May 30, 2013

Mark Pearce
Director,
Division of Depositor and Consumer Protection,
Federal Deposit Insurance Corporation,
550 17th Street, NW

Re: FDIC FR Citation: 78 FR 25268
Proposed Guidance on Deposit Advance Products

Dear Mr. Pearce:

The Corporation for Enterprise Development (CFED) applauds the Federal Deposit Insurance Corporation (FDIC) for proposing supplemental supervisory guidance to clarify its application of principles of safe and sound banking practices and consumer protection to deposit advance products (DAPs). We appreciate the opportunity to comment on the proposed guidance and thank the FDIC for recognizing that deposit advance products can pose significant safety and soundness, compliance and other associated risks, in addition to the consumer protection risks. Please note that CFED has also submitted comments to the OCC regarding their proposed guidance on deposit advance products also issued on April 30, 2013.

Background
CFED is a national, nonpartisan nonprofit organization based in Washington, D.C. that works to expand economic opportunities for all Americans by promoting and advocating asset-building policies and programs. Our work empowers low-and moderate-income households to achieve the American dream: buying a home, pursuing higher education, starting a business and saving for the future. As a leading source of data about household financial security and policy solutions, we work with a diversity of practitioners on asset-building program design, evaluation and the dissemination of best practices; we convene researchers, policymakers and practitioners to share knowledge; and we promote research, innovation and ideas. CFED also convenes the Assets & Opportunity Network, which is a national, movement-oriented group of advocates, practitioners, policymakers and others, with over 1000 members from 49 states and the District of Columbia, working nationally to expand the reach and deepen the impact of asset building strategies. Additionally, CFED's president, Andrea Levere, is a member of the FDIC's Advisory Committee on Economic Inclusion (ComE-IN).

FDIC Proposed Guidance on Deposit Advance Products

The FDIC and others who have studied this issue—including the Consumer Financial Protection Bureau (CFPB) and nonprofits such as the Center for Responsible Lending, the Pew Charitable Trusts and the National Consumer Law Center—have noted that deposit advance products (DAPs) share many of the characteristics seen in traditional payday loans, such as high fees, short lump-sum repayment terms, and an inadequate attention to the consumer's ability to repay. In addition, like traditional payday loans, DAPs are often marketed by financial institutions as short-term solutions for unexpected or emergency financial needs. DAPs often, however, trap borrowers in a long-term cycle of debt, because of product features such as triple digit annual percentage rates (APR), extremely short repayment periods (generally 12 days) and frequently-incurred costly overdraft and non-sufficient funds (NSF) fees. The CFPB recently found that 65 percent of deposit advance customers had incurred an overdraft or NSF fee during a 12-month study, compared to only 14 percent of customers who did not use deposit advance products.[1] CFED recognizes the need for short-term small-dollar lending in the marketplace and believes that the FDIC must play an important role in ensuring that banks meet these small-dollar credit needs by providing safe and affordable products.

Underwriting and Credit Administration Policies and Practices:

CFED agrees with the FDIC's guidance that banks should consider the customer's ability to repay a loan *without* needing to borrow repeatedly from any source, including re-borrowing, to meet the repayment terms of the loan. This would not only ensure that banks minimize default risk, but ensure that consumers are not burdened with debt that they cannot reasonably afford to repay. Current underwriting standards for these loans do not take into account any other fixed and variable financial obligations, as is standard in the underwriting of traditional loan products. In aggregate, this practice could undermine the bank's deposit base and expose them to further safety and soundness risks.

Below is a list of issues that we agree should be considered when underwriting DAPs:

- The Length of a Customer's Deposit Relationship with the Bank.
  We agree with the FDIC that banks should ensure that the customer relationship is of sufficient duration, defined by the FDIC to be no less than six months, to provide the bank with sufficient information to properly underwrite deposit advance loans. Information relevant to DAP underwriting includes the customer's recurring deposits, regular expenses and income levels.

