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PAYDAY LENDING: STATE AND FEDERAL REGULATION

Background

According to the National Conference of State Legislatures, 38 states have specific statutes that allow for payday lending.[1] A payday loan is a short-term cash loan based on a borrower's personal check held for future deposit or on electronic access to the borrower's bank account. Lenders will hold the check until the borrower's next payday when the loan and the finance charge must be paid in one lump sum. *The Economist* states a typical payday loan is $350, with an average duration of two weeks, and costs $15 for each $100 borrowed.[2] According to a *PEW Charitable Trusts* article, an average of 12 million Americans take out payday loans each year.[3] The Consumer Financial Protection Bureau (CFPB) states the average annual percentage rate on payday loans is around 390.0 percent. Also, 4 out of 5 payday loans are rolled over or renewed within 14 days, and 20.0 percent of payday loan sequences end up in default. In 2012, data from the Kansas Office of the State Bank Commissioner (OSBC) show a total payday loan volume of $413.9 million and more than 300 payday loan locations.

Kansas

In Kansas, two state laws regulate payday lending: KSA 16a-2-404 and KSA 16a-2-405. KSA 16a-2-404 is the overarching payday lending statute. It provides the guidelines for payday loans, including finance charges. A payday loan is a consumer transaction with the following qualities: the loan amount is equal to or less than $500, the payment term is between 7 and 30 days, and the lender anticipates a single repayment. The statute also states a lender and related interest cannot have more than two loans outstanding to the same borrower at a time and no more than three loans to any one borrower within a 30-day calendar period. KSA 16a-2-405 is strictly related to military borrowers. This statute states any person who makes a loan under the provisions of KSA 16a-2-404 cannot garnish any wages or salary paid to a military borrower for service in the armed forces and must defer all collection activity when the borrower is deployed.

Both of these statutes must be read in conjunction with federal laws that impose additional restrictions with respect to rates, terms, and required disclosures on loans to military

1 NCSL. (2016, September). Payday Lending Statutes. Retrieved from http://www.ncsl.org/research/financial-services-and-commerce/payday-lending-state-statutes.aspx
2 The Economist. (2017, April). Payday Lending Is Declining. Retrieved from https://www.economist.com/news/finance-and-economics/21720297-regulators-squeeze-industry-payday-lending-declining
3 PEW Charitable Trust. (2016, May). Payday Loan Facts and the CFPB's Impact. Retrieved from http://www.pewtrusts.org/en/research-and-analysis/fact-sheets/2016/01/payday-loan-facts-and-the-cfpbs-impact

personnel and their dependents (for example, annual percentage rates [APR] on payday loans are capped at 36.0 percent for military borrowers due to the federal Military Lending Act). The federal law and implementing regulations preempt state law.

In January 2014, the Deputy Commissioner for Consumer and Mortgage Lending, OSBC, presented an overview of financial products and consumer protections to the House Committee on Financial Institutions. The Deputy Commissioner noted one of the primary responsibilities of the OSBC is to examine companies that are licensed or registered with the OSBC for compliance with state and federal laws and regulations. Payday lenders are required to be licensed with the OSBC.

The Deputy Commissioner highlighted additional applicable protections and requirements provided in other laws governing consumer credit and lending. The Deputy Commissioner noted federal law requires the finance charge and APR on payday loans to be conspicuous on the contract. Additionally, the consumer may rescind the loan by the end of the business day following the date the transaction was made. Federal law allows for an extended payment plan (EPP), but the EPP must be an amendment to the original transaction, have four equal payments or less, and cannot charge additional fees. Kansas does not have specific laws prohibiting the use of a repayment plan on a payday advance. However, a repayment plan must conform to the laws of the Uniform Consumer Credit Code (UCCC) and must be an amendment to the original transaction.

