

Date of Hearing: June 27, 2016

ASSEMBLY COMMITTEE ON BANKING AND FINANCE

Matthew Dababneh, Chair

SB 984 (Hueso) – As Amended May 31, 2016

SENATE VOTE: 39-0

SUBJECT: Pilot Program for Increased Access to Responsible Small Dollar Loans: extension

SUMMARY: Extends the Pilot Program for Increased Access to Responsible Small Dollar Loans (Pilot) until January 1, 2023.

EXISTING LAW:

- 1) Provides under the California Finance Lenders Law (CFL), the licensure of finance lenders, who may make secured and unsecured consumer and commercial loans. (Fin. Code Sec. 22000 et seq.)
- 2) Caps interest rates that may be charged by CFL licensees who make consumer loans under \$2,500. Those caps range from 12 % to 30 % per year, depending on the unpaid balance of the loan. (Fin. Code Secs. 22303, 22304.)
- 3) Caps administrative (origination) fees that may be charged for such loans at the lesser of 5% of the principal amount of the loan or \$50. Existing law also caps the amount of delinquency fees that CFL lenders who make consumer loans under \$5,000 may impose. Those fees are capped at a maximum of \$10 on loans that are more than 10 days delinquent and \$15 on loans 15 days or more delinquent. Existing law requires CFL lenders to prominently display their schedule of charges to borrowers. (Fin. Code Secs. 22305, 22320.5, and 22325.)
- 4) Provides that until January 1, 2018, authorizes the Pilot within the CFL. (Fin. Code Sec. 22365 et seq.) CFL licensees that are approved by the Commissioner of Business Oversight (commissioner) to participate in the Pilot are allowed to receive charges for a loan subject to an annual simple interest rate not to exceed: (1) the lesser of 36 % or the sum of 32.75 % plus the United States prime lending rate on the portion of the balance, including, but not in excess of, \$1,000; and (2) the lesser of 35 % or the sum of 28.75 % plus the United States prime lending rate on the portion of balance in excess of \$1,000, but less than \$2,500. (Fin. Code. Sec. 22370.)
- 5) States that loans under the Pilot must have a minimum principal amount of \$300 upon origination and a term not less than: (1) 90 days for loans whose principal balance is less than \$500; (2) 120 days for loans whose principal balance is at least \$500 but less than \$1,500; and (3) 180 days for loans whose principal balance is at least \$1,500. (Fin. Code. Sec. 22370 (a).)
- 6) Provides that a licensee may charge an administrative fee in an amount not to exceed 7% of the principal amount, or \$90, whichever is less, on a first loan, and 6% of the principal amount, or \$75, whichever is less, on a second or subsequent loan. A licensee may not charge an underwriting fee more than once in any four-month period, and no administrative

or underwriting fee may be charged in connection with a loan refinance unless at least eight months have elapsed, as specified. (Fin. Code. Sec. 22370 (c).)

