure that the loans offered under the Pilot Program are both affordable and responsible.

AB 1158 (Calderon)
Page 12 of ?

While the Pilot Program for Affordable Credit-Building is just getting underway, it represents an attractive affordable alternative to costly payday loans for many Californians. In fact, for some people, it could arguably reduce some of the need for a short-term high-cost payday loan. Those same individuals could instead apply for a more responsible longer-term loan for \$250 (or any amount up to \$2,500) under the program.

DOES THE RECENT PASSAGE OF THE PILOT PROGRAM FOR AFFORDABLE CREDIT BUILDING REDUCE THE NEED FOR SHORT-TERM COSTLY PAYDAY LOANS?

SHOULD THE LEGISLATURE WAIT TO EVALUATE THE PILOT PROGRAM AND GIVE IT TIME TO WORK BEFORE INCREASING THE PAYDAY LOAN LIMIT, ESPECIALLY GIVEN THE SIGNIFICANT CONCERNS ASSOCIATED WITH THAT INCREASE, AS DESCRIBED ABOVE?

Bank and credit union alternatives With respect to other alternatives to payday loans, the DOC report also states that consumers "who do not have access to traditional sources of credit (credit cards, home equity lines of credit, etc.) do have alternatives to payday loans," noting that many banks and credit unions have cash advance programs that provide borrowers with cash that must be repaid generally within 35 days. For example, the Center for Responsible Lending writes about "SF Payday Plus, a collection of San Francisco credit unions offering loans with interest rates of no more than 18% APR. Many other California credit unions also offer small-dollar loans and accounts that include savings components. Because all payday borrowers must have a bank account, and the vast majority of credit unions have eased

membership restrictions that were once the norm, many Californians could become credit union members and take advantage of their responsible lending products."

Employer-based services In 2010, Emerge Workplace Solutions began offering loans to employees using a workplace-based approach. The company, whose goal "is to provide better borrowing choices for working people and end predatory lending practices," describes its loans (which require underwriting and are usually approved within one to two business days) as follows:

Emerge loans are offered by FDIC community banks and federally

AB 1158 (Calderon)
Page 13 of ?

regulated credit unions that offer fair interest rates (from 9.9 percent to a high of 19.9 percent APR) with 4-8 months to pay them back, and can build your credit if you repay on time. Also, it's easier to pay Emerge loans back because payments are automatically transferred to the financial institution via direct deposit.

Lending circles; peer-to-peer lending Also gaining popularity are "lending circles" in which participants pool their resources by making monthly contributions which are disbursed among the group at agreed-upon intervals. For example, Mission Asset Fund (MAF) in San Francisco has partnered with a local community development bank which holds the groups funds, tracks payments and reports the results to credit bureaus. As a result, unlike payday loans, participants are able to build credit. The program, which is just over a year old, is showing early signs of success:

An examination of the participants in the first two cestas over a period of six months shows, according to MAF, that credit scores rose on average by 47 points. More significantly, in Mr. Quiñonez's view, is that the same group showed an increase of 9 percent in the average number of "satisfactory" credit accounts held by members of the group. "Satisfactory" accounts are those where payments are being made on time. That nine-point gain demonstrates that participants are not only making their contributions on time, they are also improving their payment performance on other credit accounts. Quiñonez believes that MAF's approach to helping individuals join cestas, which includes a measure of financial education, is improving how they handle all their financial affairs. ("My lender, my friend: Lending circles with a Latino twist," Christian Science Monitor, January 30, 2010.)

Other alternatives Others argue that payday loan consumers also have other options ranging from borrowing money from friends or family, working out a payment plan with the creditor (e.g., credit card or utility company), getting an advance from an employer, obtaining emergency assistance from faith-based or community organizations, delaying purchases or obtaining a small consumer loan, or using a bill payment service such as BillFloat to pay a bill. According to the company, BillFloat "extend[s] your bill by up to 30 days, helping protect your credit while avoiding late fees, overdraft charges and expensive loans."

AB 1158 (Calderon)
Page 14 of ?

FDIC Small-Dollar Loan Pilot Program - a model for affordable small loans In addition, in February 2008 the Federal Deposit Insurance Corporation (FDIC) began a two-year nationwide

"Small-Dollar Loan Pilot Program" under which participating banks offered loans of up to \$1,000; payment periods beyond a single paycheck cycle; APRs below 36%; low or no origination fees; streamlined underwriting criteria; and access to financial education. In many instances, the banks indicated that loans could be processed in less than an hour. The FDIC indicated that the pilot, which ended at the end of 2009, was a success and noted that "most pilot bankers indicated that small dollar loans were a useful business strategy for developing or retaining long-term relationships with consumers. . . . The most prominent product elements bankers linked to the success of their program were longer loan terms, followed by streamlined but solid underwriting." The participating banks-with total assets ranging from \$28 million to nearly \$10 billion-demonstrated that it can be profitable to offer affordable small-dollar loans as an alternative to costly products such as payday loans.

