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Contact: Maria Cilenti - Director of Legislative Affairs - mcilenti@nycbar.org - (212) 382-6655

**REPORT ON LEGISLATION BY THE
CONSUMER AFFAIRS AND CIVIL COURT COMMITTEES**

**A.7047
S.3841**

**M. of A. Heastie
Senator Farley**

AN ACT to amend the banking law, in relation to enacting the “short-term financial services loan act.”

THIS LEGISLATION IS OPPOSED

The Civil Court and Consumer Affairs Committees submit these comments in opposition to Bill A.7047/S.3841, the “Short-term Financial Services Loan Act.” This bill would allow check cashing establishments to make small loans of between \$300 and \$2,000 to consumers. The stated purpose of the bill is to “[address] the unfulfilled need of New Yorkers for an affordable, small-dollar, short-term credit product.” The Committee, however, believes that the type of loan this bill allows would prove to be unaffordable, as demonstrated by the track record of similar products in other states. We believe that the bill creates a huge and unwarranted loophole in New York’s longstanding 25% usury cap for consumer credit transactions, and that if passed, it will be detrimental to the citizens of our state.

Highlights of the Bill

Some highlights of the proposed legislation are:

1. The bill eliminates the prohibition in the Banking Law against check cashers making loans, and affirmatively permits licensed check cashers to offer small, short-term loans. Loans may be given between \$300 and \$2,000, for a term of between 90 and 180 days.
2. The amount of a loan may not be more than 25% of a borrower’s gross monthly income. Upon completion of all scheduled payments, a borrower may enter into a new loan agreement, and a borrower may re-finance a short-term loan once prior to the maturity of a loan, if the borrower has made three consecutive timely payments. If a borrower has re-financed a short-term loan, the borrower shall not be eligible to borrow from the same or any other licensed check casher until the loan is fully repaid. So that check cashers can monitor this restriction, the bill establishes a database, to be funded through licensing fees, to allow a licensee to determine whether an applicant has any other short-term loan outstanding.

3. The bill specifically exempts short-term loans made by check cashers from the existing New York usury law that places a 25% cap on such loans.¹ The Banking Superintendent would by regulation establish the maximum interest rate and fees including such charges as loan origination, monthly maintenance and late fees. In establishing such interest rates and fees, the Superintendent is directed to consider factors including the rates and fees charged by lenders in other states for similar products, and a reasonable profit for check cashers from offering and providing short-term loans.

4. The legislation provides for creation of a financial education fund to be funded through assessments of licensed check cashers and to be administered by the Banking Superintendent in consultation with the check cashing industry.

Discussion

As noted above, the longstanding usury law in New York places a maximum interest rate of 25% on loans to consumers including the short-term loans that are encompassed in this bill. The relevant inquiry is whether the justifications put forth for carving out this exception, taken together with the consumer protections claimed by the bill's proponents, pass muster.

The available information on the cost of these loans provides no assurance that they will be reasonably priced. In fact, the data from similar products in other states compels the conclusion that these short-term loans will carry triple-digit interest rates and significant transaction fees. A number of studies have examined the costs of payday loans, which if not identical, are quite similar to the short-term loans that will be offered by check cashers in this bill. The Consumer Federation of America found that payday loans at check cashing establishments had an average annual percentage rate of more than 400%.² The National Consumer Law Center reported that the interest rate for payday loans typically ranges from 300% to 500%.³ Data collected by various state agencies shows interest rates for payday loans that are routinely in triple digits.⁴

The bill, which gives unprecedented authority to the Banking Department to set the rates and fees, practically guarantees that the high costs associated with payday loans in other states will cross state lines into New York. This is because, as noted, the Banking Department must consider the rates and fees charged in other states for similar products.

The summary accompanying the bill states that there will be "strict limits" on licensed check cashers to "only lend money to qualified borrowers based on income and ability to pay back such loans." Upon a close examination of the legislation, however, those limits are not so strict. For instance, the only provision arguably related to ability to pay is that the loan amount

¹ General Obligations Law §5-501, Banking Law §14-a, Penal Law §§190.40.

² Jean Ann Fox and Patrick Woodall, Consumer Federation of America, *Cashed Out: Consumers Pay Steep Premium to 'Bank' at Check Cashing Outlets*, November 2006, at 2, available at http://consumerfed.org/elements/www.consumerfed.org/file/finance/CFA_2006_Check_Cashing_Study111506.pdf.

