Online Lenders Alliance

May 30, 2012

Submitted via email: comments@fdic.gov; regs.comments@occ.treas.gov

Legislative and Regulatory Activities Division
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Mr. Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429

Re: Proposed Guidance on Deposit Advance Products
Docket ID OCC-2013-0005
Docket ID FDIC-2013-0043

Ladies and Gentlemen:

Online Lenders Alliance ("OLA") respectfully submits this comment letter in response to the Proposed Guidance on Deposit Advance Products set forth in the above-referenced dockets. For the reasons outlined below, OLA opposes the Proposed Guidance and urges that the Proposed Guidance be withdrawn.

OLA and its Interest in Commenting on this Rulemaking Proceeding

OLA represents the growing industry of companies offering online consumer short-term loans and related products and services. OLA's members include online lenders, as well as vendors and service providers to lenders, such as consumer reporting agencies. OLA members are subject to federal consumer protection requirements. In addition, OLA member companies have agreed to Best Practices and a Code of Conduct developed by OLA that goes beyond compliance with existing legal requirements to ensure that consumers are fully informed and fairly treated.

Some, but not all, of the loans made by OLA's members constitute "payday loans."[1] None of OLA's members is regulated by the OCC or FDIC. To the contrary, OLA's members compete

[1] Within the meaning of 12 U.S.C. § 5514(a)(1)(E).

indirectly with depository institutions in the consumer credit market, including with those institutions engaged in deposit-advance credit. The adoption of the Proposed Guidance would likely benefit OLA's members by reducing competition in the liquidity lending market. Notwithstanding this potential commercial benefit to OLA's members, OLA opposes the Proposed Guidance because it is based on poor theory, represents bad policy and would be harmful to consumers.

The Proposed Guidance would adversely affect banks' ability to continue offering deposit-advance services by significantly reducing eligibility and imposing draconian (relative to the size of the loan) underwriting requirements for such credit. Specifically, the Proposed Guidance would:

- Require that the applicant have had a deposit account with the bank for at least six months;
- Render applicants with any delinquent or adversely classified credits ineligible;
- Require each deposit-advance loan to be repaid in full before a subsequent loan is made;
- Limit borrowers to one loan per monthly statement cycle;
- Impose a cooling-off period of at least one full monthly statement cycle after repayment of a loan before another loan is made;
- Preclude an increase in a customer's deposit-advance credit limit without a full underwriting assessment, and only at the specific request of the borrower; and
- Require that the bank reevaluate the customer's eligibility and capacity for the product at least every six months and identify risks that could negatively affect the customer's eligibility, such as repeated overdrafts.

The principal motivation for the Proposed Guidance appears to be consumer protection:

> The combined impact of an expensive credit product coupled with short repayment periods increases the risk that borrowers could be caught in a cycle of high-cost borrowing over an extended period of time. Specifically, deposit advance customers may repeatedly take out loans because they are unable to fully repay the balance in one pay period while also meeting typical recurring and other necessary expenses ….[2]

As some academic commenters have noted, a significant portion of the growth of so-called "alternative" financial services since the beginning of the recent credit crisis is attributable to regulatory activity that has increased the cost of, and reduced access to, preferred credit products such as home equity loans and credit cards. For example, following the enactment of the Credit

[2] OCC Proposed Guidance, 78 Fed. Reg. 25,353, 25,354-25,355 (Apr.30, 2013); FDIC Proposed Guidance, 78 Fed. Reg. 25,268, 25,270 (Apr. 30, 2013).

CARD Act of 2009,[3] which limits the ability of lenders to adjust terms when cardholders become riskier, higher-risk borrowers receive fewer offers of credit (and, if they do receive offers at all, they are on less-favorable terms) than prior to the enactment of the law.[4]

Against this backdrop, it is easy to appreciate how well-intentioned regulatory enactments — including the Proposed Guidance — may have the unintended consequence of reducing the supply of "good" credit and driving constrained borrowers to inferior substitute forms of credit, such as late payment of bills or overdrawing their deposit account.

