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Celebrating Over 40 Years of Public Service

August 3, 2018

Gerard Poliquin
Secretary of the Board
Document Number: 2018-11591
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

RE: Notice of Proposed Rulemaking (PALs II)

Dear Mr. Poliquin:

The South Carolina Department of Consumer Affairs ("SCDCA") is pleased to offer comments in response to the National Credit Union Administration Board's ("NCUA") proposed rule regarding Payday Alternative Loans (PALs) II. SCDCA is the state's consumer protection agency. Established in 1974, SCDCA is responsible for the administration and enforcement of over sixty laws, including Title 37 of the South Carolina Code of Laws, the Consumer Protection Code. Central to SCDCA's mission is protecting consumers from inequities in the marketplace by educating them and businesses on their respective rights and responsibilities.

SCDCA helps formulate and modify consumer laws, policies, and regulations; resolves complaints arising out of the production, promotion, or sale of consumer goods or services in South Carolina, whether or not credit is involved; and promotes a healthy competitive business climate with mutual confidence between buyers and sellers. Overall, SCDCA protects consumers while giving due regard to those businesses acting in a fair and honest manner. The following comments are based upon SCDCA's experience in regulating the consumer credit marketplace in South Carolina, as well as researching current trends and topics affecting consumers in this state.

Small Dollar Loans in South Carolina

Prior to 1982, the South Carolina Consumer Protection Code provided a tiered rate structure for most forms of consumer credit in the state. Creditors were allowed to impose a finance charge of 36% on very small transactions, 21% for slightly larger ones, and 15% for larger transactions, but in no case was the combined rate to exceed 18%. By 1982 high inflation rates

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coupled with a national prime rate in excess of 20% prompted the General Assembly to pass legislation deleting the usury caps and implementing a Maximum Rate Schedule in an effort to boost competition among creditors. Still in effect today, this legislation permits creditors to charge any APR with only one stipulation: creditors wanting to charge an APR of 18% or higher [1] must first file the rate with SCDCA and post it in the creditor's place of business.[2] In the decades that followed these changes in legislation, the number of persons intending to charge rates at or under 36.99% decreased while the number of those charging triple digit interest rates increased. As a result of this shift, the most frequent APR, as a weighted average, charged by supervised lenders in 2016 on loan amounts ranging from $600.01 to $1,000 was 122.33%.[3]

SCDCA appreciates NCUA's efforts to encourage federal credit unions (FCUs) to offer responsible small loan products by adding an additional PALs program. However, we encourage NCUA to cautiously approach excluding consumer protections in the PALs I program from the proposed PALs II program. Specifically, SCDCA recommends that NCUA: (1) Establish a minimum loan term and parameters for payment amounts; (2) Assess the borrower's other obligations in determining a consumer's ability to repay the loan; and (3) Establish a tracking mechanism to ensure compliance with the limit on the number of loans during the applicable timeframe.

Establish a Minimum Loan Term and Payment Amount Parameters

Based on its Small Dollar Loan Pilot Program, the FDIC concluded that 90 days is the appropriate minimum term for small dollar loans because, according to program participants, "a longer term [is] critical to loan performance because it [gives] consumers more time to recover from a financial emergency."[4] NCUA recognized the value of terms even before the FDIC's pilot program however, as evidenced by its inclusion of a 30 day loan term requirement in its PAL I program. Yet the proposed rule not only omits this 30 day minimum loan term requirement, but also increases the maximum amount that can be loaned. SCDCA understands that flexibility is necessary to expand the number of FCUs offering loans through the PAL program, but we urge NCUA to balance the need for flexibility with an equally vested interest in consumer wellbeing by setting a reasonable minimum loan term, especially where the loan amount is greater than $1,000.

While minimum loan terms help ensure that repayment amounts are set at manageable levels, they are most effective when applied in conjunction with established parameters for loan payment amounts. It is well established that payday and similar loan rollovers and renewal rates

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[1] In 1995, the General Assembly amended § 37-3-201(2) to limit the rate that can be charged on small loans of $600 or less to the same rate that restricted lenders can charge under § 34-29-140. Restricted lender rates are one of the few set by the legislature.

[2] *S.C. Code Ann.* § 37-2-201(2) (2015), *available at* http://www.scstatehouse.gov/code/t37c002.php.; § 37-3-201(2) (2015), *available at* http://www.scstatehouse.gov/code/t37c003.php.

[3] *See* 2018 State of Credit Report, *available at* http://www.consumer.sc.gov/Documents/Legal/Comments_Advocacy/2018_SOCRprt.pdf.