[1] CFPB. "Payday Loans and Deposit Advance Products" 2013. Available at: http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf

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- Financial Capacity.
  We strongly support the FDIC's emphasis on the need for financial institutions to assess a DAP consumer's ability-to-repay and establishing underwriting standards based on a more holistic analysis of a consumers financial capability, as is consistent with other bank loans. Because bank lenders in the DAP market are not yet subject to any federal underwriting standards, they do not employ fundamental safety and soundness bank lending practices to determine the borrower's ability-to-repay the loan and meet other necessary financial obligations.

  Banks that rely on substandard underwriting requirements—and banks that do not currently have underwriting standards for these products—to determine eligibility for these products pose a significant risk to the safety and soundness of the financial institution, while putting customers in danger of entering costly long-term debt cycles. Research conducted by the Pew Charitable Trusts highlighted that only 14 percent of payday borrowers can afford to pay off the full balance of their loan within the standard two-week period.[2] In fact, this same research found that a majority is only able to afford payments of $100 per month, which only covers the fees for re-borrowing but not paying off the principal of the loan.

  Finally, underwriting DAP loans based on a consumer's ability-to-repay will demonstrate fundamental safety and soundness-oriented lending practices that decrease banks' exposure to risks identified by the FDIC in its guidance, including such as default and credit risk.

- Cooling-Off Period.
  We strongly support the FDIC's guidance that each deposit advance loan should be repaid in full before the extension of a subsequent deposit advance loan and banks should not offer more than one loan per monthly statement cycle in order to avoid repeated use of the short-term product.

- Increasing Deposit Advance Credit Limits.
  In line with the FDIC's focus on ability-to-repay and establishing underwriting standards based on a more holistic analysis of a borrower's entire financial capability, we agree that a borrower's deposit advance credit limit should not be increased without a full underwriting reassessment. We further agree that increases in the DAP credit limit should not be automatic. Instead, they should only be initiated by a request from the borrower and only granted after the underwriting reassessment has been completed.

- Ongoing Customer Eligibility.
  We support the FDIC's guidance regarding ongoing customer eligibility, because a DAP borrower's financial capability may change many times over during the course of time, including short periods of time. Assessment of a borrower's current financial capability, no less than every six months, allows for a bank to properly underwrite subsequent loans.

[2] Pew Charitable Trusts. "Payday Lending in America: Who Borrows, Where They Borrow, And Why." 2012. Available at: http://www.pewstates.org/uploadedFiles/PCS_Assets/2012/Pew_Payday_Lending_Report.pdf

Moreover, CFED would like to provide additional emphasis to the following identified areas:

1. **Cost**

   Banks should use the FDIC's template to create affordable small-dollar loans with 36 percent APR or less.

   As the FDIC finalizes its guidance on deposit advance products it should direct its supervised banks to consider its successful pilot program on affordable small-dollar loans as a model for providing responsible small-dollar credit products for consumers.[3] The small-dollar pilot program, which has been helpful for advocates, consumers and financial institutions alike, is as a useful resource for FDIC-supervised banks as they design safe, affordable small-dollar loan products. The FDIC should direct its supervised banks to focus on the key features that were found to be critical in supplying safe, affordable and feasible small-dollar loans to consumers in a timely manner, such as 90-day loan terms, 36 percent or less APR and streamlined underwriting standards. As shown in the results of the pilot program, the template would be relatively simple to implement for banks without the need for major infrastructure investments, and would allow banks to better adhere to existing regulatory standards.

2. **Repayment**

   Banks should eliminate automatic clearing house (ACH) holding as a repayment requirement of small-dollar loans and should provide additional repayment options.

   Automatic bank withdrawals to repay DAPs are a prominent feature of bank payday loans and are generally required. Unlike a payday lender, the bank has automatic access to customer's account, and can make the withdrawals directly. This practice prevents borrowers from controlling their own bank accounts, which presents a fundamental threat to the financial security of consumers. Further, these automatic withdrawals can exacerbate financial instability by causing overdraft and NSF fees that significantly increase the total cost of borrowing. While banks often advertise their deposit advance products as a way to avoid overdraft or NSF fees, research has found that nearly two-thirds of deposit advance borrowers incurred overdraft fees and that these borrowers were two times more likely to incur overdraft fees than bank customers as a whole.[4] Banks should not force customers into automatic repayments, but instead should present automatic repayment as an opt-in option. Banks should also provide other options for repayment such as in-person or by mail.