³ National Consumer Law Center, *The Cost of Credit*, 4th ed. (2009), at 342.

⁴ *Id.*

cannot be more than 25% of the borrower's gross monthly income. One obvious question then follows-- what if a borrower has other debts? This provision does not require a check casher to make a true analysis of a borrower's ability to repay. We are mindful that one of the characteristics of predatory consumer lending is that lenders make loan decisions based not on ability to repay, but on expected interest payments and fees.⁵

The bill contains other provisions aimed at protecting consumers, including a prohibition on a borrower re-financing a loan more than once, and a requirement that a licensed check casher verify through use of the statewide database that an applicant has no other outstanding loan before approving a loan. We question the efficacy of such protections, and note that in other states they have been employed largely to make high cost loans more palatable. Groups such as Consumers Union, the Consumer Federation of America, the National Consumer Law Center, and the Center for Responsible Lending, have all concluded that these safeguards fail to adequately protect consumers.⁶

The bill's proponents also point to the availability of short-term loans on the internet as an argument for allowing check cashing establishments to make such loans. That such loans are available does not make them fair or affordable. In some cases, in fact, they may be illegal, and the New York Attorney General has prosecuted out-of-state lenders who were marketing payday loans to New Yorkers.⁷ Moreover, even to the extent that short-term loans are available over the internet, this is a far cry from allowing licensed check cashers to make short-term loans from a physical storefront. We believe that the possible harm to New Yorkers will escalate if high-rate, high-fee loans are available on every block.

It is important that consumers have access to readily available sources of short-term credit. Consumer experts recognize that when traditional financial institutions pull back from providing such products, the options for persons with spotty or no credit history may lessen.⁸ In this connection we note that there are financial institutions including community credit unions that are increasingly succeeding in bringing affordable loan products to the public.⁹ The need for small-dollar loans in New York does not mean that extending to check cashing establishments the power to make loans is a way to responsibly meet that need.

⁵ Consumers Union, Consumer Federation of America, National Consumer Law Center, *Small Dollar Loan Products Scorecard--Updated*, May 2010, at 2 ("Small Loan Products Scorecard"), available at http://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/cu-small-dollar-scorecard-2010.pdf.

⁶ *Small Loan Products Scorecard*, at 3, citing Uriah King & Leslie Parrish, Center for Responsible Lending, *Springing the Debt Trap: Rate Caps Are Only Proven Payday Lending Reform*, December 2007, available at <http://www.responsiblelending.org/payday-lending/research-analysis/springing-the-debt-trap.pdf>.

⁷ See "Attorney General Cuomo Announces Distribution of \$5.2 Million Settlement in 'Rent-A-Bank' Payday Lending Scheme," Press Release, November, 17, 2009, available at http://www.ag.ny.gov/media_center/2009/nov/nov17a_09.html.

⁸ National Consumer Law Center, *The Cost of Credit*, 4th ed.(2009), at 342.

⁹ National Consumer Law Center, *Stopping the Payday Loan Trap: Alternatives That Work, Ones That Don't*, June 2010, at 19.

Conclusion

We believe that creating a carve-out in New York's longstanding 25% usury law for short-term loans by check cashing establishments would create a dangerous loophole that could easily be only the beginning of high-rate loan products in our state. Studies show that the most effective way of protecting consumers against abusive lending is through a cap on the interest rate.¹⁰ In the past few years several states that previously exempted short-term lenders from existing double-digit interest rate caps, have rolled back the exemption, and some that had no interest rate caps on short-term loans, have imposed them.¹¹ It would be a shame for New York to go in the opposite direction. New York has always been in the forefront for its protections against unfair short-term loan products, and it should maintain that position.

Thank you for the opportunity to comment on this legislation. Should you have any questions, please do not hesitate to contact us.

Respectfully submitted,

Annie Ugurlayan
Chair, Consumer Affairs Committee

Janet Ray Kalson
Chair, Civil Court Committee

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¹⁰ *Small Loan Products Scorecard*, at 3.

¹¹ See Uriah King and Leslie Parrish, Center for Responsible Lending, *Payday Loans, Inc.: Short on Credit, Long on Debt*, March 2011, at 12. For example, New Hampshire recently enacted a 36% rate cap on payday loans.