

# ICBA Summary of CFPB Potential Rulemakings for Payday, Vehicle Title, and Similar Loans

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## BACKGROUND AND SCOPE

On March 26, 2015, the Consumer Financial Protection Bureau (Bureau) released its Outline of the Proposals Under Consideration and Alternatives Considered (the Proposal) that would address the Bureau's concerns that: 1) consumers are taking out unaffordable loans and are therefore unable to breakout out of a cycle of dependency on these loans; and 2) certain lender practices to collect payment from consumers' account or paycheck may cause substantial harm. The Proposal covers several types of short- and longer-term consumer loans (covered loans).

### Covered Short -Term Consumer Loans

The following products with a term of 45 days or less:

- Payday loans
- Vehicle title loans
- Open-end lines of credit
- Deposit advance products

### Covered Longer-Term Consumer Loans

A term longer than 45 days and an all-in APR in excess of 36 percent and the lender holds:

- Access to repayment through a consumer's account or paycheck or
- A non-purchase security interest in the consumer's vehicle

The Bureau is not considering additional regulatory requirements on certain categories of loans, including credit card accounts, real-estate secured loans, and student loans under this Proposal.

Applicability to Community Banks  
The Proposal would apply to community banks and other lenders making any of the covered loans.

The Bureau is considering two different approaches to regulating covered loans – prevention and protection. Under the “Prevention Requirements,” lenders would have to determine at the outset that the consumer is not taking on unaffordable debt. Under the “Protection Requirements,” lenders would have to comply with various restrictions designed to ensure that consumers can affordably repay their debt. Lenders could choose on a loan-by-loan basis which set of requirements to follow.

Link to the Proposal: [http://files.consumerfinance.gov/f/201503\\_Bureau\\_outline-of-the-proposals-from-small-business-review-panel.pdf](http://files.consumerfinance.gov/f/201503_Bureau_outline-of-the-proposals-from-small-business-review-panel.pdf)

Link to the Bureau's summary of the Proposal: [http://files.consumerfinance.gov/f/201503\\_Bureau-proposal-under-consideration.pdf](http://files.consumerfinance.gov/f/201503_Bureau-proposal-under-consideration.pdf)

## PROPOSAL

### Covered Short-Term Loans

The Proposal defines short-term loans as credit requiring repayment in full within 45 days. Under the Proposal, lenders could offer short-term loans if they complied with certain *Prevention Requirements* or *Protection Requirements*. Specifically, under the Proposal, all lenders making covered short-term loans would be required to adhere to either the *Prevention Requirements* or the *Protection Requirements*, but not both.

#### Prevention Requirements

- This option would require lenders to make a good-faith, reasonable determination that the consumer can repay a loan when due – including interest, principal, and fees for add-on products – without defaulting or re-borrowing. For each loan, lenders would have to verify the consumer’s:
  - Income using bank statements, benefit statements or paystubs;
  - Major financial obligations that are significant in their amount and that cannot be readily eliminated or reduced in the short term;<sup>1</sup> **AND**
  - Borrowing history to determine whether the consumer has the financial ability to repay loan after covering major financial obligations and living expenses.<sup>2</sup>
- In addition to the ability-to-repay requirements above, the prevention requirements would also include the following requirements:
  - Lenders would generally have to adhere to a 60-day cooling off period between loans.
  - A consumer could not have any other outstanding covered loans with any lender.
  - Rebuttable presumption of inability to repay - To make a second or third loan within the 60-day cooling off window, lenders would have to document that the borrower’s financial circumstances have improved enough to repay a new loan without re-borrowing. Lenders would have to verify, for example, that the consumer’s income had increased following the prior loan.
  - Conclusive presumption of inability to repay - After three covered short-term loans in a sequence, there would be a conclusive presumption that the consumer lacks the ability to repay. Lenders would be prohibited from making covered short-term loans to that consumer for 60 days.

#### Protection Requirements

Alternatively, a lender could offer short-term loans by complying with the Protection Requirements. These requirements would limit the number of loans that a borrower could take out in a row and require lenders to provide affordable repayment options.

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<sup>1</sup> The Bureau is considering two alternatives for defining major financial obligations. One alternative would include housing payments (mortgage or rent), debt repayment, child support and other legally required payments. Another alternative would also include utilities, regular medical expenses and other required payment obligations.

<sup>2</sup> The Bureau is considering proposals that would require a lender to consider a consumer’s borrowing history, both with the lender and its affiliates and with other lenders.

