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Gerard Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

RE: Comments on Notice of Proposed Rulemaking (PALs II)
RIN 3133-AE84

Dear Mr. Poliquin,

I write to offer thoughts on the NCUA's proposed changes to its Payday Alternative Loan program. As an economic sociologist, I spend a great deal of time studying financial inclusion, including how immigrant and minority households become integrated into the financial system. I am interested in the financial coping mechanisms that unbanked households utilize, and how banked households use both mainstream and alternative financial services to meet their needs. The books I have written about these topics include The Sage Encyclopedia of Economics and Society and The Culture of Markets. I also edited Money Talks: Explaining How Money Really Works, published last year. My colleagues and I are now putting the final touches on a new book **Financial Citizenship From Below**. In conducting this work, I have been fortunate to have access to the Mission Asset Fund's remarkable programs, started by recent MacArthur Fellow Jose Quiñonez, where the value of credit without onerous terms is clear. A critical question posed by the research I conduct is how we can enable households facing major barriers in their daily lives to have access to financial services, without suffering the harms imposed by predatory products like payday loans. Credit can help households bridge shortfalls during months when they have an income decline so that they may keep the utilities on, buy necessities, or as my colleague Matthew Desmond has documented, stave off eviction. But payday and similar loans are so expensive that most people who use them pay more in finance charges than they originally received in credit.

Despite the onerous terms of payday loans, we see millions of Americans turn to them because they lack better credit options. I hope that NCUA will modify its proposed rule to make it more feasible for credit unions to expand their offerings of lower-cost loans, encourage reporting to credit bureaus, ensure affordable payments, and create superior alternatives not just for those who use payday and auto title loans, but those who currently use other forms of expensive credit like late fees, overdraft, pawn loans, rent-to-own services, and subprime installment loans. People who use all of these could benefit from better credit, especially if it allowed them to graduate to mainstream, lower-cost loans.

The fact that credit unions would report these loans to credit bureaus would help customers rebuild their credit scores or establish them if they lack credit scores to begin with. But unfortunately, credit unions have not been able to develop a feasible, scalable alternative to payday loans yet. The very low revenue constraints under the PAL program have made this lending unprofitable. On a $500, 3-month loan, credit unions can charge just $44—not enough to cover their costs and invest in the automation needed for this lending to grow. Payday lenders typically charge about $450 in fees to borrow $500 for 3 months—an outrageous sum. I urge NCUA not to allow rates that are anywhere in the ballpark of payday loans, but to allow somewhat higher prices than proposed, to allow small-loan programs to reach scale. Similarly, it's important that credit unions be able to offer small lines of credit. Data from the Bureau of Labor Statistics show that 80.4 million Americans were paid hourly in 2017. Hourly workers have less predictable income and are more susceptible to both income spikes and dips than salaried workers. A line of credit option could help them smooth across these changes so they could borrow during dips and repay without penalty when their incomes spike.

Below, please find my column that ran in *The New York Times* on this topic as you formulate this regulation that could make credit unions a viable source of sustainable small-dollar lending. While this Payday Alternative Loan program has been a small one so far, with a little more revenue and flexibility, it could grow and make a dent in the high-cost lending market. Typical borrowers could save hundreds of dollars per year.

Thank you for your consideration.

Frederick Wherry
Professor of Sociology
Princeton University

https://www.nytimes.com/2015/10/29/opinion/payday-loans-cost-the-poor-billions-and-theres-an-easy-fix.html?_r=0

Payday Loans Cost the Poor Billions, and There's an Easy Fix

By Frederick Wherry
Oct. 29, 2015

EVERY year, millions of Americans who need a short-term loan to repair a car, fly quickly to a sick relative's bedside, or catch up on child care payments find themselves going to payday lenders, either online or through one of the thousands of payday-lending storefronts. These are not people without credit or steady jobs. They simply can't borrow such small amounts through the traditional banking system.

What might start as a $500 lifeline can quickly become a heavy burden. Annual interest rates for payday loans typically run between 391 and 521 percent, according to the Center for Responsible Lending, and most people who use them end up paying more in fees over the course of the year than they originally received in credit. Nationally, borrowers spend roughly $8.7 billion per year on payday-loan fees.

The United States government could put billions of dollars back into the pockets of these consumers by fixing a small regulatory problem and allowing banks to get into the business of small loans.

Currently, the Office of the Comptroller of the Currency, which regulates banks, has such stringent underwriting standards that it costs more for banks to meet the paperwork-intensive requirements than they could reasonably charge for such small sums. Indeed, the regulations have in practice (though not in rule) banned banks from offering small credit to a broad range of people. Encouraging banks to lend small sums would benefit both banks and customers.

I am in the midst of conducting research in several parts of the country with low- and moderate-income households who live paycheck to paycheck. Some of them use credit to manage fluctuations in their budgets. And they are not the unbanked — a checking account and an income are both required to secure a payday loan.

We should change the regulations so that these customers could stay in the financial mainstream and not leave banks where they already have accounts just to go borrow a few hundred dollars. The high rates and aggressive collection practices of payday lenders cause consumers to lose their bank accounts and sometimes to exit the formal banking system entirely. Well-structured small bank loans, repayable in installments, could prevent that.

While these loans will never be a big part of banks' revenue compared with mortgages and credit cards, some banks are interested in offering them. A federal regulatory framework issued by the Consumer Financial Protection Bureau this year provides an initial pathway for banks to issue loans with payments limited to an affordable 5 percent of monthly income. Some credit unions already make such loans and a survey by the Pew Charitable Trusts estimates that a $500 loan made to a typical borrower would cost about $250 in finance charges over six months. The same loan from a payday lender typically costs well over $1,000.

So far policy makers have proposed a much more complex way to address this: Let the Postal Service do it. Senator Elizabeth Warren, Democrat of Massachusetts, proposed that the post office offer low-cost financial services like small loans to compete with payday lenders, with banks supplying help on the back end. It would be "the public option" for small-scale finance, but it would require that a new infrastructure of services be built and new skills acquired. Even if the Postal Service idea could be implemented without a technological glitch, the idea has already run into political opposition.

Banks are in a stronger position both to address emergency needs quickly and to achieve scale in the business. There are nearly 100,000 bank branches in the United States, and most banks could lend to their customers through their websites, mobile platforms, A.T.M.s or automated phone systems. That would help keep down the overhead costs that are the main driver of high payday loan prices. If regulators do not require excessive underwriting and documentation procedures for loans that meet basic safety guidelines, origination costs will also be low. Losses on these loans are typically modest, because access to a customer's checking account gives lenders strong collateral. Credit unions that have offered such services have written off between just 2 and 4 percent of their loans.

By contrast, the post office does not have easy access to a person's financial history, the ability to see whether there might be the resources available to repay the loan or the wide range of platforms already available for customers to apply for and receive a loan.

When discussing financial inclusion, it is tempting to focus on people who are not considered part of the financial mainstream. But most people who use fringe financial services actually are bank customers, and we should be devising ways for them to stay in the banking system rather than creating the risk that they might fall out. Banking services should be geared to their needs, and regulations should not render large groups of middle- to low-income customers as "too small to help." If our banking system is going to become an inclusive one that works for everyone and not just the affluent, allowing banks to offer small installment credit would be a great place to start.