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ILLINOIS BANKERS ASSOCIATION
Connecting Bankers. Advancing Banking.

October 7, 2016

Via Electronic Delivery to FederalRegisterComments@cfpb.gov

Ms. Monica Jackson
Consumer Financial Protection Bureau
1700 G Street NW
Washington, D.C. 20552

Re: **Docket No. CFPB-2016-0025**; **RIN 3170-AA40**
Proposed Rule on Payday, Vehicle Title and Certain High-Cost Installment Loans
81 Federal Register 47863 (July 22, 2016)

Dear Ms. Jackson:

The Illinois Bankers Association ("IBA")[1] is writing on behalf of its members to comment on the CFPB's proposed small dollar lending rule. We appreciate the Bureau's efforts to protect consumers from the threats posed by predatory nonbank lenders who trap consumers into harmful cycles of high-cost debt. However, we respectfully disagree with the proposed application of the Bureau's rule to federally insured depository institutions. While consumers would be far better served if financial institutions were to expand their small dollar lending programs (which have been contracting in recent years due to increased regulatory concerns), the proposed rule effectively would disincentivize the vast majority of them from actively participating in this market at all.

If financial institutions are required to comply with the elaborate requirements of the proposed rule (including its three elaborate exemptions), this important source of credit for many consumers will be severely restricted, leaving them with few choices other than resorting to the same unscrupulous lenders that have proliferated across the country in recent years, sometimes online and sometimes directly across the street from a bank branch. These are the same "shadow" lenders that have been skirting federal and state consumer protection laws with great success to date, often by simply declaring bankruptcy when they are caught (if they are caught) and then beginning anew. Highly regulated financial institutions should be encouraged to serve their customers and communities with responsible small dollar lending programs. The proposed rule in its current form will have the exact opposite effect.

Banks Are Making Responsible, Affordable Small Dollar Loans in Their Communities

The local economies in many Illinois communities remain relatively anemic, particularly in rural areas, and consumers often need small dollar loans in this environment to cover unexpected expenses. Frequently, these consumers have low credit scores due to myriad circumstances, and they turn to payday lenders, title lenders and other nonbank lenders. Not infrequently, these consumers ultimately approach their local bank for assistance after becoming mired in an expensive cycle of debt with one of those nonbank lenders. When banks are able to extend small dollar loans to these customers, the

[1] The Illinois Bankers Association is a full-service trade association dedicated to creating a positive business climate that benefits the entire banking industry and the communities we serve. Founded in 1891, the IBA brings together state and national banks and savings banks of all sizes in Illinois. Over 30% of IBA members are community banks with less than $100 million in assets, and over 60% of IBA members are community banks with less than $250 million in assets. Collectively, the IBA represents nearly 90% of the assets of the Illinois banking industry, which employs more than 100,000 men and women in over 5,000 offices across the state.

accompanying costs and risks for consumers are much lower, and the cycle of debt related to the same original loan is eliminated. Customers in desperate situations appreciate their bank's willingness to work with them, and they feel more secure borrowing from the same people with whom they bank for their other needs.

Banks know their customers — and their limits. Under the watchful eyes of their safety and soundness examiners, banks have found that they can underwrite these loans responsibly and quickly to meet their customers' often urgent needs. For example, banks will start by simply talking to their customers about their financial problems. Then they will verify a loan applicant's employment and length of employment, consider past performances on other loans with the bank, and sometimes require borrowers to take financial education classes. But banks generally do not – and should not – perform full affordability analyses for these loans. They have an understanding of their customers beyond algorithms, and their existing underwriting methods result in extremely low delinquencies and losses for these loans.

Banks offer small dollar loans at much lower costs than other lenders covered by the proposed rule. In most cases, banks make small dollar loans as an accommodation to their customers and as a service to the bank's community. Usually they just break even on these loans, due to the high costs of underwriting small loan amounts, which commonly are $1,000 or less, and often are less than $500. The loan origination fees that they do charge are reasonably designed to cover related expenses like credit and title reports, coupon book printing, employee time, and less frequently, credit insurance. The use of leveraged payment mechanisms targeted by the proposed rule, such as automatic monthly debits of existing accounts, also help to keep the costs down and provide customer convenience.

