

# HOUSE BILL REPORT

## ESHB 1709

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### As Amended by the Senate

**Title:** An act relating to fee and installment plan assistance for borrowers at risk of default on small loans.

**Brief Description:** Providing fee and installment plan assistance for borrowers at risk of default on small loans.

**Sponsors:** House Committee on Financial Institutions & Insurance (originally sponsored by Representatives Nelson, White, Cody, Carlyle, Orwall, McCoy, Darneille and Ormsby).

#### **Brief History:**

##### **Committee Activity:**

Financial Institutions & Insurance: 2/10/09, 2/17/09 [DPS].

##### **Floor Activity**

Passed House: 3/9/09, 84-10.

Senate Amended.

Passed Senate: 4/13/09, 40-8.

#### **Brief Summary of Engrossed Substitute Bill**

- Requires a minimum term for small loans.
- Limits the amount of money in small loans that may be borrowed by a consumer at any one time and as a percentage of gross monthly income.
- Creates a new installment plan for borrowers.
- Authorizes a real-time enforcement system.

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### HOUSE COMMITTEE ON FINANCIAL INSTITUTIONS & INSURANCE

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 10 members: Representatives Kirby, Chair; Kelley, Vice Chair; Bailey, Ranking Minority Member; Parker, Assistant Ranking Minority Member; Hurst, McCoy, Nelson, Roach, Santos and Simpson.

**Staff:** Jon Hedegard (786-7127)

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

## **Background:**

Small loans (better known as "payday loans") are regulated by the Department of Financial Institutions (DFI) under the Check Cashers and Sellers Act (Act), chapter 31.45 RCW. The Act contains provisions for the licensing and regulation of businesses offering services related to check cashing and the selling of money orders, drafts, checks, and other commercial paper. The Act regulates payday lending practices and provides for regulation of licensees who are specifically authorized to issue small loans.

The phrase "payday loan" refers to a type of short-term, unsecured loan that is typically offered to consumers by a business outlet offering check cashing services. In a typical payday loan transaction, the borrower writes the lender a post-dated check and, in return, the lender provides a lesser amount of cash to the consumer after subtracting interest and fees. Following this initial transaction, the lender holds the check for a specified period, during which the consumer has the option of either redeeming the check by paying the face amount to the lender or allowing the lender to cash the check after the loan period has expired.

### Terms of Payday Loans.

No lender may lend more than \$700 to a single borrower at any one time. The lender may charge up to 15 percent for the first \$500. If the borrower has a loan in excess of \$500, the lender can charge up to 10 percent on the amount over \$500. For example, a lender could charge up to \$30 for a \$200 loan or up to \$85 for a \$600 loan.

There is no minimum loan term for a payday loan. There is a statutory maximum loan term of 45 days.

### Right of Rescission.

A borrower may rescind a loan, on or before the close of business on the next business day at the location where the loan was made. The borrower must return the principal in cash or the original check of the licensee. A licensee may not charge the borrower a fee for rescinding the loan and must return any postdated check taken as security for the loan or any electronic equivalent.

### Payment Plan.

Borrowers and lenders may agree to a payment plan for payday loans. After four successive loans, and prior to default on the last loan, a borrower is entitled to convert his or her loans into a payment plan with the lender. A payment plan is subject to the following conditions:

- a written agreement is required;
- the lender may charge the borrower a one-time fee in an amount up to the fee or interest on the outstanding principal;
- the agreement must allow the buyer not less than 60 days to pay off the loan; and
- the borrower must be allowed to pay off the loan in at least three payments.

### Recordkeeping.

Under the Act, licensees must maintain business books, accounts, and records. The books and accounts must be maintained for at least two years after a transaction. The DFI also has statutory authority to examine books, accounts, records, and files, or other information of

licensees and persons that the agency has reason to believe is engaging in the business governed by chapter 31.45 RCW.

#### Agency Enforcement.

The Director of the DFI may impose sanctions against any:

- licensee;
- applicant; or
- director, officer, sole proprietor, partner, controlling person, or employee of a licensee.

