Louisiana
Credit Union League

Via electronic filing

October 5, 2016

Ms. Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street
Washington, DC 20552

Re: CFPB Small Dollar Lending Proposal

Dear Ms. Jackson:

On behalf of the Board and member credit unions of the Louisiana Credit Union League (LCUL), representing over 1.2 million citizens, I would like to take this opportunity to comment in response to the CFPB's Small Dollar Lending Proposal. Although intended by the CFPB as a proposal designed to end payday debt traps by requiring lenders to take additional steps to ensure that borrowers have the ability to repay their loans, this proposal goes much further by imposing significant costly restrictions and limitations that unfortunately and perhaps unintentionally will have a detrimental effect on the ability of responsible credit unions to make small-dollar loans to the very people who need them most. For this reason and those discussed below, LCUL strongly urges the CFPB to reconsider and withdraw this proposal in its current form.

Proposal Fails to Distinguish Responsible Regulated Lenders by Imposing A One-Size Fits-All Regulatory Standard

While we can appreciate the CFPB's noble intentions to end abusive and unfair practices that have been often associated with small-dollar or "payday" lending, we are concerned that this proposal will ultimately force responsible and government-regulated lenders like credit unions to stop making these type of loans. As in other CFPB-proposed and implemented regulation over the years since the CFPB's formation, there is a lack of distinction between credit unions and non-traditional lenders who have been historically associated with questionable lending practices in the small-dollar market. This proposal lumps all lenders together in a "one-size-fits-all" complex regulatory scheme.

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Such an approach is ill-advised in our view and will result in unnecessary increases in compliance costs and the imposition of additional regulatory hurdles that will do very little to curb the behavior the CFPB is trying to thwart. Indeed, LCUL is convinced that most responsible lenders (who are already operating on very tight margins) will be forced to make a business decision as to whether the additional compliance costs and regulatory scrutiny justify making small-dollar loans. For a state like Louisiana, with a significant underserved population that has seen more than its fair share of natural and manmade disasters since 2005, the exit of credit unions from the small dollar market will be devastating and will only exacerbate further the very issues the CFPB purports that it is trying to eliminate. Ultimately, this proposal will force the good guys out of the market, leaving borrowers with less choice and undesirable costly options for their short-term cash needs.

For that reason, government-regulated lenders with a proven track record of responsible lending practices should be exempted entirely from this proposed rule.

Proposal is Overly Complex

Coming in at over 1,300 pages long and almost 18,000 words this proposed rule is more than three times the length of the United States Constitution. Riddled with a multitude of nuances, exemptions, exceptions, exceptions to exemptions and numerous disconnects, the compliance burdens of cost and time expended to comply with this regulation will be too great to bear on credit unions with already narrow margins. Without question, abusive and deceptive practices in the small dollar loan marketplace are much too commonplace and clearly should be addressed. We do not understand why the CFPB doesn't choose to directly target the bad actors in the payday loan arena, while exempting the not-for-profit credit union industry as a whole, and thereby acknowledging the over 80 years of consumer-friendly service that credit unions have provided.

In addition, the complexity of this proposed rule, combined with its overly prescriptive approach, will negatively impact the very borrowers it is intended to protect by forcing them to turn to less-regulated lenders who may not fully adhere to responsible lending practices or remove the small dollar options they prefer altogether.

Implementation of Full-Payment Test Places Undue Burden on Responsible Lenders

Implementing the "full-payment" test will be a challenge for credit unions who currently make loans covered under this proposal. Although credit unions already consider a borrower's ability to repay (and rightly so) whenever making a loan decision, the specific provisions in the proposal dictating how lenders would be required to do so going forward will unquestionably present significant extra hurdles in the underwriting process for loans that, for the most part, will be less than $1000.