- 7) Provides that a licensee may require reimbursement for the actual insufficient fund fees incurred due to actions of the borrower, and, may contract for and receive a delinquency fee that is: (1) for a period of delinquency not less than 7 days, \$14; (2) for a period not less than 14 days, \$20. No more than one delinquency fee may be imposed per delinquent payment; no more than two delinquency fees may be imposed during any period of 30 consecutive days. (Fin. Code. Sec. 22370 (d), (e).)
- 8) States that prior to disbursement of loan proceeds, a licensee must either offer a credit education program or seminar, or invite the borrower to a credit education program or seminar offered by an independent third party, as specified. (Fin. Code. Sec. 22370 (g).)
- 9) Requires a licensee to report each borrower's payment performance to at least one consumer credit reporting agency, upon acceptance as a data furnisher by that consumer reporting agency. A licensee that is accepted as a data furnisher after admittance into the Pilot must report all borrower payment performance since its inception of lending under the Pilot, as specified. (Fin. Code. Sec. 22370 (g).)
- 10) Requires a licensee to underwrite each loan and states that the licensee shall not make the loan if it determines that the borrower's total monthly debt service payments exceed 50% of the borrower's gross monthly income, as specified. (Fin. Code. Sec. 22370 (h).)
- 11) Authorizes a licensee who participates in the Pilot to use the services of one or more finders, as specified, and defines a "finder" as an entity that, at the finder's physical location for business, brings a licensee and a prospective borrower together for the purpose of negotiating a loan contract. (Fin. Code. Sec. 22371.)
- 12) Authorizes a finder to perform one or more of the following services for a licensee at the finder's physical location for business: (1) distributing written materials; (2) providing written factual information about the loan; (3) notifying a prospective borrower of the information needed to complete an application; (4) entering information from a prospective borrower into a database; (5) assembling credit applications and other materials; (6) contacting the licensee to determine the status of a loan application; (7) communicating a response regarding underwriting; and (8) obtaining the borrower's signature on documents. (Fin. Code. Sec. 22372.)
- 13) States that a finder may be compensated by the licensee pursuant to a written agreement between the licensee and the finder, and that the total compensation paid by a licensee to a finder may not exceed \$65 per loan, plus \$2 per payment received by the finder on behalf of the licensee for the duration of the loan, when the finder receives borrower loan payments on the licensee's behalf. (Fin. Code. Sec. 22374.)
- 14) Provides that a licensee shall develop and implement policies and procedures designed to respond to questions raised by applicants and borrowers regarding their loans, including those involving finders, and to address customer complaints as soon as reasonably

practicable. (Fin. Code. Sec. 22370 (f).)

- 15) States that the Commissioner may examine the operations of each licensee and each finder to ensure that the activities of the licensee and the finder are in compliance with the requirements of the Pilot, and specifies that in addition to any other penalty, the Commissioner may impose an administrative penalty up to \$2,500 for violations of the Pilot's requirements committed by a finder. (Fin. Code. Sec. 22377.)
- 16) Requires the Commissioner to examine each licensee that is accepted into the Pilot at least once every 24 months. (Fin. Code. Sec. 22379.)
- 17) Requires the Commissioner to file reports summarizing the utilization of the Pilot, and specifies information to be contained within the reports. (Fin. Code. Sec. 22380.)
- 18) Provides that the Pilot shall remain in effect only until January 1, 2018, and as of that date is repealed. (Fin. Code. Sec. 22381.)

FISCAL EFFECT: According to the Senate Appropriations analysis, annual costs potentially in excess of \$150,000 through 2022 to the DBO to continue administrative and enforcement activities over the Pilot, to be recovered through the authority to charge fees. To the extent the removal of the sunset date fosters growth and greater participation in the Pilot, the future costs of the Pilot could potentially increase.

COMMENTS:

This bill extends the sunset date for the Pilot to January 1, 2023.

Need for the bill.

According to the author,

Low income communities in California with low or now credit histories often struggle to gain access to traditional forms of credit. The few options available to them are often at a significant cost. In 2010 the legislature passed SB 1146 to establish a pilot program that would allow for slightly higher interest rates than currently allowed under the CFLI in exchange for consumer protections. That pilot was updated in SB 318 in 2013 and again with SB 235 in 2015. Last year the Department of Business Oversight released a report on the status of the Pilot that has shown its tremendous success in lending money to communities in need. Pilot lending increased 83 % from 2011 to 2014. Nearly half a million loans were made, and over 60% of them were made to individuals of low to moderate income. Most importantly, the DBO has reported that 60% of customers of the pilot saw their credit scores increase, and on average they have increased 355 points. This type of lending has been substantially beneficial to consumers and the lenders operating under the pilot should be allowed to continue to offer these loans to consumers.

Background.