Sanctions may include:

- the denial, revocation, suspension, or conditioning of a license;
- an order to cease and desist from specific practices;
- the imposition of a fine not to exceed \$100 per day for each day's violation;
- the provision of restitution to borrowers or other injured parties; and
- the removal from office or banning from participation in the affairs of any licensee.

#### Consumer Protection Act.

A violation of the Act is a violation of the Consumer Protection Act (CPA). Remedies under the CPA do not affect any other remedy available to an injured party.

In a suit for a CPA violation, an injured party may sue for:

- the actual damages sustained;
- the costs of the suit;
- reasonable attorney's fees; and
- additional damages in the amount of up to three times the actual damages sustained by the plaintiff. These discretionary treble damages are capped at \$10,000 in superior court and \$50,000 in district court.

The Attorney General may also sue to:

- prevent or restrain violations of the CPA; and
- seek restitution for persons injured by violation of the CPA.

#### **Summary of Engrossed Substitute Bill:**

##### Loan Terms.

The minimum term of a loan is the borrower's next paycheck unless that is less than seven days. If it is less than seven days, the minimum term is the date of the next following pay date. A borrower may not take out more than \$700 in small loans at any time from all lenders. A borrower may not borrow more than 30 percent of his or her gross monthly income.

A licensee is prohibited from making a small loan to a borrower that is in default on a small loan. This prohibition lasts until the loan is paid in full or for two years after the small loan was made, whichever is earlier. A licensee is prohibited from making a small loan to a borrower that is in an installment plan. This prohibition lasts until the installment plan is paid in full or for two years after the origination of the installment plan, whichever is earlier. A licensee is prohibited from making a small loan to a borrower if making that small loan

would result in a borrower receiving more than eight small loans from all licensees in any 12-month period.

#### Disclosure.

An application form for a small loan must disclose the installment plan to the borrower in a specified manner.

#### Installment Plan.

The existing payment plan is eliminated. A new installment plan is created. The lender must inform the borrower that if the borrower cannot repay a loan when the loan is due, then the borrower may convert the small loan to an installment plan. The lender must convert a small loan to an installment plan at the borrower's request. A loan of up to \$400 has a minimum term of 90 days for a loan with payments in substantially equal installments on or after a borrower's pay dates and at least 14 days apart. A loan of over \$400 has a minimum term of 180 days with payments in substantially equal installments on or after a borrower's pay dates and at least 14 days apart. A fee is not allowed for the installment plan. The borrower may pay the total at any time without a penalty. The lender must return any postdated check from the borrower for the original small loan when the borrower enters into an installment plan. A licensee may take postdated checks for the installment plan. A licensee may not charge a fee for a dishonored check in connection to an installment plan but may charge a one-time \$25 fee if the borrower defaults on the installment plan.

#### Enforcement System.

A system is authorized to enforce these provisions and other parts of chapter 31.45 RCW. The use of the system will enable a licensee to verify if the potential borrower is eligible for a small loan. The system must be available in real-time and secure against unauthorized acquisition or use, tampering, or theft. The Director of the DFI (Director) must establish the fee by rule. A lender may not charge an additional sum to recover the fee. Information in the system is exempt from public disclosure.

#### Report.

The Director must collect and submit the following information to the Legislature:

- the number of borrowers entered into an installment plan since the effective date of this section;
- how the number of borrowers in installment plans compares to the number of borrowers in payment plans in years previous to the effective date of this section;
- the number of borrowers who have defaulted since the effective date of this section;
- the number of borrowers who have defaulted compared to the number of borrowers who defaulted in years previous to the effective date of the new installment plan; and any other information that the Director believes is relevant or useful.

#### **EFFECT OF SENATE AMENDMENT(S):**

The bill, as amended by the Senate, retains several provisions of the bill that passed the House. A provision still limits the amount loaned to \$700 per borrower or 30 percent of the 30 percent of the borrower's gross monthly income at any one time. An enforcement system is created and personal information of a borrower related to that system is exempt from public disclosure. The effective date remains January 1, 2010.