As we interpret the proposal, lenders would be required to make a reasonable determination that the borrower's "residual income" will be sufficient to repay the loan and meet basic living expenses for the borrower and the borrower's dependents during

the shorter term of the loan or for 45 days after the loan is paid. In addition to determining the ability to repay within the shorter of the life of the short-term loan or 45 days, the lender must reasonably conclude that the borrower will be able to repay the loan, make any payments due on major financial obligations, and meet basic living expenses for 30 days after making the highest payment due on the loan. Although the proposal does allow the lender to rely to some degree on the representations made by the borrower, the lender must still verify the applicant's income (after taxes), borrowing history, and payments for "major financial obligations."

The proposal also limits short-term loan extensions and renewals and encourages various cooling off periods before borrowers may obtain new covered loans.

We do note that the proposal does provide an exemption to the "full payment test" where lenders could in certain circumstances make a loan using the "principal payoff option." As we understand it, this would essentially permit lenders to make loans up to $500 without performing the full-payment test as long as the loan is structured in such a way as to keep the borrower from getting trapped in debt. If the borrower cannot pay off the original loan or returns to re-borrow within 30 days, the lender is not permitted to offer more than two extensions on the original loan and only if the borrower repays at least one-third of the principal at the time of the extension. However, this option is limited in that it can only be offered to a borrower who has not been in debt on short-term loans lasting longer than 90 days in the preceding year. This seems like a lot of hoops for a lender to jump through in order to use an exemption on a $499 loan.

A practical analysis of the expenses to initiating this type of loan includes cost of pulling a credit report and staff salaries to take the application and underwrite the loan. In addition, the tracking and calculation process that is needed to comply with this regulation does not already exist within most credit union core processors, and any cost to update systems into compliance will be passed along directly to credit unions, with additional expenses for staff training, legal advice, and document/disclosures. Included in the cost of compliance is the lost revenue and business opportunities that occurs during the implementation for compliance. We add this information to our comment letter to illustrate some of the touchpoints a credit union's volunteer board of directors and management will consider when they decide whether to offer small dollar loans in the future.

We must mention that the ability to repay also extends to long-term credit options as well, although there are additional requirements for long-term credit that are somewhat different than what is required of short-term credit. While the verification rules for long-term credit seem nearly identical to short-term credit, lenders will most likely have to separately review and implement long-term credit verification rules because the proposal does not appear to have added a consolidated set of standards for long-term credit.

For long-term credit, the lender must determine if the borrower's residual income will permit the borrower to repay the loan and meet basic living expenses. This determination must be made within 180 days before any advance under a line of credit.

As with short-term credit, the proposal does extend two conditional exemptions for long-term credit through the use of two alternative loan products. The first would be for lenders to offer loans that meet the parameters of the NCUA payday alternative loan (PAL) program. The second alternative would be to offer loans that meet three conditions:

1. term is less than two years with roughly equal payments;
2. total cost of the loan is 36% or less excluding a reasonable origination fee;
3. annual default rate on all such loans cannot exceed 5%.

A lender is also limited in how many loans it can make under the second alternative.

On its face the implementation of "full-payment" test may appear to be reasonable. However, the level of detail and specificity in the small-dollar loan space that this proposal requires seem overly burdensome when lenders are under pressure to quickly provide loan decisions to borrowers who have an immediate need for cash.

That said, credit unions have been making small loans to their members for years by using solid underwriting practices and good common sense, while maintaining low delinquency and default ratios. Credit unions also devote a significant portion of their resources to educating their members and to providing free financial counseling. Credit unions have a proven record of knowing their members and doing a solid analysis of these members' ability to repay loans, as evidenced by the credit union industry's history of low delinquency and default rates.

While there is an obvious level of risk associated with these types of loans that the lender must clearly take into account, loans of this nature can be done in a way that is not punitive to the borrower or the lender without implementing costly regulatory hurdles that will likely curtail, if not end, the willingness of most responsible lenders to engage in small dollar lending.

