American Bankers Association
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Ms. Monica Jackson
Consumer Financial Protection Bureau
1700 G Street NW
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Re: Comments on payday lending hearing transcript
77 Fed.Reg. 16817, March 22, 2012

The American Bankers Association (ABA)[1] appreciates the opportunity to comment on the transcript of the Consumer Financial Protection Bureau's (Bureau) field hearing on payday loans held on January 19, 2012, in Birmingham, Alabama. The purpose of the field hearing was to help the Bureau understand short-term, small dollar loans such as payday loans and bank "direct deposit advance" loans. The Bureau is offering the public the opportunity to review the transcript and provide additional feedback on these products and the issues raised.

The field hearing primarily focused on payday loans but also discussed "direct deposit advance loans" offered by some banks and credit unions. These loans are short-term, small dollar loans offered through a deposit account. Customers must "opt in" or initiate the loan, which is deposited into their deposit account and repaid automatically through a required recurring direct deposit. The products include various protective features to help customers avoid large debts and a cycle of debt. For example, typically, the amount of the loan is limited to the lesser of $500 or half of the direct deposit amount. In addition, new loans are not advanced until any existing loan is repaid, and consecutive use triggers a "cooling-off" period, during which the allowable loan is decreased until the customer achieves a zero balance.

The testimony of Mr. Richard Cordray, borrowers, lenders, and consumer and community representatives at the hearing vividly demonstrates two undeniable realities: one, there are people who need small dollar loans such as payday loans and direct deposit advance loans for whom other options are limited or unavailable, and two, there are costs to providing the services which must be recovered if those needing these products are to continue to have access to credit. We believe that direct deposit advance loans can respond to these realities and that users of direct deposit advance loans value the convenience, control, anonymity, and potential cost-savings of the product.

Demand and need for direct deposit advance loan product.

As Mr. Cordray acknowledged at the hearing, there is a demand for short term loans such as payday loans and direct deposit advance loans. At the hearing, he stated, "I want to be clear about one

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1 ABA represents banks of all sizes and charters and is the voice for the nation's $13 trillion banking industry and its two million employees. The majority of ABA's members are banks with less than $165 million in assets.

thing: We recognize that there is a need and a demand in this country for emergency credit."[2] He explained further, "People often are responding to an emergency that requires quick access to cash. It appears that a significant share of payday borrowers do not have savings or a credit card, and many like the payday option because it is relatively anonymous, quick and easy." Others speakers and witnesses supported the view that people need these loans and have few other choices:

> "Given these challenging economic times, many of my constituents in the 7th Congressional District and families across this country rely upon payday loan industry to satisfy many of their everyday needs for short-term cash." [3] (Statement of Congresswoman Terri Sewell.)
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> "I'm talking about anxiety, family stress, the catastrophe that comes from either medical bills, these unexpected expenses. . .and that's big stuff. Car repairs. Or little stuff, like your baby has to go on a field trip and you don't have the extra money." [4] (Statement of Mr. Stephen Stetson.)
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> "The thing that I want people to understand is that the people that live in my district don't have an alternative. " [5] (Statement of Alabama State Representative Oliver Robinson.)

Users of payday loans spoke about their need for the loans and lack of alternatives:

> LaDonna Banks described how she used a payday loan to bridge the gap between her paycheck and the short-term disability payment. "I borrowed the money. I paid the money back in two weeks. It was perfectly fine, and it was a need and a necessity for me at that time." [6]
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> Leigh Osborn testified about needing extra money to pay bills when she was between jobs. "You need your money . . . And it's a lot cheaper for me to go and get a payday loan than three $30 late fees on my bills."[7]
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> Tanji Thomas described how she needed a loan because of a family emergency. "I didn't have any other way to . . . come up with this extra money for this family emergency. . . And I was really glad that it was there, an option available to me. And I would like to know that in the future that it would be there in the event that I need it also." [8]

The fact is that for various reasons, some people lack sufficient funds to cover emergencies or to make ends meet from time to time. They also often do not qualify for other flexible credit products such as credit cards because they have had trouble managing those products in the past or have ended up with sizable debts that strained their finances.