A little over 55% of Californians have subprime credit, meaning they have credit scores below 700.¹ The Consumer Financial Protection Bureau (CFPB) has found that due to no credit files or very thin credit files one in five Americans have no traditional credit score. Couple these factors together and you have a large group of consumers that may have difficulty in getting a personal loan at a bank or credit union or attaining a low interest credit card. This is not to say that everyone in these categories will have the same level of difficulty or need. Some consumers will not need to borrow money, or may have access to credit cards though only 27% of consumers that use small-dollar credit have a credit card, compared to 61% of consumers who do not use small dollar credit.² In other surveys, 29% (majority of those surveyed) of payday loan borrowers believe, often correctly that they would not qualify for a loan from a bank or a credit card.³ Overall American consumers spent \$138 billion in fees and in interest across 26 financial products in 2014 with overdraft representing the single largest revenue category of \$23.4 billion.⁴

DBO recently released a report, *Report of Activity Under Small Dollar Loan Programs*, on the performance of the Access to Credit Building Opportunities program and the Pilot covering January 1, 2011 to December 31, 2014. The data presented in the report includes loans arranged without a finder as finder activity was very limited and not reported until 2014. The following are highlights from the report:

- Loan applications – Borrower applications increased by 58.5% over the period, from 207,092 in 2011 to 328,198 in 2014. The loan approval rate increased from 39% in 2011 to 50% in 2014.
- Aggregate principal – The annual total principal of loans made increased by 83.8% over the period, from \$97.9 million in 2011 to \$179.9 million in 2014.
- Dollar amounts – Loans made in the \$300-\$499 range fell by 42.3% over the period, from 1,518 in 2011 to 876 in 2014. Loans made in the highest range, from \$1,500 to \$2,499, increased by 106%, from 21,349 to 43,975.
- Interest rates – Of the 6,560 loans made in the \$300-\$499 range over the period, 73.9% carried an APR of 40% to 49.99 %. In the \$500-\$999 range, 43.4% carried APRs of 40% to 49.99%, while 25.2% had APRs of 35% to 39.99%. In the \$1,500-\$2,499 range, the APR distribution was more even. In that category, 42.8% of the loans had APRs of 35% to 39.99%, while 19.6% had APRs of 30% to 39.99%, 18.2 % had APRs of 40% to 49.99%,

¹ Corporations for Enterprise Development (CFED), Asset and Opportunity Scorecard, <http://scorecard.assetsandopportunity.org/latest/state/ca>

² Rob Levy and Joshua Sledge. A complex Portrait: An Examination of Small-Dollar Credit Consumers. Center for Financial Services Innovation. August 2012

³ Consumers and Mobile Finance Services 2014. Federal Reserve Board, March 2014. Pg 9

⁴ 2014 Underserved Market Size, Center for Financial Services Innovation, CORE Innovation Capitol, Morgan Stanley. <http://www.cfsinnovation.com/CMSPages/GetFile.aspx?guid=ac5235a9-a42a-434c-a26a-66a1b148b712>

and 15.6% had APRs of 25% to 29.99%.

- Delinquencies – Of the 164,300 loans made in 2014, 22.5% were delinquent for seven days to 29 days, 7.3% were delinquent for 30 days to 59 days, and 3.9% were delinquent for 60 days or more.
- Multiple loans – The number of borrowers who took out more than one loan jumped dramatically from 2011 to 2012. Since then, however, the upward trajectory has been less steep. The number went from 2,189 in 2011 to 10,804 in 2012. From 2012 through 2014, the number rose by 21.6%, to 13,136. Of the 13,136 multiple-loan borrowers in 2014, 12,999 took out two loans.
- Credit scores – The share of multiple-loan borrowers who obtained higher credit scores on subsequent loans averaged 61% annually over the four-year period. The average size of the increase for those borrowers jumped from 34 points in 2011 to 355 points in 2014.
- Loan term – In 2014, of the 164,300 loans made, 50.9% were for 360 days or more. The ratios for other terms: 120 days to 179 days, essentially 0% (only two loans); 180 days to 269 days, 20.2%; and 270 days to 359 days, 28.8 %.
- Borrower income – Of the 486,287 loans from 2011-2014, 18.4% were made in low-income neighborhoods. The ratios for other neighborhood income levels: moderate-income, 45.4%; middle-income, 21.1%; and upper-income, 4.4%. The annual low-income ratio increased from 16.6% in 2011 to 19.5% in 2014.
- Loan purpose – Of the 164,300 loans made in 2014, borrowers took out 45% (74,026) to build or repair credit. Ratios for other purposes: medical or other emergency, 18.4%; pay bills, 12.7%; consolidate debt, 5.7%; non-vehicle purchase, 5.3%; vehicle purchase, 2.7%; vehicle repair, 2.6%; other, 6.4%.