Rule Creates Undue Safety and Soundness Issues by Substantially Limiting the Collection Efforts of Lenders Actively Engaged in Small Dollar Lending

The proposed rule would limit lender-initiated "payment transfers" which includes many methods of presentment such as electronic fund transfers, paper checks, payment orders and intra-institution fund transfers. Under the rule the lender may not initiate payment transfers from a borrower's account after two consecutive payment transfer attempts have failed due to insufficient funds in the borrower's account. While the lender may obtain reauthorization from the borrower for additional transfer attempts, they must be signed or agreed to by the borrower in writing or electronically or by phone if the lender records the call and sends a written memo to the borrower before initiating the re-authorized transfer. The authorization must specifically provide when the transfer will be made, what amount will be transferred, and how it will be transferred. The lender can only re-present a reauthorized transfer only once if the first presentment fails. Additional

disclosures are required when the lender only collects late fees with the reauthorized transfer.

Credit union loans are often paid through the transfer of funds from a credit union deposit account, and a credit union would not make multiple attempts to collect from an account that does not contain sufficient funds, nor would a credit union charge multiple overdraft fees for failed loan payment transfers. The payment provisions should not apply when payments are coming from an account that exists with the same loan holder

The proposal also requires disclosures regarding payment transfer attempts, both before any transfers are attempted and after the second transfer fails. All of these disclosures must be in writing unless the borrower agrees to accept them electronically. Pre-written transfer disclosures must be provided 6-10 business days prior to initiating the transfer. Shorter time frames of 3–7 days apply to electronic and in-person notices. LCUL is concerned that this lead time on disclosures may significantly impact lenders since the timeframe will be extended by re-noticing a second transfer after the first fails, and will introduce the need for a complicated notice tracking system. The rule includes model disclosure forms recommended and drafted by CFPB.

In addition, a consumer rights notice must be provided after two consecutive failed payment transfers within three business days of the second failed attempt. The CFPB should consider a) the expense of generating these notices, b) the expense of delivering these notices, c) the inclination of the average consumer to ignore well-intentioned notices, d) the existence of periodic statements that credit unions already provide to their members and the consumer protections available to members surrounding these statements, and e) the existence of account agreements that already govern many of the "problems" this proposal is attempting to address.

While all responsible lenders can appreciate that borrowers need to be fully aware of the terms of any loan they are taking and that borrowers have the ability to repay the loan, there should also be an equal expectation that borrowers clearly understand that they actually must repay the loan once they enter into a contract.

In the end, as is often the case with well-intentioned proposals from the CFPB, it is the consumer who stands the most to lose. Lenders with proven track records in responsible lending will simply see no legitimate business reason to continue offering small-dollar loan products in such a highly-regulated and burdensome environment. That said, payday loans will continue to proliferate because there is clearly a demand for this type of loan. These borrowers would be better served by a regulatory scheme that kept responsible lenders in the game. Unfortunately, most credit unions and other regulated lenders will abandon these types of loans rather than deal with the additional compliance costs and heightened regulatory scrutiny. As a point of reference, the CFPB would benefit from a post-compliance study of how many credit unions discontinued offering, or limited international wire transfers after the CFPB implemented the International Fund Transfer regulations in 2014. Financial institutions have been forced to do a risk vs. reward analysis of services and products over the past 5 years to survive in the overly-

regulated landscape, and there has been much unevaluated "collateral damage" done to the consumer after credit unions discontinue or limit their offerings

In closing, we would strongly recommend that the CFPB withdraw this proposal in its entirety or at a minimum exempt those lenders with a proven track record of responsible lending. Credit unions making small dollar loans to the very members who need them most should not be lumped into a "one-size-fits-all" regulation just because there are irresponsible unregulated lenders operating in this market space who often utilize abusive practices. A better approach would be to distinguish the responsible lenders from the irresponsible lenders. To apply this regulation across the board to all lenders regardless of their lending history can be compared to the analogy of giving every motorist on the freeway a ticket because two or three are speeding.

If the goal of the CFPB for consumers is to shorten and simplify documents and disclosures, the same duty of care should be applied to the proposal and consideration of new regulation. In particular, the CFPB should steer clear of "global" regulatory changes that do not differentiate credit unions from other types of financial institutions.

Again, thank you for the opportunity to comment on this important matter.

Sincerely,

Anne M Cochran
President/CEO