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Attacks on Payday Lending: Ballot Initiatives, Legislation, and Attorney General Enforcement

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On October 26, 2018, the Bureau of Consumer Financial Protection issued a public statement announcing that it intends to issue proposed rules in January 2019 reconsidering its Payday, Vehicle Title, and Certain High-Cost Installment Loans rulemaking. This reconsideration suggests a shift in the Bureau's attitude towards short-term lending, and lenders may be more hopeful about the future of the industry. But caution is still prudent, as recent state activity demonstrates that the fight against payday lending is far from over, with states taking aim at the industry through ballot initiatives, legislation, and attorney general actions.

Ballot Initiatives - South Dakota and Colorado

Within the last two years, the citizens of two western states approved ballot measures capping the interest rate on payday loans at 36% per annum. In November 2016, South Dakotans for Responsible Lending spearheaded a campaign to cap the interest rates on all consumer loans, including payday loans. The measure was hugely popular with South Dakota voters, garnering 76% of the votes, and ultimately resulted in the virtual elimination of the payday lending industry in the state.

More recently, in November 2018, the citizens of Colorado overwhelmingly approved a similar measure. In addition to capping annual percentage rates at 36% for deferred deposit loans and payday loans, Proposition 111 makes it an unfair or deceptive act or practice to offer, guarantee, arrange, or assist a consumer with obtaining a deferred deposit loan or payday loan with an APR greater than 36% through any method, including mail, telephone, internet, or any electronic means. This prohibition applies regardless of whether the person or entity is physically located in Colorado. As a result, Proposition 111 impacts not only "typical" payday lenders, but also bank partnerships and lead generators.

The Colorado and South Dakota ballot initiatives demonstrate that, when presented with the option, citizens are likely to approve an interest rate cap, and will do so with gusto, even when it may not be in their best interests. Approving ballot initiatives like those in Colorado and South Dakota can be detrimental to voters' actual interests, severely restricting or even eliminating the availability of credit products for less creditworthy individuals.

Legislation - New Mexico and Ohio

A few state legislatures have also passed recent legislation that either prohibits or significantly curtails short-term, small-dollar lending. In April 2017, New Mexico passed House Bill 347, which capped the annual percentage rates on loans of $5,000 or less at 175%. While a 175% APR may seem generous, the legislative move was nonetheless remarkable, given that interest rates in New Mexico were previously uncapped. Even more remarkably, the statutory amendment repealed the provisions authorizing payday lending, regardless of the rate charged by payday lenders, suggesting that legislators do not perceive high interest rates as the only negative aspect of payday lending.

In July 2018, Ohio passed a law requiring most loans of $1,000 or less with a term of one year or less to be made under Ohio's law governing short-term loans (lenders may be able to make some loans of less than $1,000 under the Ohio Consumer Installment Loan Act, provided the term is at least six months). The new law also prohibits credit services organizations from arranging credit in amounts of $5,000 or less, credit with a term of one year or less, or credit with an annual percentage rate exceeding 28%. A "credit services organization" obtains an extension of credit for a buyer or provides advice or assistance to a buyer in connection with obtaining an extension of credit, in return for the payment of money or other valuable consideration readily convertible into money. Currently, entities that traditionally offer payday loans in other states operate as credit services organizations in Ohio. These entities partner with a lender who makes loans at the rates permitted under Ohio law and arranges the transaction, taking a credit services organization fee in exchange for their services. By April 27, 2019, credit services organizations must stop all brokering activities in connection with the types of credit outlined above.

Attorney General Action - Virginia

State attorneys general have also stepped up their enforcement of high-cost lenders. For example, the Virginia Attorney General established a special Predatory Lending Unit, dedicating to tackling suspected violations of state and federal consumer lending statutes. The Predatory Lending Unit has been particularly aggressive towards online high-cost lenders, taking action against several high-cost online lenders over the last two years, alleging the lenders exceeded Virginia's 12% per annum usury rate and misrepresented that they were licensed by the state of Virginia.

The Virginia actions, similar to Colorado's Proposition 111, show that some states are also trying to regulate online lenders who are stepping in to fill the need for high-cost credit in those states that have prohibited or restricted payday lending.

What Does this Mean for You?

Despite the Bureau's declining interest in the small-dollar industry, the industry still has many obstacles to face on the state level. Given the recent flurry of state activity, it is likely that more and more state legislatures, attorneys general, and active citizen groups will take action to restrict or eliminate payday lending at the state level. Thus, members of the industry should actively monitor state legislative developments.

In states that have already taken action to curb or eliminate small-dollar lending, lenders must develop and implement plans for compliance with changes to the law. A careful review of state law, including regulatory actions and litigation, will aide lenders with tailoring existing products to meet legal requirements.

Lenders should also ensure they are complying with state and federal laws applicable to payday lending even in more industry friendly states. Running a tight ship from a compliance perspective goes a long way in showing citizens, legislators, and regulators that payday lenders are good actors, providing residents with a beneficial service.

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