The Fair Debt Collection Practices Act (FDCPA) applies only to third-party debt collectors. The CFPB and the Federal Trade Commission (FTC) have oversight of the FDCPA. Collections are not subject to the FDCPA if the debt being collected belongs to the entity collecting the debt. Payday lenders may contact a borrower in an attempt to collect on a payday loan, or to notify the borrower the loan is coming due. However, the lender cannot commit an unconscionable act under the UCCC or the Kansas Consumer Protection Act. The Deputy Commissioner noted the common violations for payday lenders include:

- Unsigned contracts: the licensee attempts to contract without the consumer's signature;
- Payment term: the loan is made for less than 7 days or more than 30 days. The loan is not considered a payday loan under state law, and the maximum periodic finance charge is limited to 36.0 percent;
- APR: the APR is either understated or no APR is disclosed to the consumer; and
- Amount of loans: the consumer has more payday loans than allowed under law. Within a 30-day period of time, the consumer may have only 3 payday loans.

Case Law

In 2012, the Kansas Court of Appeals reversed the ruling of a district court concerning *Master Finance Co. of Texas v. Pollard,* 47 Kan. App. 2d 820, 283 P.3d 817 (2012).[4] Kim Pollard

4 *Master Finance Co. of Texas v. Pollard* Retrieved from https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&uact=8&ved=0ahUKEwieg7_V8NzWAhVnzVQKHUdTCfUQFggpMAA&url=http%3A%2F%2Fwww.kscourts.org%2FCases-and-Opinions%2FOpinions%2FCtApp%2F2012%2F20120622%2F106673.pdf&usg=AOvVaw2R2y8meLquG2FU

(Pollard) entered into a $100 payday loan contract with a 199.91 percent interest rate with Ma ter Finance Co. of Texas (Master Finance) in 2005 and defaulted on the loan. The origina lawsuit was filed in Missouri where Master Finance was granted a default judgment against Pollard in 2009. Master Finance was awarded a total amount of $1,512.72 and a post-judgment interest rate set at the contract rate of 199.91 percent. Master Finance was granted an order for wage garnishment, to which Pollard objected. After a hearing, the district court adjusted the interest rate to the Kansas statutory interest rate, ordered the parties to enter into a voluntary withholding order, and ordered Master Finance to release the wage garnishment. Master Finance appealed this ruling. The Kansas Court of Appeals found the district court exceeded its authority and reversed its findings and reissued the order of wage garnishment.

Payday Lending in Select States

Overview

Arkansas, Arizona, Connecticut, Maryland, Massachusetts, North Carolina, Pennsylvania, Vermont, West Virginia, and the District of Columbia do not statutorily authorize payday lending in their jurisdictions. Both Arizona and North Carolina allowed payday lending statutes to sunset. Arkansas repealed its statute in 2011, and the District of Columbia repealed its statute in 2007. Georgia explicitly prohibits payday lending in the state. According to Georgia's statute, Ga. Code Ann. 16-17-1, "the General Assembly declares that it is the general intent of this chapter to reiterate that in the State of Georgia the practice of engaging in activities commonly referred to as payday lending, deferred presentment services, or advance cash services and other similar activities are currently illegal and to strengthen the penalties for those engaging in such activities." New Jersey and New York essentially prohibit payday lending through their criminal usury statutes. Usury laws make it a felony to charge a borrower more than 25.0 percent APR on a loan in New York or more than 30.0 percent APR in New Jersey. Payday lending regulations in select states are described below.

Colorado

Regulations pertaining to payday lending are found in CRS 5-3.1-101 *et seq.* In Colorado, a payday lender may not lend an amount greater than $500, and the amount financed cannot exceed $500 to a consumer. There is no maximum loan term; however, the minimum loan term is six months from the loan transaction date. A lender may charge a finance charge for each deferred deposit loan or payday loan that cannot exceed 20.0 percent of the first $300 loaned plus 7.5 percent of any amount loaned in excess of $300. The lender also may charge an interest rate of 45.0 percent *per annum* for each deferred deposit loan or payday loan. If the loan is prepaid prior to the maturity of the loan term, the lender shall refund to the consumer a prorated portion of the annual percentage rate based upon the ratio of time left before maturity to the loan term.

Case Law

Two of the following cases dealt with the interaction between state law and tribal sovereign immunity and another focused on whether a certain type of transaction fits under the legal definition of a payday loan.