Given the above arguably less expensive alternatives to a payday loan, the Committee should consider whether this bill's provision increasing the maximum value of a payday loan check from \$300 to \$500 as discussed above would, in fact, aid consumers struggling in the present economy or instead contribute to a cycle of debt.

GIVEN THE ARGUABLY LESS COSTLY ALTERNATIVES TO A PAYDAY LOAN, WOULD THIS BILL'S INCREASE OF THE LOAN LIMIT TO \$500 IN FACT AID CONSUMERS OR WOULD IT FURTHER EXACERBATE A CYCLE OF DEBT, AS DISCUSSED ABOVE?

4. DOC report: policy options

As noted in the Background, the December 2007 DOC report was based upon a survey of payday lenders and DOC's annual report for 2005-06. That report included 22 recommendations, divided into those intended to improve DOC's oversight of the industry and those intended to strengthen its enforcement of the CDDTL.

In addition, DOC included a number of policy options for consideration. DOC noted that its policy options were "based on the premise that the payday loan will be available to meet the short-term emergency case needs of the consumers, while allowing

AB 1158 (Calderon)
Page 15 of ?

for a longer-term installment product for those consumers that are not able to pay back the full amount of the payday loan on the due date and have sufficient funds remaining to pay their normal living expenses." The author notes that one of the policy options suggested by DOC for further consideration was an increase in the amount of the payday loan limit from \$300 "to another amount such as \$500 or \$750."

In addition to this policy option, DOC also suggested the following for further consideration:

- extend the term of a payday loan to 31 days (staff notes that opponents to this bill suggest an amendment to the bill that would implement this policy option);
- prohibit a licensee from entering into a payday loan with a borrower while that borrower had another payday loan outstanding from any other licensee;
- make the payday loan origination fee a flat fee rather than a percentage;
- base the fees for payday loans on the loan amount on a sliding scale;
- restrict a borrower from having a payday loan outstanding for more than three months in the previous 12 months;
- require a payment plan with a minimum of six equal monthly installments; and
- implement a database to track transactions

Support : California Financial Service Providers' Association; California Hispanic Chambers of Commerce; Community Financial Services Association

Opposition : AARP California; African American Network of Kern County; Alliance of Californians for Community Empowerment; Black Economic Council; California Association for Micro Enterprise Opportunity; California Budget Project; California Labor Federation - AFL/CIO; California Reinvestment Coalition; California Rural Legal Assistance Foundation; California Teamsters Public Affairs Council; Catholic Charities of California United; Center for Responsible Lending; City of San Diego; City and County of San Francisco; Coalition for Quality Credit Counseling; Community HousingWorks; Community Legal Services, East Palo Alto; Consumers Union; Council of Mexican Federations; Dolores Huerta Foundation; East Los Angeles Community Corporation; Greenlining Institute; Insight Center; JERICHO; Honorable Jose Cisneros, Treasurer, City and County of San Francisco; Korean Churches for Community Development; Latino

AB 1158 (Calderon)
Page 16 of ?

Congreso; Los Angeles Metropolitan Churches; LULAC - CA Council 3120; National American Indian Veterans Inc.; National Asian American Coalition; National Council of La Raza - CA; New America Foundation; Opportunity Fund Northern California; Public Interest Law Firm; Santa Clara County Board of Supervisors; Silicon Valley Community Foundation; The Americas Group; Ubuntu Green; United Way of California; Western Center on Law and Poverty

HISTORY

Source : Author

Related Pending Legislation : SB 365 (Lowenthal) would clarify that a payday lender may not issue a payday loan to a customer if the customer already has a loan outstanding with any other licensee. The bill would also provide Legislative intent to enact legislation that would authorize the Commissioner of Corporations to contract with a third-party provider for the implementation of a common database to aid in the enforcement of the CDDTL. This bill is in the Senate Banking and Financial Institutions Committee.

Prior Legislation :

SB 1146 (Florez, Ch. 640, Stats. 2010). See Comment 2.

AB 377 (Mendoza, 2009). See Background.

AB 7 (Lieu, Ch. 358, Stats. 2007) authorized DOC to enforce, under the CDDTL, federal protections related to payday loans for members of the military and their dependents.

SB 898 (Perata, Ch. 777, Stats. 2002) enacted the Deferred Deposit Transaction Law and shifted authority for its administration to the Department of Corporations.

SB 1959 (Calderon, Ch. 682, Stats. 1996) expressly authorized payday lending in California and gave regulatory authority to the Department of Justice.

Prior Vote :

Senate Banking and Financial Institutions Committee (Ayes 5,
Noes 0)
Assembly Floor (Ayes 49, Noes 16)

AB 1158 (Calderon)
Page 17 of ?

Assembly Appropriations Committee (Ayes 11, Noes 1)

Assembly Banking and Finance Committee (Ayes 7, Noes 1)