It is therefore important to scrutinize carefully the asserted theoretical bases for regulatory steps, such as this one, that will manifestly reduce the supply of consumer credit.

In this comment letter, we explain why the safety-and-soundness concerns about this product are unfounded; address a similar lack of basis for the consumer protection concerns; and discuss the expected adverse consequences to consumers of losing access to this form of credit.

Safety-and-Soundness Issues

To the extent that the Proposed Guidance invokes safety-and-soundness concerns, the proposals lack any comprehensive analysis showing how a depository institution's soundness would be adversely affected by the continued offering of deposit-advance products on a historical basis. Neither the Proposed Guidance nor any regulatory or academic study suggests that deposit-advance credit comprises a material portion of any depository institution's business, nor of the industry as a whole. Indeed, there are no empirical data from any source that would lead to the conclusion that deposit-advance credit poses a threat to safety and soundness. No examples of actual harms or material losses sustained by any depository institution presently in this market are cited. Quite to the contrary, for those institutions which offer this form of credit, the results seem exclusively salutary, when measured in traditional terms such as credit losses, profitability and litigation costs.

Reputation risk is more difficult to assess, but to date the actual results from banks' offering of the service appear equally salutary. Deposit-advance services provide credit to an underserved market and one where constrained consumers lack superior alternatives. Providing such access furthers an important federal policy goal embodied in the Dodd–Frank Wall Street Reform and Consumer Protection Act.[5] Indeed, it could be argued that the failure to offer such products would do more to harm the reputation of depository institutions than continuance of existing programs. For a credit product that has been in existence for as long as deposit-advance

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[3] Pub. L. No. 111–24, 123 Stat. 1734, 1736 (2009).

[4] *See, e.g.*, American Financial Services Association, Response to Request for Information Regarding Credit Card Market (Feb. 19, 2013), available at http://www.afsaonline.org/library/files/legal/comment_letters/AFSA-InformationonCreditCardMarket-DocketNo.CFPB-2012-0048.pdf (last visited May 17, 2013).

[5] *See* 12 U.S.C. § 5511.

programs have, one would expect that some of the potential safety-and-soundness harms theorized in the Proposed Guidance would have materialized by now.

Consumer Protection Concerns

The principal consumer protection basis for the Proposed Guidance appears to be the contemporaneous report by the Consumer Financial Protection Bureau, "Payday Loans and Deposit Advance Products: A White Paper of Initial Data Findings," dated April 24, 2013 (the "White Paper").[6]

The White Paper is careful to emphasize that the Bureau has studied only consumer usage, not consumer welfare outcomes; and the Bureau notes that additional study will be required to determine whether and to what extent consumers may be harmed as a result of the use of these products. Indeed, the Bureau presently has projects underway intended to elicit precisely such information.

The Proposed Guidance, however, elides the Bureau's caution on this topic and concludes, without an evidentiary basis, that the risk of consumer harm from use of deposit-advance products exceeds the benefits provided by the products. This is poor economic science and worse regulatory policy.

We believe that the leading scholars on the use of similar products — who have concluded that that "restrictions [on short-term lending] could deny some consumers access to credit, limit their ability to maintain formal credit standing, or force them to seek more costly credit alternatives"[7] and that "the long-run effect of payday borrowing on credit scores and other measures of financial well-being is close to zero" — would agree with us.[8]

Nor is there evidentiary support for the notion, as asserted in the Proposed Guidance, that borrowers may be "caught in a cycle" of debt because of the high-cost nature of the product. To the contrary, borrowers do not get "caught" in high-cost debt with any greater propensity or duration than in lower-cost (or interest-free) debt.[9]

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[6] Available at http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf (last visited May 17, 2013).

[7] Edmiston, Kelly D., Could Restrictions on Payday Lending Hurt Consumers? (April 2011) (finding that States where payday lending is banned have a higher share of consumers with low credit scores and histories of late bill payments), available at http://www.kansascityfed.org/publicat/econrev/pdf/11q1Edmiston.pdf (last visited May 17, 2013).