In the early 2000s, the Colorado Attorney General's office began receiving complaints about online payday lenders Cash Advance and Preferred Cash Loans. In 2005, the Attorney General issued investigative subpoenas to the companies. During the investigation, it was found two other Nevada-based companies did business under the names Cash Advance and Preferred Cash Loans, which both employed James Fontano (Fontano) as executive officer and director. These two companies were issued subpoenas, as well, which also went unanswered. Due to the lack of response, the trial court allowed the Attorney General to serve all those involved citations to show cause as to why they should not be held in contempt. Fontano and the two companies he directed filed motions to dismiss stating they were not connected with Cash Advance and Preferred Cash Loans. Two other companies, Miami Nations Enterprises Inc. (MNE) and SFS, Inc. (SFS), then jointly filed a motion to dismiss the proceedings against Cash Advance and Preferred Cash Loans. MNE and SFS claimed Cash Advance and Preferred Cash Loans had been incorporated by the Miami Nation of Oklahoma and the Santee Sioux Nation, respectively, and were therefore immune from any enforcement action by the Attorney General. The Attorney General then issued a request for documents indicating the relationship between the two Nevada-based companies, Fontano, the Miami Nation, the Santee Sioux Nation, MNE, SFS, Preferred Cash Loans, and Cash Advance. Fontano and the two Nevada-based companies filed a statement denying they had these documents. MNE and SFS separately filed a motion objecting to the request, stating they were not required to produce the documents based on tribal sovereign immunity. The Attorney General filed a motion to compel all parties to produce the documents; however, the trial court originally denied this motion. The trial court partially reconsidered this ruling in 2006 after the Attorney General filed the motion again. The trial court ordered MNE and SFS to produce some of the documents. MNE and SFS objected to providing further documentation. In 2007, the trial court denied the MNE and SFS motions to dismiss and determined the lending activities of Cash Advance and Preferred Cash Loans did not occur on tribal lands but in Colorado. The Colorado Court of Appeals, in *State of Colorado v. Cash Advance and Preferred Cash Loans*, 205 P.3d 389 (2008), reversed the trial court's ruling in 2008 and remanded the case back to the trial court for further proceedings. In 2010, the case reached the Colorado Supreme Court. The Colorado Supreme Court agreed with the court of appeals and remanded the case to determine whether Cash Advance and Preferred Loans were arms of the Miami Tribe of Oklahoma and the Santee Sioux Nation, respectively, and therefore entitled to tribal sovereign immunity. In 2012, the trial court concluded, in *Cash Advance and Preferred Cash Loans v. State of Colorado*, 242 P.3d 1099 (2010), the Attorney General could not enforce the administrative subpoenas based on tribal sovereign immunity. The trial court also granted the Miami Nation's and Santee Sioux Nation's motion to dismiss. The Attorney General appealed the ruling, but the Colorado Court of Appeals dismissed the appeal in *State of Colorado v. Cash Advance and Preferred Cash Loans*, No. 2012CA1406 (Col. Court of Appeals, filed Dec. 19, 2013).

A similar case, State of Colorado v. Western Sky Financial LLC., No. 11CV638 (Col. District Court, filed Apr. 15, 2013) reached a different verdict in 2012. The District Court of Denver County ruled against Western Sky Financial, LLC (Western Sky), a payday lender operated by a member of the Cheyenne River Indian Reservation in South Dakota. Western Sky made more than 200 unlicensed supervised online loans with excessive finance charges to Colorado consumers in 2010. After Western Sky failed to comply with a cease and desist order, the Attorney General filed suit. The district court ruled Western Sky was not entitled to tribal sovereign immunity and was required to pay a financial penalty to consumers.

The Supreme Court of Colorado heard *Oasis Legal Finance Group LLC v. Coffman*, 2015 CO 63, 361 P.3d 400, concerning several national litigation finance companies that provided money, typically less than $1,500, to plaintiffs with pending personal injury claims arising from events, such as automobile accidents, slips and falls, construction site injuries, and medical malpractice incidents. In exchange, the plaintiffs agreed to pay the companies a sum of money from the future litigation proceeds. This sum included the amount advanced, an additional amount based on a "multiplier" that increased with the length of time it took to resolve the claims, and various application and administrative fees. If the litigation proceeds were less than the amount due, the plaintiffs were not required to repay the shortfall. The companies contended they were asset purchases, but a state regulatory body classified them as loans. In 2015, the Supreme Court ruled these transactions were "loans" under Colorado's UCCC.