Value of direct deposit advance loans to users and user protections.

Direct deposit advance loans that some banks offer are designed for this audience—people who find other credit products challenging, which may offer more choices and flexibility but also demand a certain level of financial management, attention, and responsibility. They also offer more convenience and anonymity than payday loans.

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2 "In the Matter of: A Field Hearing on Payday Lending," January 19, 2012. (p.19).
3 *Ibid.* p. 10.
4 *Ibid.* p. 37.
5 *Ibid.* p. 96.
6 *Ibid.* p.98.
7 *Ibid.* p.102.
8 *Ibid.* pp. 102, 103.

Customers enrolled in the direct deposit advance loan programs appreciate the “discipline” imposed by the products’ advance limits and automatic repayment features. Advances and maximum credit lines are modest—advances can be as low as $20 and maximum credit lines are usually limited to the lesser of $500 or 50 percent of the total amount of the recurring electronic deposit. Repayment of an advance occurs automatically with the next electronic deposit into the account, ensuring that borrowers make their payment. Customers enrolling in these programs are also people looking to *actively manage* their finances when unexpected expenses have depleted their checking account balance. They *anticipate* account overdrafts and take advances to cover them, avoiding overdraft, nonsufficient fund, and returned check/payment fees.

Customers also understand that deposit advance programs are the functional equivalent of receiving an advance on income or other regular deposit. For example, people who obtain a payroll advance from an employer understand that their employer will deduct the advance from their regular paycheck. The bank that offers a deposit advance program is behaving similarly, but, as a third party, the bank charges a fee for the accommodation.

In addition to the loan limits and automatic repayment feature, these programs feature other protections to help customers avoid a “cycle of debt” about which Mr. Cordray and witnesses at the hearing expressed concerns. For example, programs usually include “cooling off” periods: if the customer uses the product consecutively, e.g. for six to nine months, the amount available is gradually reduced to zero, leaving the customer debt-free at the end of the cooling off period. In effect, direct deposit advance programs enable customers to live within their means by limiting consecutive uses and the amount of advances, permitting them to control and manage the timing of the loan, and making repayment easier by making it automatic.

Another important protective element of this product is the eligibility requirements that increase the likelihood borrowers will have the ability to repay, a concern raised in the hearing with regard to payday loans. Customers must: (1) have at least one recurring electronic deposit of $100 or more every thirty to thirty-five days, (2) hold a checking account at the bank for a defined period of time (e.g. six months), and (3) maintain the account in good standing. While banks may not in all instances know the source of the recurring payment or gather information about the customers’ continued employment, and there is the potential that the customer will change jobs, redirect the deposit to an account at another bank, or elect another payment channel, experience demonstrates that abiding by these minimal standards results in a financially sound customer service that does not present “abnormal risk” of default. Moreover, the protections discussed above (loan amount limits, automatic repayments based on the recurring deposit, and cooling off periods) also help to ensure that customers have the ability to repay the loan.

Other features and practices ensure customers understand the product, their obligations, and options. Customers must elect, or opt-in, to participate. They receive information about fees as well as less expensive options such as overdraft lines of credit, and clear disclosures about initial and on-going eligibility requirements, how advances are requested and repaid, how credit lines are calculated, and cooling off periods that may apply.

Finally, direct deposit advance loan programs offer greater convenience and accessibility than payday loans. A payday loan requires a consumer to travel to the payday lender, wait in line, and in many instances, transport the cash to a bank or payment recipient. A direct deposit advance, in contrast, is available 24-hours a day, may be made in the privacy of the borrower’s home, and is deposited directly into the borrower’s account.

Fees and recovery of lenders' costs.