- In lieu of determining a consumer’s ability to repay, a lender must apply the screening requirements noted below:
  - The lender verifies the consumer’s income;
  - The lender verifies the consumer’s borrowing history and reports use of the loan to all applicable commercially-available reporting systems;
  - The consumer does not currently have a covered loan outstanding with any lender;
  - The consumer takes out no more than three such alternative loans in a sequence (any loan taken out within 60 days of having a prior loan outstanding), and has not completed a three-loan sequence of alternative loans from any lender within the past 60 days;
  - After repayment of the third loan in a sequence, the lender extends no additional credit, whether or not a covered loan, to the consumer for a period of 60 days;
  - The loan would not result in the consumer receiving more than six covered short-term loans from any lender in a rolling 12-month period; and
  - Following completion of the contractual loan term, the consumer will not have been in debt on covered short-term loans for more than 90 days in the aggregate during a rolling 12-month period.
  
- If the consumer meets the screening criteria, a lender could extend a loan that:
  - Is for no more than \$500;
  - Has a contractual duration of 45 days or less with no more than one finance charge for the period of the loan;
  - Does not take a security interest in a vehicle as collateral; and
  - Is designed to taper off the consumer’s indebtedness. To taper off indebtedness, the Bureau is considering requiring either that: (a) lenders provide a no-cost off-ramp for consumers unable to repay the debt after the third loan in a sequence<sup>3</sup> or (b) lenders reduce the principal amount of subsequent loans so that the debt amortizes over three loans.

### **Covered Longer-Term Loans**

The Proposal generally covers longer-term credit products with a contractual duration longer than 45 days and an all-in annual percentage rate in excess of 36 percent where the lender holds either (1) access to repayment through a consumer’s account or paycheck, or (2) a non-purchase money security interest in the consumer’s vehicle.

The Bureau indicates that in order to reduce compliance burdens for lenders, it is considering the use of existing thresholds, such as the Military Lending Act’s 36 percent all-in annual percentage rate, which includes interest, fees, and add-on product charges.<sup>4</sup>

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<sup>3</sup> Under the Bureau’s Proposal, lenders would be required to allow a consumer to repay the third loan over an additional four installments without incurring additional cost.

<sup>4</sup> Under the Military Lending Act, all-in APR includes the following cost elements associated with the extension of consumer credit to a covered borrower if they are financed, deducted from the proceeds of the consumer credit, or otherwise required to be paid as a condition of the credit: (i) Interest, fees, credit service charges, credit renewal charges; (ii) Credit insurance premiums including charges for single premium credit insurance, fees for debt cancellation or debt suspension agreements; and (iii) Fees for credit-related ancillary products sold in connection with and either at or before consummation of the credit transaction. The Military Lending Act all-in APR does not include: (i) Fees or charges imposed for actual unanticipated late payments, default, delinquency, or

The Bureau is also considering whether to require lenders to take steps to determine that borrowers have the ability to repay their loans. Just as with short-term loans, lenders would have two alternative ways to meet this requirement – *Prevention Requirements* or *Protection Requirements*. Lenders must adhere to either the *Prevention Requirements* or the *Protection Requirements*, but not both.

#### Prevention Requirements:

- This option would require lenders to make the same good-faith, reasonable determination that the consumer can repay a loan when due that would be required for short-term loans.
- Presumption of inability-to-repay - The Proposal would create a presumption that the consumer lacks the ability to repay a covered longer-term loan for certain refinancing and reborrowing:
  - Rebuttable presumption of inability to repay refinanced loan - When a consumer seeks to refinance certain prior debts into a covered longer-term loan, the lender would be required to presume that the consumer lacks the ability to repay such a loan. To overcome the presumption, the lender would have to verify a change in circumstances such that the consumer would have the ability to repay the loan. This rebuttable presumption would be applicable to refinancing transactions in certain circumstances where there is an indication that the consumer has struggled to afford payments on the loan being refinanced.
  - Rebuttable presumption of inability to repay covered longer-term loan with balloon payment - The Bureau is considering treating covered longer-term loans with a balloon payment in the same manner as covered short-term loans. For covered longer-term loans with a balloon payment, there would be a rebuttable presumption of inability to repay for repeated borrowing in the same loan sequence. The presumptions would apply to the second and then third loans in a sequence. A loan sequence would include loans extended within 60 days of the consumer having a covered longer-term loan with a balloon payment outstanding. To overcome the presumption, the lender would have to verify a change in circumstances that would show that the consumer has the ability to repay the loan.
    - After three covered longer-term loans with a balloon payment (or covered short-term loans or a combination of both types of loans) in a sequence, there would be a conclusive presumption that the consumer lacks the ability to repay. Lenders would be prohibited from making covered loans until a 60-day cooling-off period had elapsed.
    - In determining a consumer’s ability to repay covered longer-term loans with a balloon payment, lenders would need to consider income and major financial obligations for 60 days beyond the term of the loan.

#### Protection Requirements

Alternatively, a lender could offer longer-term loans by complying with the Protection Requirements.

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similar occurrence; (ii) Taxes or fees prescribed by law that actually are or will be paid to public officials for determining the existence of, or for perfecting, releasing, or satisfying a security interest; (iii) Any tax levied on security instruments or documents evidencing indebtedness if the payment of such taxes is a requirement for recording the instrument securing the evidence of indebtedness; and (iv) Tax return preparation fees associated with a tax refund anticipation loan, whether or not the fees are deducted from the loan proceeds.

