

House Government Accountability and Oversight Committee
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Testimony supporting H.B. 123

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Payday and car title lenders in our state are charging unconscionable interest rates, typically 591% APR on loans of \$300 for two weeks. These lenders do this by exploiting a loophole in Ohio law, taking out Credit Services Organization (CSO) licenses to “broker” these loans, in partnership with a single lender who bears no risk, and all the while holding themselves out in their storefronts and in their advertising as making the loans themselves. Their practices are not just unethical and immoral, but also directly violate Ohio law, and yet the Ohio legislature has done nothing about them for the past ten years. The last time that this body attempted reform, the payday lenders’ lobbyists saw to it that their deceptive loan products and business practices would continue, despite the clear consensus of the citizens of Ohio that these loans should be regulated. Ohio Supreme Court Justice Paul Pfeifer probably said it best:

I write separately because something about the case doesn't seem right. There was great angst in the air. Payday lending was a scourge. It had to be eliminated or at least controlled. So the General Assembly enacted a bill, the Short-Term Lender Act (“STLA”), R.C. 1321.35 to 1321.48, to regulate short-term, or payday, loans. And then a funny thing happened: nothing. It was as if the STLA did not exist. Not a single lender in Ohio is subject to the law. How is this possible? How can the General Assembly set out to regulate a controversial industry and achieve absolutely nothing? Were the lobbyists smarter than the legislators? Did the legislators realize that the bill was smoke and mirrors and would accomplish nothing?

Ohio Neighborhood Fin., Inc. v. Scott, 2014-Ohio-2440, ¶¶ 42-43, 139 Ohio St. 3d 536, 547-48, 13 N.E.3d 1115, 1126. It seems that the Ohio House leadership is about to head down this same

path again by willfully ignoring the Credit Services Organization Act loophole and by codifying this industry's "best practices" into Ohio law.

While payday and car title lenders take out CSO licenses under R.C. 4712.01 *et seq.*, they do none of the usual CSO services, such as improving consumers' credit history or removing adverse credit information from consumers' credit reports. Payday and car title lenders do not provide, or even claim to provide, any of these services. They hold themselves out as companies that loan money and take either a personal check or a car title as collateral. CSO's are not allowed to make or collect loans under Ohio law. However, CSO's are permitted to assist consumers in obtaining an extension of credit from others. CSO's ordinarily would do this to consolidate several more expensive consumer debts into a single, low interest rate loan.

Payday and car title lenders use this "extension of credit" loophole as the basis for their unconscionable lending practices. They charge CSO fees that are far greater than the fees they could legally charge if it were licensed under Short-Term Loan Act, R.C. 1321.35 *et seq.*, the Small Loan Act R.C. 1321.01 *et seq.*, or even the Ohio Mortgage Loan Act R.C. 1321.51 *et seq.* Usually the CSO fee that is charged is greater than the principle amount of the loan that they are "brokering." This is a violation of the CSO statute which requires that CSO's disclose to borrowers that they may be charged "reasonable" fees. A fee greater than the loan amount is not reasonable by any legal standard.

Instead of directly making loans, the payday or car title lender arranges loans solely through a single lender, which usually has a license under the Ohio Mortgage Loan Act (OMLA) R.C. 1321.51 *et seq.* They do not take into account the borrower's ability to repay the loan. They take the consumer's personal check or car title as collateral on the loan and use the threat of bouncing the check or repossession to trap the borrower in a cycle of debt. The bi-weekly or

monthly payment that is owed is often a substantial proportion, or in some cases more than, the borrower's monthly income. So when the loan comes due, the borrower is unable to repay the loan in full and pay all of their other bills and expenses. The borrower must refinance, continuously rolling over the loan and incurring more fees, to avoid losing their checking account or car. The payday or car title lender provides the store fronts and advertising, provides the employees that do the paperwork, collects the payments, and contacts the borrower when there is a default.

The payday or car title lender operating as a CSO also guarantees the loans, so that if there is a default, they pay off the actual lender and collect the debt themselves, in direct violation of the CSO statute, as a CSO does not include a "person that makes or collects loans." R.C. 4712.01(C)(2)(a). Payday and car title lenders have been operating under this illegal model for a decade in Ohio. They violate the CSO statute by holding themselves out as lenders, charging unconscionable fees, and collecting the debts themselves. What legitimate lender would go through such a charade? This has meant that lower-cost, more responsible lenders have been locked out of the market while a handful of the least reputable companies thrive.

Payday and car title lenders also violate the Short Term Loan Act (STLA), R.C. 1321.35 et seq., which was adopted by the legislature in 2008 and approved by Ohio voters by a margin of 2:1. Zero short-term lenders in Ohio are licensed under the STLA. The STLA imposes an APR cap of 28% and several other requirements on the loans that high-cost short-term lenders make. The STLA specifically prohibits using a device or subterfuge to evade its requirements, precisely what payday and car title lenders do with their CSO scheme.

In accordance with the rest of Ohio's consumer finance statutes, it is critical that all short-term loans be well-regulated. In the payday and auto title loan markets in particular, where

borrowers in financial distress risk losing their checking accounts or cars, setting appropriate limits on rates and fees is a necessity. To address the churning of loans that is at the heart of these lenders' deceptive business model, the legislature must ensure that all loans have affordable payments. Borrowers also need a reasonable amount of time to repay. H.B. 123 provides fair prices, affordable payments, and enough time to repay. It closes the CSO loophole and still provides lenders with a reasonable profit. This represents a reasonable compromise between the industry's anti-consumer status quo, and an outright ban or severe restrictions on payday lending, as 15 states and the Department of Defense have already done.¹

Every week, I see clients in my office who are unable to pay back one of these loans and are suffering. They are the working poor, the elderly and the disabled, living paycheck to paycheck. They have taken out loans with the same lenders for months or even years. Offering or requiring consumer education will not fix this problem without addressing the products that are designed so trap consumers in debt. You don't give someone driver's education and then hand them a car with no brakes. The law must require that all of these products are designed to work in a reasonable and fair way. Giving an extended repayment plan once per year is not going to make this product any less defective or flawed if the payments are unaffordable. Proposals from industry that neglect the CSO lending model and policies like "free no-cost extensions," "cooling off periods," have proven to be ineffective.

This is an industry built on deceptive and unconscionable practices. Their proposed fixes, which are apparently gaining traction with house leadership, have been proven to fail time

¹ It is noteworthy that The Department of Defense reported to Congress that "...predatory lending undermines military readiness, harms the morale of troops and their families, and adds to the cost of fielding an all-volunteer fighting force." Department of Defense, Report On Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents, August 9, 2006, p. 9. www.defenselink.mil/pubs/pdfs/Report_to_Congress_final.pdf., and capped interest rates at 36% APR, prohibited securing loans with checks, electronic access to bank accounts, vehicle titles, or allotment of military pay.

and again. H.B. 123, on the other hand, will fix Ohio's laws and make the marketplace safe for Ohio's citizens and reasonably profitable for lenders. Does Ohio really need another bill that is smoke and mirrors and accomplishes nothing?