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News Release

Immediate Release **March 30, 2015**

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Draft Federal Consumer Financial Protection Board Proposal to Stop the Payday Lending Debt Trap Is On Right Track but Contains Dangerous Loophole

[Charleston, WV] The Consumer Financial Protection Bureau has released a working draft of a proposal to rein in abusive, low-dollar lending schemes such as payday, auto title and installment lending. The draft, presented at a field hearing in Richmond, VA, would require that before making a loan that lenders verify that borrowers can afford to pay it back on time, without re-borrowing, and without having to skip paying for basic necessities like rent, food and utilities. Lenders could chose to ignore this principle requirement, however, by adhering to some other relatively non-restrictive standards in the proposal that are a loophole that would still allow for abusive practices. For example, short-term lenders could make up to six unaffordable loans to the same borrower, with interest rates that can average 400 percent.

This is of concern for West Virginia even though it already has some protections for borrowers. Limits on charges for check cashing and usury limits on interest rates keep out some of the worst lenders, but some lenders could use the Internet and other attempts to get around these safeguards.

Back-to-back loans are not a side effect of these kinds of loans, they are the business model. Payday, auto title and similar lenders market their products as short-term quick fixes but the average borrower winds up taking out nine loans, each with a new fee and a triple-digit interest rate.

“The Consumer Financial Protection Bureau’s proposal takes an important step toward reining in a wide range of abusive lending products,” stated David McMahon, a West Virginia attorney for low-income consumers. “It also includes a gaping loophole that puts what could be viewed as a government seal of approval on unaffordable back-to-back loans with interest rates that average near 400 percent that could target West Virginians over the Internet. We urge the CFPB and Director Cordray to reconsider and leave this loophole out of the rule.”

The principal proposed affordability standard in the proposal would require small-dollar lenders to do business the same way responsible banks and mortgage lenders claim that they operate – by making good loans.

If adopted, this simple change would go a long way toward discouraging predatory lenders from using the Internet and finding new ways to circumvent existing West Virginia consumer protections. Along similar lines, in Ohio, when payday lenders became subject to a rate cap, the lenders simply changed their names, calling themselves mortgage lenders to skirt new rules.

The principal provisions of the proposal would strengthen access to good credit for consumers who need it and give responsible lenders a fighting chance to compete, thrive and profit in a fair environment.

“As the CFPB moves forward to protect consumers, we hope that it removes the ‘look-the-other-way,’ loophole standard for the first six loans and applies a strong affordability standard to the first loan and to every loan,” continued McMahon.

“Only with consistent, airtight standards that require loans to be affordable will protections work to stop debt trap lending, keep hard-working Americans from being lured into financial quicksand, and maintain and grow a strong, responsible low-dollar loan market of responsible, West Virginia lenders,” added Linda Frame, Communications Manager with the West Virginia Center on Budget and Policy.

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The West Virginia Center on Budget and Policy (www.wvpolicy.org) is a public policy research organization that is nonpartisan, nonprofit, and statewide. The Center focuses on how policy decisions affect all West Virginians, especially low- and moderate-income families and part of the Stop the Debt Trap Campaign, which is fighting for an end to abusive lending.