Financial Regulators Should Not Sanction High-Cost Unaffordable Loans

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As the OCC soon clarifies its position on small dollar loans, it should ensure loans are reasonably priced and based on account holders' income and expenses

WASHINGTON, D.C. – **The Center for Responsible Lending, Americans for Financial Reform, National Consumer Law Center (on behalf of its low income clients), U.S. PIRG, Missouri Faith Voices—a Federation of Faith in Action, Consumer Federation of America, UnidosUS, and NAACP** sent a letter urging federal bank regulators to prevent high-cost loans by banks and credit unions—whether short-term, balloon payment payday loans (also known as "deposit advance" loans) or high-cost longer-term installment loans.

The letter came as the Office of the Comptroller of the Currency (OCC) has announced it will soon clarify its position on installment lending. "While financial institutions should be encouraged to make low-cost, affordable small dollar loans, we reject calls for banks to make loans with rates as high as 99%," **the group wrote**. In addition, the letter stated that replacing traditional underwriting with a payment-to-income ratio of 5% would result in unaffordable loans for many financially distressed borrowers.

The groups emphasized that loans made by banks should carry interest rates of 36% or less, consistent with the Military Lending Act and the laws of many states. They also urged all regulators to require banks to determine whether borrowers have the ability to repay their loans based on an assessment of the borrower's income and expenses. Otherwise, banks may lend based on their ability to seize repayment directly from the customer's next incoming deposit—meaning the bank is repaid but the customer is left without sufficient funds to meet other obligations and expenses.

The letter also urged regulators to keep unaffordable 200-300% short-term balloon-payment payday loans at bay. The OCC's position on these "deposit advance" payday loans may be in flux. Last October, the OCC rescinded its 2013 guidance curbing those loans in response to the Consumer Financial Protection Bureau's (CFPB) announcement that it would put in place ability to repay standards for short-term payday and car-title loans. But the CFPB has since announced it will reconsider its payday loan rule, potentially opening the door for banks to return to toxic 300% payday loans.

Six banks—Wells Fargo, US Bank, Regions Bank, Fifth Third Bank, Bank of Oklahoma and GuarantyBank—were making 200-300% interest predatory payday loans to their own account holders until 2013, when a public outcry and risks to the banks' safety and soundness led bank regulators to establish commonsense guidelines that curbed these unaffordable loans. The banks were siphoning $500 million annually from customers who were caught in a devastating debt trap structured just like storefront payday lending.

The letter underscores the need for the OCC to reinstate its deposit advance guidance; the FDIC to retain its deposit advance guidance; the Federal Reserve to issue guidance mirroring the OCC's and FDIC's; and the CFPB to retain its payday loan rule's general applicability to short-term bank deposit advance loans.

In addition, the letter urges regulators to prevent banks from engaging in rent-a-bank arrangements with nonbanks, which facilitate nonbank lenders' ability to rely on banks' preemption privileges to circumvent state usury laws.

The group of organizations sent their letter to the OCC, National Credit Union Administration, CFPB, FDIC, Federal Reserve System, and the Office of Management and Budget.