[3] "Template for Success: The FDIC's Small-Dollar Loan Pilot Program." FDIC Quarterly Vol. 4. No. 2 (2010). Available at: http://www.fdic.gov/bank/analytical/quarterly/2010_vol4_2/FDIC_Quarterly_Vol4No2_SmallDollar.pdf.

[4] Center for Responsible Lending. "Big Bank Payday Loans." 2011. Available at: http://www.responsiblelending.org/paydaylending/research-analysis/big-bank-payday-loans.pdf

Additionally, banks should extend the minimum time needed to repay a small-dollar loan to 90 days.

Bank deposit advance products are marketed as a two-week product (the average length of a DAP being 12 days).[5] They are marketed as products designed to help borrowers meet short-term or emergency financial needs, but similar to trends in the traditional payday lending space, bank deposit advance products end up indebting consumers for a much longer period of time. On average bank deposit advance users spend 175 days–nearly six months–in bank payday debt, and often racking up additional fees and penalties over time.[6]

The FDIC small-dollar pilot found that 90 days was "the minimum time needed to repay a small-dollar loan."[7] Establishing a minimum loan term is important because the shorter the repayment period is the more likely that the borrower will have to re-borrow rather than pay back the loan in full. More than 80 percent of payday loan borrowers cannot afford to repay the loan in full at the end of the initial two-week term; once they take out a loan they effectively have no choice but to re-borrow and enter a cycle of debt.

3. **Repeat Usage Controls**

Banks should provide small-dollar borrowers installment repayment options, which are easy to qualify for or obtain, prior to the disbursement of a loan.

Banks that are providing bank deposit advance products typically include safeguards against long-term, repeat usage such as installment payments or "cooling off" periods. However, research has found that these safeguards, as designed, are often ineffective and are difficult to qualify for or obtain.[8] For example, one financial institution's payment plan allows payments in $100 increments instead of withdrawing the entire balance at once, but it is available only *after* a borrower had already been in deposit advance debt for three consecutive months and had at least $300 in bank payday debt outstanding. In order to address this issue the FDIC should direct its supervised banks to offer closed-end deposit advance loans, rather than the current open-end standard and should provide customers with clear and easy access to affordable installment payments.

Additionally, banks should implement effective "cooling off" periods that can prevent customers from incurring unsustainable debt.

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[5] CFPB. "Payday Loans and Deposit Advance Products". 2013. Available at: http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf; Center for Responsible Lending."Triple-Digit Danger: Bank Payday Lending Persists." 2013. Available at: http://www.responsiblelending.org/payday-lending/research-analysis/Triple-Digit-Bank-Payday-Loans.pdf

[6] Center for Responsible Lending. "Big Bank Payday Loans." 2011. Available at: http://www.responsiblelending.org/paydaylending/research-analysis/big-bank-payday-loans.pdf

[7] "Template for Success: The FDIC's Small-Dollar Loan Pilot Program." *FDIC Quarterly* Vol. 4. No. 2 (2010). Available at: http://www.fdic.gov/bank/analytical/quarterly/2010_vol4_2/FDIC_Quarterly_Vol4No2_SmallDollar.pdf.

[8] Center for Responsible Lending. "Triple-Digit Danger: Bank Payday Lending Persists." 2013. Available at: http://www.responsiblelending.org/payday-lending/research-analysis/Triple-Digit-Bank-Payday-Loans.pdf

"Cooling off" policies currently implemented by banks offering deposit advance products are ineffective and offer little safeguards for the borrower against repeat usage. Some of these "cooling off" periods do not go into effect until the customer has already been in a sustained level of deposit advance debt, with some banks allowing up to six consecutive months *before* a "cooling off" period is instituted.[9] The FDIC should direct its supervised banks to implement effective "cooling off" periods that can prevent customers from incurring unsustainable debt.