Iowa

State statutes pertaining to payday lending are found in Iowa Code Ann. § 533D.1 *et seq*. The maximum payday loan amount is $500 at any one time. The loans cannot be made for more than 31 days. The finance charge can be no more than $15 on the first $100 of the face amount of a check or more than $10 on subsequent $100 increments of the face amount of the check, or *pro rata* for any portion of the $100 face value.

Missouri

Statutes pertaining to payday lending are found in MRS 408.500 through 408.506. A payday loan cannot be more than $500 in Missouri. It must be made for a minimum of 14 days and no more than 31 days. There is no set finance charge or interest rate; however, a borrower is not required to pay a total amount of accumulated fees and interest in excess of 75.0 percent of the initial loan amount on any single loan.

Case Law

In 2012, the Supreme Court of Missouri heard the case of *Robinson v. Title Lenders, Inc*., 364 S.W.3d 505 (Mo. 2012) addressing the issue of arbitration provisions in payday loan contracts. From 2005 to 2006, Lavern Robinson (Robinson) entered into 13 separate payday loan agreements with Title Lenders. The loan agreements all contained the company's standard arbitration language, which stated arbitration would be administered by the American Arbitration Association, and indicated Title Lenders would cover the filing fees and costs for arbitration when "it would be unfair or burdensome" for the borrower to pay. The arbitration agreement indicated borrowers were waiving a jury trial or access to a class action, but it did not otherwise contain a waiver of any claims, remedies, or damages available to borrowers. Robinson sued Title Lenders in 2006, alleging its lending practices violated the Missouri Merchandising Practices Act and certain regulatory statutes. Robinson represented herself, as well as a putative class of borrowers who also obtained payday loans using Title Lenders' loan agreement form. Title Lender moved to stay the suit and compel Robinson to pursue her claims *via* individual arbitration or in the small claims division of the circuit court. However, Robinson stated Title Lenders' class waiver in its arbitration provisions rendered its arbitration agreement unconscionable and, therefore, unenforceable. She also asserted Title Lenders' class waiver would effectively immunize it from suits because attorneys would not agree to handle borrowers' cases unless a class action was available. In March 2009, the trial court granted Title Lenders' motion to stay Robinson's court case. However, the court also found the lack of class availability left borrowers without a practical remedy for their relatively small claims. The court stated the class waiver provisions were unconscionable insofar as their "practical effect affords Title Lenders immunity" from suit. Titled Lenders appealed the March 2009 judgment, but the initial appeal was dismissed and the case remanded because the trial court had not addressed one of the borrowers' declaratory-relief counts. In a judgment entered in January 2011, the trial court found it was precluded from ordering arbitration on a class basis but rather only could compel individual arbitration. The Supreme Court ruling reversed the previous decision, stating the trial court erred in finding the arbitration agreement was unconscionable based on its class waiver when it should have determined whether the agreement was enforceable.

Nebraska

Requirements pertaining to payday lending can be found in Neb. Rev. Stat. 604A.010 *et seq*. In Nebraska, the maximum payday loan amount is $500 per consumer. The loan cannot exceed 34 days. The finance charge cannot be more than $15 per $100 or *pro rata* for any part of the face amount.

Case Law

In 2016, the Attorney General of Nebraska reached a $1.6 million settlement with CashCall Inc. and Western Sky Financial LLC, who were accused of unlicensed lending and excessive interest rates. Both companies attempted to utilize tribal sovereign immunity to avoid regulation, as they claimed to be based on the Cheyenne River Indian Reservation. The settlement required the unlicensed loan companies to pay $950,000 in restitution, forgive $557,000 in debts, notify credit reporting agencies for credit history repair, and stop lending in Nebraska. The Nebraska Department of Banking and Finance would receive $150,000 as part of the settlement agreement.

Ohio

Laws concerning payday lending can be found in ORC §1321.35 *et seq*. The maximum payday loan amount is $500, and the loan must be made for at least 31 days. Interest is calculated in compliance with federal law, 15 USC §1606, and it cannot exceed 28.0 percent annually.