- The Bureau is considering two specific approaches to the protection requirements for longer-term products. Under either approach, loans would have a minimum duration of 45 days and a maximum duration of six months.
  - Under the first approach, all lenders could provide generally the same terms as loans offered under the National Credit Union Administration (NCUA) program for “payday alternative loans.” Under this requirement, the following restrictions would apply:
    - Screening requirements - Among other criteria, the lender would need to verify the consumer’s income and that the consumer had no other covered loans outstanding, and determine that the loan would not result in the consumer having more than two covered longer-term loans under the NCUA-type alternative requirement from any lender in a rolling six-month period.
    - Structural protections - If the consumer meets the screening criteria, a lender could extend a loan that:
      - 1) Is between \$200 and \$1,000 with a duration between 45 days and six months;
      - 2) Fully amortizes over no more than two payments; and
      - 3) Meets NCUA cost criteria (charging no more than 28 percent interest and an application fee of no more than \$20).
  - Under the second approach, for loans with payment-to-income ratios of below five percent lenders could make a longer-term loan provided the following conditions are met:
    - Screening requirements - Among other criteria, the lender would need to verify the consumer’s income and that the consumer had no other covered loans outstanding, and determine that the loan would not result in the consumer receiving more than two covered longer-term loans under the maximum PTI loan alternative requirements from any lender in a rolling 12-month period.
    - Structural protections - If the consumer meets the screening criteria, a lender could extend a loan that:
      - 1) Limits periodic payments to no more than 5 percent of the consumer’s expected gross income during the same period;
      - 2) Has a duration between 45 days and six months;
      - 3) Has no prepayment penalties; and
      - 4) Is closed-end and repayable in at least two substantially equal payments over no fewer than 45 days.

### **Limits on Collection Practices**

The Bureau is concerned that lenders of both short-term and longer-term loans often obtain access to a consumer’s checking, savings, or prepaid account to collect payment through a variety of methods, including post-dated checks, debit authorizations, or remotely created checks. The Bureau believes that this can lead to unanticipated withdrawals or debits and overdraft fees.

To mitigate these issues, the Bureau is considering:

- Requiring borrower notification before accessing deposit accounts: Lenders would be required to provide consumers within three business days advance written notice before submitting a transaction to the consumer’s bank, credit union, or prepaid account for payment. The notice would require key information about the forthcoming payment collection attempt including:
  - 1) The exact amount and date of the upcoming payment collection attempt;
  - 2) The payment channel through which the attempt will be made;

- 3) A break-down of the application of payment amount to principal, interest, and fees (if applicable);
  - 4) The loan balance remaining if the payment collection attempt succeeds;
  - 5) The name, address, and a toll-free phone number that the consumer can use to reach the lender; and
  - 6) For payment collection attempts made by check, such as a post-dated signature check or RCC, the check number associated with the payment attempt.
- Limiting unsuccessful withdrawal attempts that lead to excessive deposit account fees: If two consecutive attempts to collect money from the consumer's account were unsuccessful, the lender would not be allowed to make any further attempts to collect from the account unless the consumer provided a new authorization.

### **Possible Required Disclosures**

The Bureau is considering whether to require lenders to provide a disclosure to consumers explaining the operation of the alternative requirements for covered short-term loans. Lenders would need to develop policies and procedures for filling out and providing the disclosures, and lenders' employees would have to spend time preparing the disclosure for each borrower.

### **Compliance Requirements**

The Proposal considers requiring lenders to maintain policies and procedures that are reasonably designed to achieve compliance with the proposals under consideration. These policies and procedures would cover:

- The lender's process for determining ability-to-repay when originating covered loans;
- Reporting to and checking covered loan information in commercially available reporting systems;
- Maintaining the accuracy of loan information furnished to a commercially available reporting system; documenting the ability-to-repay determination in the consumer's loan file;
- Overseeing third-party service providers; ensuring that payment notices are provided; and
- Tracking the payment presentments on a loan.

The Proposal also considers requiring lenders to retain records documenting actions taken with respect to a covered loan until 36 months after the last entry on the loan. The consumer loan file would be required to include:

- Documentation of the ability-to-repay determination, verification of the consumer's history of covered loans;
- Application of any of the alternative requirements for certain loans;
- History of payment presentments (including date of presentment, amount presented, payment channel used, and outcome);
- Whether attempts to collect payment on the loan triggered the presentment limit;
- Details of any new payment authorizations provided by the consumer; and
- Notices sent prior to attempts to collect from consumers' accounts.

These records would also include annual reports containing data sufficient to monitor performance of covered loans.

## **Expected Next Steps**

In addition to conducting the Small Business Review Panel review, the Bureau is meeting with various stakeholders, including ICBA members, to discuss the Proposal. A rulemaking is expected later this year.