Direct deposit advance loans may be more expensive than other products such as an overdraft line of credit—and banks highlight that there are less expensive options—but they are often less expensive than other options, such as those resulting in multiple overdraft or returned payment fees. In addition, as an economic reality, fees must be sufficient to cover costs in order to continue to offer the product. Yet, that can be a challenge. As the Listerhill Credit Union witness, Mr. Daryl McMinn, testified at the hearing, even with a $25 fee to join the credit union and a $50 annual program fee, the credit union does not make a profit on its direct deposit advance loan program.[9]

The cost of providing these loans includes not just the cost of funds but unavoidable fixed costs that do not vary much based on the amount of the loan. These include, for example, the costs of employee salaries and benefits, light, heat, electricity, rent, computers, websites etc. Because of the unavoidable fixed costs, the fees for the loan can appear high *relative to the amount of the loan.* In addition, the fees have to cover losses from defaults. While losses from defaults are manageable, they do exist because the recurring direct deposit does not guarantee repayment, as the customer may leave that job, redirect the deposit into an account at a different bank, or elect to receive the salary through an alternative payment mechanism like a check or payroll card.

In addition, there are compliance costs to which we urge the Bureau to be sensitive when reviewing these products. We agree with Mr. McMinn that regulatory challenges facing regulated depository institutions are "steep," and we urge the Bureau "not to tie the hands of those of us who work every day to provide consumers with services they want in a fair, honest and reasonable way" and "not stifle our ability to offer the services and products that consumers want and that serve them well."[10]

Installment features.

It has been suggested that banks automatically provide an installment option for direct deposit advance loans. Under this option, borrowers could choose to repay a single advance in multiple periodic payments. We are aware of one bank that offers installment repayments after three consecutive months, and we understand that banks are considering permitting installment repayments. However, it is not clear that these borrowers want or benefit from an automatic option to repay through installments. One bank found through its customer research that this was a low priority for users of the product and that customers may not want the temptation of the option as their past history with credit has suggested that an installment feature makes them more vulnerable to repayment problems. When reviewing installment options on these loans, the Bureau should consider the users' perspective and benefit as well as lender costs which will impact price.

Disclosures.

ABA believes that consumers should and do receive clear and conspicuous disclosures describing key program criteria and limitations, costs, and risks before enrolling in a deposit advance program. In addition, banks offering these products highlight the fees and the availability of less expensive alternatives that customers should consider. We also believe that banks should disclose the fact that repayment of a deposit advance may take priority over the payment of other items presented for payment and may result in overdraft or non-sufficient fund fees being assessed. We do not, however,

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9 *Ibid.* Mr. Daryl McMinn, Listerhill Credit Union. "This is not a money maker for us. At best, we break even," (p. 78) "We're not in the profit in this." (p. 60)

10 *Ibid.* pp. 61, 62.

believe that the disclosure should also include a broader disclosure of the bank's transaction clearing policy and process. Such a disclosure invites a false reliance on a process that varies based on presentment factors that neither banks nor customers control, thereby defying any effort by consumers to manage precisely the clearance process. At best, this clutters the disclosure and distracts users without enlightening them in a meaningful way.

In addition, we agree that customers should also be informed that if they have a question or believe there is an error concerning their use of the deposit advance service, they should follow the procedure for resolving questioned or disputed electronic funds transfers described in their checking account agreement.

Conclusion.

ABA appreciates the Bureau's outreach to learn about and gather information about payday loans and direct deposit advance loans. As the witnesses and speakers at the hearing attest, there is a demand and need for direct deposit advance loans for people who need the money but have few alternatives. Direct deposit advance loans can serve that need, incorporating features that suit and protect this type of borrower. In addition, there are unavoidable costs, both fixed and variable, that must be recovered if borrowers are to continue to have this option. In reviewing these products, the Bureau should be sensitive to the borrowers' needs and the lenders' costs so these products continue to be available to those who otherwise may not have access to credit at the time they most need it. We are happy to provide additional information or suggestions.

Regards,

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