Prior and Related Legislation:

- 1) SB 1146 (Florez), Chapter 640, Statutes of 2010: Authorized California's original small-dollar loan pilot program within the CFLL, named the Pilot Program for Affordable Credit-Building Opportunities. Allowed lenders approved to participate in the pilot program to charge higher interest rates and fees on loans of up to \$2,500 than those authorized under CFLL. Required pilot program lenders to rigorously underwrite their loans, offer credit education at no cost to their borrowers, and report borrower payment history to at least one major credit bureau. Required detailed reporting of loan outcomes to DBO. Originally scheduled to sunset on January 1, 2015, but was replaced by the Pilot Program for Increased Access to Responsible Small Dollar Loans, as described immediately below.
- 2) SB 318 (Hill), Chapter 467, Statutes of 2013: Replaced the Pilot Program for Affordable, Credit-Building Opportunities with the Pilot Program for Increased Access to Responsible Small Dollar Loans. Retained several aspects of the original pilot, including the underwriting requirements, offers of free credit education, reports to at least one major credit bureau, and detailed reporting of program loan outcomes, but modified other aspects of the

original pilot program. These modifications increased the maximum interest rates and fees that pilot lenders could charge, allowed pilot lenders to originate new loans and to refinance loans more frequently than under the original pilot, and eliminated several administrative and licensing rules that were serving as bureaucratic barriers to the success of the original pilot. Scheduled to sunset on January 1, 2018.

- 3) SB 235 (Block), Chapter 505, Statutes of 2015: Expanded the activities in which Program finders could engage on behalf of Program lenders. Authorized finders to disburse loan proceeds to borrowers, receive loan payments from borrowers, and provide notices and disclosures to borrowers, as specified, and provided Program lenders with greater flexibility in the ways in which they may compensate their finders.

Suggested amendment.

Existing law requires DBO to post a report on their website, on or before January 1, 2017 summarizing the utilization of the Pilot and a recommendation on whether the Pilot should continue beyond January 1, 2023. The January 1, 2017 date was in statute based on the existing sunset date of January 1, 2018 which this bill now proposes to extend. If it is appropriate to extend the Pilot for five more years beyond 2018 it would also be suitable to be able to collect as much data as possible so that policy makers can make a determination in the future whether to extend or make permanent the pilot beyond 2023. Therefore, staff recommends that that in addition to the January 1, 2017 report, that an additional report be added for July 1, 2020. This will give policy makers additional data and provide DBO sufficient time to compile the data for the report.

- 1) Page 10, line 36 after "2017" insert "and again, on or before July 1, 2020."

REGISTERED SUPPORT / OPPOSITION:

Support

Oportun (Sponsor)
 African-American Farmers of California
 Avanza Inc. (Listo!)
 Brightline Defense Project
 California Teamsters Public Affairs Council
 California Urban Partnership
 Capitol Good Fund
 Casa Familiar
 Center for Financial Services Innovation (CFSI)
 Credit Shop
 Fathers & Families of San Joaquin (FFSJ)
 Greenlining Institute
 Hispanic 100
 INSIKT
 Latin Business Association (LBA)
 National City Chamber of Commerce
 National Federation of Filipino American Association (NaFFAA)
 National Hmong American Farmers

Nisei Farmers League (NFL)
Northern California Community Loan Fund
Otay Mesa Chamber of Commerce
Pacoima Beautiful
Pew Charitable Trusts
Salvadoran American Leadership and Educational Fund (SALEF)
Service Employees International Union (SEIU)
Silicon Valley Community Foundation (SVCF)
Silicon Valley Leadership Group
United Domestic Workers of America/AFSCME Local 3930
Western Center on Law & Poverty

Opposition

None on file.

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