Payday Lending Expansion

Background

With the enactment of the Deferred Presentment Service Transactions Act (DPSTA) in 2005, the payday lending industry was permitted to operate in Michigan in exchange for regulation by the Department of Insurance and Financial Institutions (DIFS). The legislation included several consumer protections designed to curb practices that put borrowers at the highest risk of financial abuse. These protections include: licensing by DIFS, DIFS exam authority, fee limits and prohibitions on interest, a ban on rollovers, maximum advance of $600, a term from 7 to 31 days, a statewide database that all transactions must run through and limitations on the number of transactions, among others.

Michigan credit unions all too often see the negative impact on consumers of payday lending products. While credit unions offer loans of all sizes, they are required through federal regulation to calculate a borrower's ability to repay. Payday lenders are not subject to the same state and federal lending requirements that are imposed on traditional lenders. While payday lenders say their product provides a short-term lending solution for consumers, it has been found that 91% of Michigan consumers reborrow within 60 days of a previous loan being repaid. Even under the DPSTA, payday lending transactions frequently put consumers at significant financial risk, with fees often quickly accumulating for consumers without substantial financial resiliency. Short-term installment loans are so damaging to consumers, payday lenders are prohibited from operating in twelve states. Through debt consolidation, financial counseling and teaching budgeting skills, credit unions can often help a member before they descend into a debt spiral. Unfortunately, for others, bankruptcy is the only option.

The Consumer Financial Protection Agency (CFPB) is concerned about the predatory and high-cost products of state-regulated payday lenders. As a result, this federal agency proposed a new Small Dollar Lending regulation last fall that would curb the abuses of less-regulated payday lenders. Michigan should not consider increasing their loan authority when the federal government is considering ways to increase regulation on their industry.

SB 430, 431, and 432 expose Michigan consumers to predatory loan products with few consumer protections.

Senate Bills 430, 431, and 432 would establish a new regulatory act and create a new higher-dollar installment loan product with a longer term. Under the Small Loan Regulatory Act created in SB 431, a licensee would be able to offer borrowers small loans with a maximum $2,500 to be repaid within 2 years. Under the bills, licensees are required to check for any outstanding payday loans utilizing a combined database before lending to the borrower. If the borrower has any outstanding payday loans, the difference of the outstanding payday loan balance would be subtracted from the maximum amount they could borrow. These new loans could be offered at payday lender storefronts, provided it had a license under the DPSTA and the Small Loan Regulatory Act.

The consumer protections established in the legislation are inadequate. Lenders would be able to make small loans immediately after the previous loan has been repaid. Payday loans could be taken out to repay a small dollar loan and vice versa, meaning borrowers will essentially be trapped in a cycle of triple-digit loan debt. State-wide standards for calculating a borrower's ability to repay the loan are not established; rather, each licensed location could determine its own criteria for calculating the credit-worthiness of a borrower and access his or her ability to repay the loan. In the event of default, the lender would be authorized to electronically debit a borrower's account twice before contacting the borrower. If written authorization is obtained at the time of loan origination, this legislation would authorize licensees to continue electronically debiting the account. As a result, customers without sufficient funds would likely incur several overdraft fees from their traditional banking institutions.

Interest

Like payday loans, the installment product created under the Small Loan Regulatory Act puts consumers at risk of considerable economic harm. SB 431 allows the debt trap business model to continue for larger and longer loans. A $1,500 loan due in 12 months will carry a 170% APR, and a borrower will pay back double what they were lent. Less than halfway through the loan term, the lender will have collected enough in payments to cover the original loan amount. Due to indistinct language in the bills, it is unclear to the average consumer what he or she will end up paying in interest and fees over the course of the loan.

The examples below are based on the following: SB 431 will legalize loans up to $2,500 lasting up to 2 years, costing up to 180% APR. Lenders can charge a monthly finance loan charge of the aggregate of: 15% of the first $500 of the original principal loan amount; 14% of the next $500; 13% of the 3rd $500; 12% of the 4th $500; and 11% of the final $500. Payments are due in roughly equal amounts. Although language in the bill is unclear, the examples assume the finance charge is on the outstanding principal remaining. For a loan with the finance charge on the original loan amount, the APR could be as high as 265%.

30 day - $600

- Payment: $689.00
- Total Interest: $89.00
- Total Paid: $689.00
- APR: 178%

60day - $1,000

- Monthly Payment: $261.74
- Total Interest: $570.43
- Total Paid: $1,570.43
- APR: 176%

1 year - $1,500

- Monthly Payment: $267.42
- Total Interest: $1,708.80
- Total Paid: $3,208.80
- APR: 170.5%

2 year - $2,500

- Monthly Payment: $347.72
- Total Interest: $5,844.04
- Total Paid: $8,344.04
- APR: 158%

2017 Payday Lending Expansion

Michigan's current law continues to provide significant loan authority to payday lenders. Since the enactment of the DPSTA in 2005, hundreds of new payday loan store locations have opened up throughout the state, financing thousands of triple-digit interest loans. Consumer protections in SB 430, 431 and 432 are insufficient. Offering consumers higher-dollar loans with unreasonable interest rates and inadequate consumer protections preys on a vulnerable group of individuals. Michigan's credit unions are opposed to any legislation designed to expand the authority and product offerings of high-cost payday lenders. As member-owned, not-for-profit financial cooperatives, credit unions stand ready to help our members with their long- and short-term financial needs.

1. CFPB-Supplemental Findings on Payday, Payday Installment, Vehicle Title Loans, and Deposit Advance Products (2016). Web.

2. Organizations such as the National Conference of State Legislatures, the Center for Responsible Lending, Council of State Governments, and CUNA estimate that between 12-16 states ban payday lenders outright or by capping interest rates at such a point that their business model is no longer profitable.

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