4. **Marketing and Access**
Banks should be more prudent in the marketing of their small-dollar loans and should clearly inform the customer that their short-term, small-dollar loans carry long term associated risks as well as inform customers of less expensive alternatives.

DAPs are marketed as providing much-needed, quick and easy credit to customers who are facing unexpected hard times. However, research has shown that 69 percent of first-time payday borrowers, which includes traditional and bank payday lending, used the loan to cover recurring expenses, such as utilities, credit card bills, rent or mortgage payments, or food. In fact, only 16 percent used these products for unexpected expense, such as car repairs or emergency medical expenses.[10] In effect, by marketing DAPs as short term products, banks are taking advantage of the borrower's need for a cash infusion and the trust they have in the bank. While banks do provide warnings that DAPs should not be used as long-term credit, it is not clear that the customer is made equally aware of less expensive alternatives.[11] The FDIC should direct its supervised banks to clearly inform the customer that short-term, small-dollar loans carry long term risks, and also inform customers of less expensive alternatives.

Furthermore, engaging in practices that are perceived to be unfair or detrimental to customer can cause a bank to lose community support and business, thus ultimately exposing them to reputational risk. Due to the similarities between deposit advance products and traditional payday loans media reports have frequently use terms like "predatory" or "debt trap" to describe these products in the press.[12]

[9] Center for Responsible Lending. "Triple-Digit Danger: Bank Payday Lending Persists." 2013. Available at: http://www.responsiblelending.org/payday-lending/research-analysis/Triple-Digit-Bank-Payday-Loans.pdf
[10] Pew Charitable Trusts. "How Borrowers Choose and Repay Payday Loans" 2013. Available at: http://www.pewstates.org/uploadedFiles/PCS_Assets/2013/Pew_Choosing_Borrowing_Payday_Feb2013.pdf
[11] Center for Responsible Lending. "Triple-Digit Danger: Bank Payday Lending Persists." 2013. Available at: http://www.responsiblelending.org/payday-lending/research-analysis/Triple-Digit-Bank-Payday-Loans.pdf
[12] Center for Responsible Lending. "Bank Payday Lending: Overview of Media Coverage and Public Concerns" (2013). Available at: http://www.responsiblelending.org/payday-lending/tools-resources/BPD-media-coverage-3-7-13.pdf

Additionally, banks should restructure how they allow customers to access these products in order to prevent high cost credit from going to customers who cannot afford to take on this type of debt.

In one study, borrowers expressed trust in the bank and the belief that DAPs are more regulated that other payday products, while others cited the temptation of having loans that were "too easy" to obtain as a reasons for using these products.[13] As noted in the guidance, customers are alerted to the availability of these products through advertisement at branches, by direct mail, ATMs, or by a "button" or hot link on their personal account webpage. The FDIC should direct its supervised banks to be more prudent in the marketing and access for these loans, since some marketing is causing significant harm to unsuspecting and susceptible customers who may be unable to repay a deposit advance within the original period.

Thank you for the opportunity to comment on the agencies' proposed guidance. CFED appreciates the FDIC's recognition that there is a need for responsible short-term, small-dollar lending in the market and we thank you for highlighting that shared viewpoint in your guidance. If banks structured their deposit advance products responsibly and properly, in line with the small-dollar guidance and pilot program developed by FDIC, they can provide borrowers with safe and affordable small-dollar loans that enable customers to move away from other high-cost, small-dollar loan products.[14] We encourage the FDIC to finalize this guidance in a manner that reflects the strong consumer focus of this proposal.

Sincerely,

Jeremie Greer
Director, Government Affairs

[14] FDIC. "Affordable Small-Dollar Loan Products Final Guidelines". (2007). Available at: http://www.fdic.gov/news/news/financial/2007/fil07050a.html