

Date of Hearing: May 2, 2011

ASSEMBLY COMMITTEE ON BANKING AND FINANCE
Mike Eng, Chair
AB 336 (Dickinson) – As Introduced: February 10, 2011

AS PROPOSED TO BE AMENDED

SUBJECT: Consumer loans.

SUMMARY: Establishes standards, prohibitions and requirements on lenders that provide loans collateralized by a motor vehicle (Car title loans). Specifically, this bill:

- 1) Requires a licensee that makes a car title loan to do the following:
 - a) Provide the consumer with a disclosure that informs the consumer of the interest rate and any fees or other charges associated with the consumer loan, the consequences for defaulting on the consumer loan, and a complete amortization schedule indicating the total cost to the consumer over the life of the loan and samples of other term options.
 - b) Provide to the borrower a “High Interest Rate” disclosure in Bold Arial in at least 16 point font, all capital letters. The disclosure must be in a separate box and must be signed by the borrower and any additional cosigner, if any. The High Interest Rate Disclosure shall contain the following words: THIS IS A HIGH-COST LOAN. YOU MAY BE ABLE TO OBTAIN A LOAN FROM ANOTHER SOURCE AT A LOWER RATE OF FINANCE CHARGE. THINK CAREFULLY BEFORE YOU DECIDE TO ACCEPT THIS LOAN.
 - c) Prior to disbursement of loan proceeds, the licensee shall offer, but not require either (A) offer a credit education program or seminar to the borrower that has been previously reviewed and approved by the commissioner for use in complying with this section; or (B) invite the borrower to a credit education program or seminar offered by an independent third party that has been previously reviewed and approved by the commissioner for use in complying with this section.
 - d) Underwrite each loan to determine a borrower’s ability and willingness to repay the loan pursuant to the loan terms, and shall not make a loan if it determines, through its underwriting, that the borrower’s total monthly debt service payments, at the time of origination, including the loan for which the borrower is being considered, and across all outstanding forms of credit that can be independently verified by the licensee, exceed 50 percent of the borrower’s gross monthly income.
 - e) Seek information and documentation pertaining to all of a borrower’s outstanding debt obligations during the loan application and underwriting process, including loans that are self-reported by the borrower but not available through independent verification.
 - f) Verify the borrower's credit information using a credit report from at least one of the three major credit bureaus or through other available electronic debt verification services that provide reliable evidence of a borrower’s outstanding debt obligations.

- 2) Prohibits the structuring of a car title loan as a sale-lease-back transaction and provides civil penalties.
- 3) Provides that if a borrower defaults on a car title loan the borrower shall not owe a deficiency, nor shall the licensee request a deficiency judgment to recover any outstanding balance.
- 4) Prohibits the use of any prepayment penalty on the car title loan.
- 5) Provides that if the borrower fails to perform their obligations under the loan, the licensee shall not make any negative report to any of the national credit reporting agencies.
- 6) Requires that any advertisements used for car title loans must include the annual percentage rate (APR) of the loan.

EXISTING LAW

- 1) Provides for the California Finance Lenders Law (CFLL), administered by the Department of Corporations (DOC), which authorizes the licensure of finance lenders, who may make secured and unsecured consumer and commercial loans (Financial Code Sections 22000 et seq.). The following are the key rules applied to consumer loans made pursuant to the CFLL:
 - a) CFLL licensees who make consumer loans under \$2,500 are capped at interest rates which range from 12% to 30% per year, depending on the unpaid balance of the loan (Sections 22303 and 22304). Administrative fees are capped at the lesser of 5% of the principal amount of the loan or \$50. An administrative fee of \$75 may be charged for loans of \$2,500 or more (Section 22305);
 - b) In addition to the requirements in “a” above, CFLL licensees who make consumer loans under \$5,000 are prohibited from imposing compound interest or charges (Section 22309); are limited in the amount of delinquency fees they may impose (Section 22320.5; delinquency fees are capped at a maximum of \$10 on loans 10 days or more delinquent and \$15 on loans 15 days or more delinquent); are required to prominently display their schedule of charges to borrowers (Section 22325); are prohibited from splitting loans with other licensees (Section 22327); are prohibited from requiring real property collateral (Section 22330), and are limited to a maximum loan term of 60 months plus 15 days (Section 22334);
 - c) In addition to the requirements in “a” and “b” above, CFLL licensees who make consumer loans under \$10,000 are limited in their ability to conduct other business activities on the premises where they make loans (Section 22154); must require loan payments to be paid in equal, periodic installments (Section 22307); and must meet certain standards before they may sell various types of insurance to the borrower (Sections 22313 and 22314); and,
 - d) Generally speaking, the terms of loans of \$10,000 or above are not restricted under the CFLL.
- 2) Authorizes the licensure of finance brokers under the CFLL, and defines a finance broker as any person who is engaged in the business of negotiating or performing any act as a broker in connection with loans made by a finance lender (Section 22004).

