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CFPB Payday Rules Are Win-Win for Lenders and Consumers

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By Ken Rees – April 6, 2016

The Consumer Financial Protection Bureau is about to issue new rules that will define the future of small dollar and non-prime lending in our nation. Almost everything the CFPB has done to date has been controversial, prompting strong responses from consumer advocates, members of Congress and the industry. Likewise, the debate around the upcoming rules — which will affect payday, auto title and other small-dollar credit products — has been especially contentious.

Many groups are calling for lengthy delays to the CFPB's rules to allow for further analysis and review. Yet, for the benefit of millions of Americans who rely on non-prime credit and the thousands of lenders that provide it — including my company — the clarity and consumer protections offered by a new CFPB regulation can't come soon enough.

The last few decades of rising income inequality as well as the Great Recession have "hollowed out" the middle class. This has led to reduced savings, declining household income and rising income volatility resulting in a dramatic downward shift in credit scores and access to traditional forms of credit. In fact, there are now 160 million American adults who have credit scores less than 700 (the cutoff for "prime" quality credit) or no credit score at all — more than the number of Americans with prime credit. And at the same time, banks have continued to tighten credit standards and have eliminated nearly $150 billion in credit availability to non-prime households.

As a result, more Americans than ever before are using alternate credit products like payday loans, pawn, title loans and even bank overdrafts to cover their credit needs. Unfortunately, while technology and advanced analytics have created a new breed of credit products in many areas of financial services for prime consumers, the massive but underserved market for non-prime credit continues to be served mainly by storefront lenders — often with punitive pricing and extremely aggressive collections practices.

The lack of clear federal regulation of nonbank lenders has perpetuated many bad lending practices and has warded off needed innovation and new products. Usually a huge, unmet consumer need is filled by new entrants. However, given the level of ambiguity over federal regulations for several years, few entrepreneurs have been willing to invest in innovating new, more responsible credit solutions for non-prime consumers.

In this environment, the CFPB has been laboring to develop rules that will eliminate "unfair, deceptive and abusive" practices while maintaining access to responsible credit for the millions of non-prime Americans who rely on it when they face unexpected bills, auto repair, or health care emergencies.
In fact, all of the preliminary ideas proposed by the CFPB make sense and will ensure better outcomes for the consumers of these products. (Note that the CFPB can't change the pricing of the products since the Dodd-Frank Act specifically precludes the bureau from setting rate caps.)

These include having lenders improve how they assess a borrower's "ability to repay" to determine affordability rather than rely on aggressive debt collection practices, such as suing customers or taking title to a customer's car to ensure repayment of the debt. With the vast range of new data sources and analytical techniques now available to lenders, there is no excuse for poor underwriting or outdated debt collection approaches.

The CFPB rule could also specifically target abusive ACH processing. Most non-prime credit (especially from online lenders) is repaid via ACH. This is convenient and actually preferred by consumers as well as cost-effective for lenders, but if abused can cause excessive charges to customer bank accounts. The CFPB wants to ensure that consumers know their rights to rescind the ACH authorization and for lenders to limit the number of times they re-present a payment that has been returned for non-sufficient funds. This is a very simple, common sense change that will reduce consumer harm and prevent excessive bank charges.

But more broadly, implementing the proposed CFPB rules could provide this industry with the regulatory stability necessary to encourage more innovation and competition. With more options and adequate protection from the bad players with antiquated lending practices, consumers in desperate need of better non-prime credit products will have something they have lacked for decades: responsible, competitively-priced choices.

Will the upcoming rules make everyone happy? Absolutely not. Consumer groups will likely decry the rules as insufficient and lenders will declare that the rules are unfair and a burden on their business practices. Certainly, I have concerns that the rules may be more complicated than absolutely necessary and make implementation unwieldy. However, despite the noise from both sides of the issue, the CFPB has actually been very transparent. They have engaged extensively with consumer groups, lenders and consumers to guide their policymaking.

There is an urgent need to implement thoughtful regulations that create a balance between access to credit and protections against predatory lenders. I feel strongly that the upcoming CFPB regulations will help both consumers and lenders and should be expedited without any further delays. A protracted debate will only delay what is truly necessary: regulations now.

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