[8] Bhutta, Neil, Skiba, Paige Marta and Tobacman, Jeremy Bruce, Payday Loan Choices and Consequences (Jan. 25, 2013). Vanderbilt University Law School Law and Economics Working Paper No. 12-30, available at http://ssrn.com/abstract=2160947 (last visited May 17, 2013).

[9] Fusaro, Marc Anthony and Cirillo, Patricia J., Do Payday Loans Trap Consumers in a Cycle of Debt? (Nov. 16, 2011), available at http://ssrn.com/abstract=1960776 (last visited May 17, 2013).

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Finally, there is no support for the notion implicit in the Proposed Guidance that consumers are misled into taking out short-term debt that, to their surprise, turns out to be long-term in nature. Borrowers of these loan products generally repay after a number of renewals that comports extremely well with their ex ante expectations.[10]

In summary, neither the White Paper nor any other research of academic quality supports the imposition of the restrictions set forth in the Proposed Guidance in the interest of consumer protection.

Consumer Harm From Loss of Access to Deposit Advance

Bank deposit-advance services are generally the lowest-cost, and arguably the most intensely regulated, form of short-term, small-dollar unsecured consumer credit available in the market. The unavailability of this product would not address the underlying issues of consumers who are financially constrained, with poor or "thin" credit histories, and limited other resources. Substantially restricting the supply of this product will not reduce the demand for it.

Loss of access to this product would deny consumers an extremely favorable form of borrowing. If such consumers are unable to borrow from banks and lack access to online credit, they may have to rely on inferior substitutes, such as higher-cost overdraft protection and missed payments (with attendant late-payment penalties).

A logical consequence of the Proposed Guidance is that depository institutions which currently provide deposit-advance services will no longer do so. The Proposed Guidance imposes requirements that will hasten the retreat of banks from providing small-dollar consumer financial services and will serve to entrench existing non-bank lenders. Despite the interest of OLA's members in having this market to themselves, there can be no gainsaying that these factors will harm competition and harm consumers.

Access to credit is important and beneficial to consumers — perhaps particularly so with respect to consumers with limited liquidity.[11] If the regulatory concern is that deposit-advance credit is too expensive for consumers, then the solution is to increase the supply of credit, not to decrease it, as this Proposed Guidance inevitably will.

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10 Mann, Ronald J., Assessing the Optimism of Payday Loan Borrowers (March 12, 2013), Columbia University School of Law, Center for Law and Economic Studies Working Paper No. 443, available at http://ssrn.com/abstract=2232954 (last visited May 17, 2013).

11 *See, generally*, Edmiston, Kelly D., Could Restrictions on Payday Lending Hurt Consumers?, *supra* note 7.

Neither the consumer protection nor safety-and-soundness grounds for the Proposed Guidance have any meaningful evidentiary support. Most importantly, there is no evidence that the potential harms from the use of deposit-advance services outweigh the benefits to consumers of such services. Additional study of these issues should be undertaken and concluded prior to the imposition of any sea-change regulation such as that under contemplation now. The Proposed Guidance itself will inflict real and substantial harms on consumers by eliminating a low-cost source of credit and forcing consumers to substitute inferior sources of credit.

It does not appear that the agencies have contemplated other, less restrictive, means of accomplishing the objectives of the Proposed Guidance. Such means may consist of consumer financial education, better disclosures, mandatory principal reductions or other modest changes in product design. While the full scope of such possible changes in design is beyond the scope of this letter, the interests of consumer welfare demand that any perceived shortcomings with the deposit-advance product be addressed in a manner that does not materially reduce the supply of available credit to middle-income consumers — a near-certain outcome if the Proposed Guidance becomes final.

For all of the foregoing reasons, OLA opposes the Proposed Guidance and urges that the Proposed Guidance be withdrawn.

Thank you again for the opportunity to comment on the Proposed Guidance. If you have questions or would like additional information, please feel free to contact me at LMcGreevy@onlinelendersalliance.org.

Very Truly Yours,

Lisa McGreevy

Lisa S. McGreevy
President and CEO

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