- 3) Imposes a 36% APR on consumer credit extended to members of the military and their dependents. (10 USC Sec. 987.)

FISCAL EFFECT: unknown

COMMENTS:

A car title loan is in where a consumer borrows money against the title of their car for a specified period of time. During the loan period, the consumer continues to use their vehicle as necessary. If the consumer defaults on the loan then current law authorizes the lender to repossess the car for the costs of the loan. Car title lending in California is conducted under the CFL, under which various forms of consumer lending are authorized. The CFL does not explicitly authorize car title lending, but CFL licensees may offer these types of loans. Car title loans are subject to the provisions of the CFL, which for loans above \$2,500 no interest rate caps exist. A rate cap does not exist for any personal loan (Auto, Auto-title, personal) made under the CFL.

Car title lending has come under recent scrutiny due to recent media coverage, specifically, an LA Times article, "Title Loans' Interest Rates are Literally Out of Control" that highlighted the high interest rates on these loans and the consequences if a consumer does not pay off such a loan. The article did not point to any specific egregious acts on the part of car title lenders, but instead was making the point that car title loans under current interest rates are inherently egregious. For example, one lender mentioned in the article charged interest rates of up to 180% APR. Proponents of a 36% rate cap make a similar argument that car title lending is inherently a bad deal for consumers and that any benefits are outweighed by the risk and charges. Additionally, proponents argue that because a car title loan is securitized by the automobile, meaning the lender has less risk involved.

Industry representatives argue that the borrowers who use their service have very low credit scores and are not likely to have access to other means of credit, if at all. Additionally, they point out that while the loan may be securitized, the repossession and disposition of an automobile is a costly endeavor and such costs must be built into the costs of the loan.

What has been the effect of a 36% rate cap in other states? It appears that in states that have placed 36% rate caps on title loans and similar products that title lending has disappeared. A July 6th, 2008 from *The Oregonian*, "Oregon's payday lenders all but gone" found that "Car title lenders, which also made small, high-interest loans using car titles as collateral, have all but disappeared in Oregon."

Rates:

Obviously, both sides of this proposal disagree on whether a 36% APR cap for car title loans. Proponents argue that such lending can still take place at such a rate, while opponents argue that 36% could potentially put the industry out of business. What would a 36% APR cap look like? For a one year loan of \$2,500, the total interest charges would be \$513.86. On the same loan at 96% APR, the interest charges would be \$1,480.85. From the interest charges, the lender must cover the costs of the capital (often borrowed from a bank), labor costs, property rent for the business, and other overhead costs.

An important determining factor in this discussion is the default rates of these loans. At this time, staff has been unable to determine from neither industry representatives nor DOC, default

rates in California. The default rate may help put in context the costs associated with the loan. Additionally, it is also difficult to gauge the average car title loan amount. Under the CFL, licensees can make auto loans and car title loans, but nothing in statute requires this information to be categorized to determine which licensee is doing what type of transaction. In looking at CFL licensees who make secured car loans (This includes car title loans and car purchase loans) finds that in 2009 approximately 18,921 auto related loans were made in California with APRs over 40%, for a total volume of \$64,204,118. In 2009, for loans with APRs over 100%, 4,243 loans were made, totaling \$13, 948,175. Again, it is important to note that these numbers are approximations because an auto-purchase lender could be in these categories. Additionally, anecdotal information suggests that most car title loans are made with APRs between 90-120%.

Discussion:

This analysis is for a mock-up of language provided by the author. This mock-up represents discussions between the author, consumer groups and some industry participants. Committee staff did not receive the mock up until late in the process. At this time, it is the understanding of staff that this mock-up may not be a final version of the bill and several provisions are a product of continued controversy. It is clear that the impact of this language has not been fully vetted so staff is unable to provide a full analysis of the language.

REGISTERED SUPPORT / OPPOSITION

(Letters are for the February 10, 2011 version of the bill):

Support

Center for Responsible Lending
Consumer Attorneys of California
Consumers for Auto Reliability and Safety (CARS)
Consumers Union

Opposition

California Financial Services Association (CFSA)
Check Into Cash
Check 'n Go
Community Loans of America
Equal Access Auto Lenders of California (EAALC)

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