[4] *See* A Template for Success: The FDIC's Small-Dollar Loan Pilot Program, *FDIC Quarterly*, 2010 Vol. 4 No. 2, *available at* https://www.fdic.gov/bank/analytical/quarterly/2010-vol4-2/fdic-quarterly-vol4no2-smalldollar.pdf.

occur primarily because consumers are unable to repay large sums in a short term in light of other financial obligations. Setting repayment amounts at a capped percentage of the consumer's paycheck or deposits increases the likelihood that consumers can successfully repay the loan without incurring additional financial hardship.[5] Data shows that these two initiatives would result in fewer delinquencies and/or defaults, with the potential for increased financial stability for consumers.[6]

Assess Borrowers' Other Obligations in Ability-to-Repay Determinations

SCDCA recommends NCUA to require that ability-to-repay determinations in the PAL II program include an assessment of a borrower's other financial obligations. While guidelines are included in current regulations, consumer income is the sole basis for ability-to-repay determinations.

NCUA should require assessment of a borrower's other obligations to maximize the likelihood that loans are repaid successfully without causing additional financial distress. For example, payday lenders notoriously fail to account for existing consumer obligations which contributes to loan rollovers and renewals.[7] Were NCUA to require that other financial obligations be considered in conjunction with existing underwriting guidelines, consumers would be better situated to successfully repay a loan.[8]

Establish a Tracking Mechanism to Ensure Compliance

Prior to 2010, deferred presentment providers (payday lenders) garnered nearly one third of the small dollar loan market in South Carolina. Whereas in 2015 these lenders only represented approximately 12% of the market share. This significant drop in market share was a direct result of amendments to the South Carolina Deferred Presentment Services Act[9] (the "Act"), which became effective in 2010. Among other things, the Act limited the number of outstanding payday loans for borrowers and prohibited the use of a new loan to pay off an existing one. Notably, the amendments also increased consumer protections by establishing a single loan database for tracking transactions to ensure any loans advanced are in compliance with the statutory requirements[10] and to minimize the occurrence of consumers taking out multiple payday loans by engaging in transactions with multiple payday lenders.

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[5] *See* The PEW Charitable Trusts' Payday Lending in America: Report 2 (2013), *available at* http://www.pewtrusts.org/~/media/assets/2013/02/20/pew_choosing_borrowing_payday_feb2013-(1).pdf. *See also* The Consumer Federation of America and Center for Responsible Lending's Driven to Disaster: Car-Title Lending and Its Impact on Consumers (2013), *available at* http://www.responsiblelending.org/other-consumer-loans/car-title-loans/research-analysis/CRL-Car-Title-Report-FINAL.pdf.
[6] *See id.*
[7] *See* Center for Responsible Lending's Payday Lending Abuses and Predatory Practices (2013), *available at* http://www.responsiblelending.org/state-of-lending/reports/10-Payday-Loans.pdf.
[8] *See* CFPB's Payday Loans and Deposit Advance Products White Paper (2013), *available at* https://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf.
[9] *S.C. Code Ann.* § 34-39-10 *et seq.* (1987), *available at* http://www.scstatehouse.gov/code/t34c039.php.
[10] *S.C. Code Ann.* § 34-39-175 (Supp. 2016), *available at* https://www.scstatehouse.gov/code/t34c039.php.

The amendments were successful in this respect, as implementation of the database was followed by a decrease in the number of transactions, which dropped from approximately 4 million in 2009, to just over 1 million in 2011. By 2015, there were 876,985 reported transactions, or less than one quarter of the number of transactions entered into in 2009.[11]

Other states have also increased consumer protection by implementing databases to track all payday loans,[12] and the Consumer Financial Protection Bureau similarly approached regulation of small dollar lenders at the federal level by requiring lenders to retain records in a manner that can be "easily transmitted, analyzed, and processed by a computer program, such as a widely used spreadsheet or database program."[13]

SCDCA encourages NCUA to establish and implement a mechanism for tracking consumer loans that fall into both the existing PALs I program, and the proposed PALs II program to ensure FCUs comply with the limitations on the number of loans that consumers can obtain within the applicable timeframes. Implementing such a system is critical for the PALs II program if NCUA's final rule indeed omits the requirement that consumers be a member of an FCU for at least one month to obtain a loan under this program. Without a tracking mechanism, FCUs would have more difficulty in determining whether a consumer had an existing loan at the time of the application. A system for tracking these loans would prove beneficial to both consumers and FCUs as it deters risky financial decisions by consumers and enables FCUs to more easily comply with NCUA regulations. Furthermore, the use of such a system would prove beneficial to NCUA in evaluating the success of the program and providing necessary information for future data-driven endeavors.

Conclusion

SCDCA appreciates the opportunity to comment on NCUA's proposed PALs II program. Should you have any questions pertaining to our comments, please feel free to contact me at 803-734-4233.

Best Regards,

Carri Grube Lybarker

Carri Grube Lybarker, Esq.

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[11] *See* 2017 State of Credit Report, *available at*
http://www.consumer.sc.gov/Documents/Legal/Comments_Advocacy/2017_SOC_Rprt_FINAL.pdf.

[12] *See e.g.*, Ala. Code sec. 5—18A-13(o); Del. Code Ann. Tit. 5, sec. 286.9-100(19)(b); Wis. Stat. sec. 138.14(14); Okla. Stat. tit. 59, sec. 3109(B)(2)(b).

[13] *See* 12 C.F.R. Part 1041, Subpart D 1041.11.