The Proposed Rule Is Overly Complex, and the Exemptions Are Inadequate

The proposed rule's 1,341 pages of new requirements present a grave threat to the existing small dollar lending programs of financial institutions. Simply put, most banks will not be able to provide small dollar loans under either the ability-to-repay requirements or any of the three exemptions. Minor clarifications will not be enough. Most financial institutions simply do not have the resources to establish new compliance programs to implement and monitor expansive new requirements for loans that have never been and are not designed to be profitable in the first place.

The ability-to-repay requirements and all three loan exemptions are loaded with complex requirements for underwriting small dollar loans, with specific prescriptions for information gathering, income and expense calculations, documentation, verification, and recordkeeping (all of which easily could result in technical violations or misinterpretations of the requirements). These requirements not only will eliminate the possibility of any profits for a prospective bank lender, they also will scare off borrowers, who typically need a quick turnaround to meet their urgent needs, rather than intense scrutiny of their financial lives through an inordinately long underwriting process in a time of crisis.

All three of the proposed rule's exemptions require heavy documentation, significant staff time, and disproportionate compliance costs. In order to make an exempt short-term loan, banks would need to demonstrate and document that they had reviewed the applicant's borrowing history, pulled at least one credit report, checked for existing loans with other lenders, ensured compliance with limits on loan amounts and other loan term restrictions, and more. To make an exempt longer-term loan, banks would need to familiarize themselves with the NCUA's Payday Alternative Loan Program requirements, plus additional requirements layered on top of those, or else operate under a separate set of complex requirements — all topped off with a requirement to track and maintain no more than a 5% portfolio default rate. Moreover, the 5% portfolio default rate requirement is particularly problematic; banks that make just a handful of small dollar loans each year (19 or fewer) would need to ensure that *zero* defaults occur in order to remain under the 5% ceiling, while also upgrading or restructuring their loan tracking systems, which currently do not break out loans in the categories required by the proposed rule.

In addition, the exclusion for longer-term loans with a 36% "all-in" APR is unworkable. It would greatly increase compliance costs and pitfalls, because its calculation differs significantly from the general Truth-in-Lending Act APR calculation. With banks barely breaking even on small dollar loans, they often must charge fees that cause the APR calculation to exceed 36% just to cover their costs (the notion of issuing a loan that was underwritten to incur a loss is inconceivable under contemporary safety and soundness standards). For small loans under $500, permissible fees under the proposed rule are extremely low — for example, a $300 loan with a term of three months would be limited to $20 in total fees, yet the credit report fee alone easily could exceed that amount.

In other words, those banks determined to continue making small dollar loans under the proposed rule would be faced with untenable options: (a) making the loans at a loss, (b) unnecessarily placing customers into higher loan amounts or longer term loans in order to reduce the APR, (c) restricting the use of leveraged payment mechanisms (which customers often prefer to use), or (d) removing security interests in vehicles (which help control costs by reducing collection risks).

Conclusion

The IBA and its member banks genuinely hope to see the Bureau's final rule curb the irresponsible and predatory lending practices of the many small, fly-by-night lenders. But extending its reach to highly regulated, federally insured depository institutions would harm consumers by pushing most responsible lenders out of the small dollar loan business altogether, removing an important source of credit for consumers and leaving them without responsible and affordable alternatives.

The proposed rule exempts credit cards, deposit account overdrafts, pawn loans, student loans, and other types of credit because they are "already subject to specific Federal consumer protection regulations and requirements." We urge the Bureau to adopt a similar exemption for loans made by highly regulated financial institutions, which already are subject to frequent and intense examinations and an alphabet soup of federal consumer protection regulations and requirements.

Thank you for your consideration of our comments, and please let us know if you have any questions.

Very truly yours,

Micah R Bartlett

Micah R. Bartlett
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President and CEO, Town and Country Bank

Linda Koch

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Illinois Bankers Association
President and CEO

cc: Illinois Congressional Delegation