Case Law

In 2014, the Ohio Supreme Court found (*Ohio Neighborhood Finance, Inc. v. Scott*, 139 Ohio St.3d 536) payday loan lenders were not required to obtain licenses under the Short-term Loan Act, contained within ORC §1321. They were also allowed to be mortgage lenders under the Mortgage Lending Act, thereby allowing them to charge an APR above the 28.0 percent limit for a licensed payday lender.

Case Law

In 2009, *Hawkins v. O'Brien*, 2009-Ohio-60, which involved arbitration requirements, was brought before the Court of Appeals of Ohio. Tim Hawkins (Hawkins) had signed a contract for a payday loan with Kentucky Check Exchange (Kentucky Check) in 2006. However, when Kentucky Check went to deposit Hawkins' check, the bank stated he had closed his account. In 2007, Kentucky Check's attorney, Kevin O'Brien (O'Brien), demanded payment of the amount due and threatened to take action against Hawkins if he did not pay Kentucky Check or reach an agreement. O'Brien sent Hawkins a letter stating the amount due if a judgment was obtained would total $2,106.50. The letter further alleged Hawkins committed a theft offense by passing a bad check. Hawkins then began an action against Kentucky Check, O'Brien, and O'Brien's law firm (defendants). Hawkins alleged violations of the FDCPA, based on statements in O'Brien's letter. He also invoked rights granted by the Ohio Consumer Sales Practices Act (CSPA), as well as the right of consumers to prosecute a class action for alleged CSPA violations. The defendants filed a notice of removal of Hawkins' action to federal district court. After the federal court declined the removal request, the defendants filed a joint motion to stay the trial of the action. The motion included a copy of the written agreement between Hawkins and Kentucky Check, which contained an arbitration clause. The clause permitted small claims actions, but it required the parties to submit all claims to arbitration in any action in another forum relating to the parties' agreement and waived the consumer's right to have a court determine those claims instead. The trial court granted the defendants' motion and ordered the trial of Hawkins' action stayed until arbitration of the issues in that action was had. Hawkins then filed an appeal. The court of appeals upheld the judgment of the trial court.

Oklahoma

Requirements concerning payday lending can be found in Okla. Stat. tit. 59-3101 *et seq*. In Oklahoma, the maximum payday loan amount is $500, exclusive of the finance charge. The loan must be for more than 12 days, but less than 45 days. A deferred deposit lender's finance charge may be $15 or less for every $100 advanced up to the first $300 of the loan. For amounts over $300, the lender may charge an additional finance charge of $10 for every $100 over $300.

Federal Action

On July 21, 2010, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act into law ("Dodd-Frank Act," PL 111-203). Title X of the Dodd-Frank Act, titled the "Consumer Financial Protection Act of 2010," established the CFPB within the Federal Reserve System with rulemaking, enforcement, and supervisory powers over a number of financial products and services and the entities selling them (including payday and student loans). The law also transferred to the CFPB the primary rulemaking and enforcement authority over several federal consumer protection laws, including the Truth in Lending Act. The CFPB does not, however, have the authority to establish usury limits (such as a cap on interest rates) on payday loans. Among the provisions applicable to the use of payday loans (short-term loan products) is Title XII of the Dodd-Frank Act, the Improving Access to Mainstream Financial Institutions Act of 2010.

The CFPB evaluated rules to address the "sustained use of short-term, high-cost credit products" (various types of small-amount loans). On October 5, 2017, the CFPB issued a final rule which limits how often and how much customers can borrow with regard to payday, vehicle title, and certain high-cost installment loans. The rule requires a lender making a payday loan to reasonably determine a consumer's ability to repay the loans according to the loan's terms, exempts certain loans from the underwriting criteria prescribed in the rule if there are specific consumer protections, and requires lenders to provide notice to borrowers before attempting to withdraw payment from the borrower's bank account. The effective date of the rule is generally 21 months after publication in the *Federal Register*. The CFPB rule does not require congressional approval to take effect, but Congress could overturn the final rule under the Congressional Review Act.

The House passed HR 10, also known as the Choice Act, on June 8, 2017. This bill would ease or remove many of the financial regulations put in place under the Dodd-Frank Act. Section 733 of the bill states the CFPB may not exercise any rulemaking, enforcement, or other authority with respect to payday loans, vehicle title loans, or other similar loans. Due to the potential legislative actions of Congress, there is uncertainty concerning the future regulation of payday loans.

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