Several sections of the bill passed by the House are struck. Changes in definitions are removed. The provisions establishing a minimum loan term of at least 7 days are removed. Prohibitions on making a loan to a borrower that is in default or in an installment plan are removed. The loan limit of eight loans to a single borrower every twelve months is removed. The provisions establishing an installment plan for borrowers that cannot pay a loan when it is due are removed. The disclosure provisions are removed. The report to the Legislature is removed.

**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill takes effect on January 1, 2010.

**Staff Summary of Public Testimony:**

(In support) This bill preserves the ability to get a small loan. The fee is reduced to 10 percent of the borrowed amount. A minimum term of 60 days is established. If a borrower has trouble paying off the loan, it is probably because the principal is too high. This bill would allow that borrower to convert into an installment plan. The borrower can repay the debt and get out of the cycle. The fees on these loans can lead to a situation where the borrower never catches up. The state should place greater restrictions on the payday lending industry. These loans are often rolled over. Some credit unions offer similar products at much lower interest rates. Those credit unions probably break-even. Loan fees can add up and lead to additional loans. The business model of payday lenders is set up to exploit those who have no other options. Payday loans often lead to further payday loans. A cycle is created that traps the borrower. Some lenders violate or maneuver around the law. Other lenders use questionable collections practices. Collection agency restrictions do not apply to a business that is not a collection agency. This bill provides valuable consumer protections. There is no credit analysis or consideration of the ability to repay when these loans are made.

(Opposed) As drafted, this is a ban. It reduces fees by 33 percent and makes the loan term four times longer than the average loan term in the state. The installment part has flaws but it won't be used because loans will not be made under this structure. The Oregon law has more generous terms to lenders than this bill but it has led to lender closures. The demand has not gone away but the lenders have left. The result is consumers will have fewer, more costly choices or will borrow from internet lenders in violation of the law. House Bill 1709 is unrealistic. Revenue would be reduced by 80 percent under the provisions of the bill. No industry could survive that kind of revenue reduction. According to the 2007 payday lending statistics from the DFI, the average store makes a monthly profit of about \$1,500 after expenses. This bans the industry. This would mean thousands of people will lose their jobs. It would also eliminate a choice for borrowers. House Bill 1709 will reduce revenue to a point that lenders will close their stores. Studies show that borrowers are low to middle income backgrounds who understand these products and their option. The borrowers are better educated than the average populace. Recent research shows that when this option is taken from people, those communities are harmed. People bounce more checks, go bankrupt more often, and are more likely to take out illegal loans. There are too few credit options

today; the choices should not be reduced. House Bill 1709 would prohibit small loans. No company will make a loan under these conditions. It is increasingly difficult to find credit. These bills would eliminate a current credit option. This is a well-regulated product. The loss of this product will lead to the loss of many of these lenders and the loss other products offered by these lenders like money transmitter services. Many people in minority communities don't have bank accounts. Some prefer non-traditional options. Many are also employed by these lenders. Many people in minority communities have trouble getting credit. Taking away an option will not help them and it will not pay their bills. They will turn to unregulated loans that are more costly and have no consumer protections. Payday loans can be a useful tool for a person who uses the loans wisely. Some people don't want long-term debt. The fees and terms are known to the borrowers. Borrowers understand the transaction. It does not make sense to take this option away. Credit cards, bouncing a check, taking out an illegal loan, these are the options that will be left. Payday loans may be the only credit option for a person trying to leave a bad relationship. Most loans are used responsibly.

**Persons Testifying:** (In support) Representative Nelson, prime sponsor; Michael O'Hanlon; Bob Cooper, National Association of Social Workers; Jeanne Henderson, Poverty Action; Margaret Engel; Eden Greer, Washington State American Association of Retired Persons; and Laurie Tufford.

(Opposed) Dennis Bassford, Moneytree; Darrell Wells, Paycheck Financial Systems; Kevin McCarthy, Checkmasters; Oscar Eason; Chris Guillen, Plaza Bank Washington; and Pamela Fann.

**Persons Signed In To Testify But Not Testifying:** None.