Testimony in Support of Bill 25-609
Protecting Affordable Loans Amendment Act of 2023
Before the Committee on Business and Economic Development
of the Council of the District of Columbia
By Lauren Saunders, Associate Director, National Consumer Law Center

March 13, 2024

Chairperson McDuffie and Members of the Committee,

Thank you for the opportunity to testify. I am Lauren Saunders, Associate Director of the National Consumer Law Center (NCLC), a national non-profit organization that uses its consumer law expertise to work for economic justice for low-income and vulnerable consumers. NCLC publishes a treatise, Consumer Credit Regulation, which discusses state lending laws and attempts to evade them. We also regularly survey all 50 states' interest rate caps on installment loans and issue reports, including Predatory Installment Lending in the States and, most recently, Larger Loans Need Lower Rates: A 50-State Survey of the APRs Allowed for a $10,000 Loan.

I am pleased to support the Protecting Affordable Loans Amendment Act of 2023 ("PALs Act"). The bill prevents evasions of the District of Columbia's strong consumer protection laws by codifying the widely-accepted "true lender" doctrine and by opting DC out of a federal law that allows out-of-state, state-chartered banks to charge high rates not allowed in DC. The bill will prevent predatory lenders that charge annual percentage rates (APRs) of 200% or more from evading DC's 24% interest rate limit.

Rent-a-bank schemes and fake tribal loans evade interest rate limits

In a rent-a-bank scheme, a high-cost, nonbank lender launders its loan through an obscure bank, mostly in Utah, and claims that it is a "bank loan" exempt from state laws. Rent-a-bank schemes started with payday lenders and more recently have been used by on-line installment lenders, including:

- Opportunity Financial, dba OppFi or OppLoans, which makes installment loans at rates up to 160% APR.

- Elevate Credit, which makes Rise installment loans at 99% to 149% APR and markets Elastic lines of credit with effective APRs of about 100%.
- Enova, which makes NetCredit-branded installment loans up to 99.99% APR.
- EasyPay Finance, which makes loans up to 188.99% APR through brick-and-mortar businesses that sell auto repairs, furniture, home appliances, pets, and tires.
- American First Finance, which makes similar loans through stores at rates up to about 161% APR.

Loans at these rates are debt traps, with payments that go primarily to interest, high refinancing rates that extend the debt even longer, and high default rates. These loans are illegal in nearly every state and in DC, which limits interest rates to 24%. But the lenders use "rent-a-bank" schemes to put a bank's name on the paperwork and claim that their loans are bank loans exempt from state law.

Despite the bank's name on the loan, the bank has a minor role. The nonbank lender typically designs and owns the loan program, processes applications, approves loans, collects payments, and reaps the vast majority of the revenues, up to 96%. The bank rubber stamps the underwriting criteria and "originates" the loan by sending the money to the consumer. The bank is then quickly paid back by the nonbank lender or sells the vast majority of the loan revenues to the nonbank lender.

Many of the predatory lenders listed above have operated in DC, but strong enforcement actions by the attorney general have pushed them out for the time being. But enforcement is time-consuming and does not prevent new schemes to evade DC law.

In another type of evasion that is similar to rent-a-bank schemes, predatory lenders have affiliated with Native American tribes in an attempt to use their tribal sovereign immunity as a shield against enforcement of state or District law. These lenders charge triple-digit interest rates that can be as high as 700% or 800%. Fake tribal lenders have operated in DC.

DIDA opt out

Rent-a-bank schemes exploit a federal law, the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA or DIDA), 12 U.S.C. § 1831d, which allows out-of-state, state-chartered banks to charge, anywhere in the country, whatever interest rate is allowed in their home state. This is called "rate exportation." Many states do not cap interest rates for banks, and predatory lenders have exploited this fact to enable 100% to 200% APR loans in states where those rates are illegal.

However, states may opt out of DIDMCA and require the banks to comply with rate caps in the consumer's state. The PALs Act would exercise this right. Notably, Iowa, the only state that currently is opted out of DIDA, has none of the predatory lenders listed above. Predatory lenders have also exited Colorado, which adopted legislation to opt out of DIDA effective this July.

The true lender doctrine

The PALs Act also codifies the “true lender” doctrine, which allows courts to look behind the name on the loan document to discover that the true lender is not a bank but rather is a nonbank lender subject to state or District law. The true lender doctrine is an application of anti-evasion principles that go back over two hundred years in hundreds of cases in 49 states and DC. The true lender doctrine often focuses on which party has the “predominant economic interest” in the loan. But that is not the sole factor. Anti-evasion efforts require looking at the totality of the circumstances because usury evasions are infinitely varied.

In the modern context, the true lender doctrine has been recognized in a variety of situations by at least 33 court decisions. The Federal Deposit Insurance Corp. has acknowledged the true lender doctrine and, in 2020, a bipartisan vote of Congress under the Congressional Review Act repealed a regulation by the Office of the Comptroller of the Currency that would have overturned the true lender doctrine.

The DC attorney general has already relied on the true lender doctrine in its enforcement actions, but codifying the doctrine will strengthen the AG’s hand. Many states have codified the true lender doctrine in statute including, since 2021, Illinois, Maine, New Mexico, Connecticut and Minnesota. The Washington State legislature also just voted nearly unanimously to adopt a true lender bill, which is awaiting the governor’s signature. These laws have been effective, causing rent-a-bank lenders to leave those states.

The PALs Act stops 200% APR predatory lending evasions

DC has among the strongest anti-predatory lending laws in the country, with clear interest rate limits that prohibit payday loans and other forms of high-cost lending. But those laws are at risk of evasion, and rent-a-bank and fake tribal lenders have operated in DC.

By opting DC out of DIDA and codifying the true lender doctrine, the PALs Act will allow DC to enforce its law. The DIDA opt-out will put an immediate end to triple-digit rent-a-bank schemes by state-chartered banks. Codifying the true lender doctrine will strengthen DC’s ability to prevent predatory lenders from turning to national banks (which can still export their interest rates) or from hiding behind tribes.

The PALs Act will preserve access to affordable credit

Credit cards will still be available to DC residents. Most credit cards are offered by national banks, which will not be affected by the bill. Those offered by state-chartered banks need only comply with the District’s interest rate limits. Most credit cards are within DC’s legal limits, and higher rates are excessive for a credit card and lead to a debt trap. Indeed, it was the pain and outrage generated by 29% APR penalty rates that led Congress to pass the federal Credit CARD Act of 2009.

Fintech lenders can also operate within DC's interest rate limits, and most of their loans already do. But for larger loans, even 36% is an exorbitant and unaffordable rate. For example, raising the rate on a $10,000, five-year loan from 24% to 36% adds a whopping $4,419 in interest – nearly half the loan itself. Many fintechs make even larger loans up to $30,000 or larger, which would be especially burdensome if rates approached 36%. Loans above the rates authorized in DC are likely to be unsustainable burdens, not affordable credit. DC has appropriately determined fair interest rates for District residents, and the PALs Act will ensure that all nonbank lenders comply with the law.

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The DC City Council has adopted strong anti-predatory lending laws, and the PALs Act will ensure that those laws cannot be evaded. Predatory credit is not access to credit. It is access to a debt trap. The PALs Act will protect DC residents and I urge you to support it.

Thank you for the opportunity to testify. If you have any questions, please reach out to me at lsaunders@nclc.org.