City of Columbia
701 East Broadway, Columbia, Missouri 65201

Department Source: City Manager
To: City Council
From: City Manager & Staff
Council Meeting Date: June 19, 2017
Re: Report on Short Term Lending

Executive Summary

Staff has prepared for Council a report on Short Term Lending.

Discussion

Short term loans are often referred to as "payday or title loans." These loans are offered as an alternative to borrowing through a bank. Most often these loans are for smaller amounts and are available more quickly than standard loans. These loans are available more readily for the borrower in that the borrower often just needs a pay stub or car title to receive cash. Many people utilize these loans in emergency situations such as unexpected bills with the intent of paying back the loan with their next paycheck. Borrowers have the ability to roll over the loan which adds an additional amount for interest charges to the original amount borrowed. Under state law, borrowers can roll over their loan up to six times allowing for up to triple digit interest charged on a loan typically smaller than $1,000.

Short term loan establishments argue that they are providing a service that is needed for lower income populations. They fill a gap that banks cannot by offering these quick loans in smaller amounts. They also have easier approval processes than most banks and therefore make it easier for low income people to have access to a line of credit they would not otherwise have. They argue that the high interest rates protect and allow their businesses to operate since they lend to more "risky" people with lower incomes and less credit history. Others argue that the establishments prey on low income populations. Many times there are multiple establishments in close proximity to one another and are often located in lower income areas. Some also argue that the establishments are deceitful because they do not fully convey what their interest rate translates into as an annual percentage rate (APR), often leaving borrowers with a loan that they cannot afford to pay off until many years later due to the interest being so high.

Fifteen other cities in Missouri have begun to regulate these short term loan companies within their own jurisdictions, furthering the efforts of the state.[1] The regulations on these short term lending establishments range from permit, density, distance requirements, a cap on the number of establishments within the jurisdiction or an all-out ban on short term lending establishments.

Kansas City

The City of Kansas City has chosen to regulate their short term lending establishments due to the financial hardships it can put on their citizens and the effects that it can have on

[1] http://iowacci.org/wp-content/uploads/2012/05/PAYDAY-LENDING-ZONING-LAWS-chart%C2%A05-12.pdf

the neighborhoods where these are established.[2] If a short term lending establishment wants to operate within the city limits it must have a permit which costs $1,000 per year or $500 if less than 6 months remaining in calendar year. This permit must be renewed annually. The establishment must also allow city inspectors in during any time during normal business hours. Zoning requirements also apply to these establishments including not allowing more than one of these types of businesses within one mile of another, not located within 1,000 feet of a property or district which has been designated as a historic landmark and cannot be adjacent to or within 150 feet of a park, boulevard or parkway.[3]

Short term lending establishments must post a no loitering policy, limit signage to one wall and may not use electronic signs or banners. These establishments must also post in no less than 24 point bold font the interest rate and fees charged, the APR, a computation of the amount of the loan if it were rolled over six times and a warning that defaulting could result in loss of property. Other regulations on the establishments are similar to the City of St. Louis' "Good Neighbor" policy.[4]

St. Louis

On March 7, 2017 voters in the City of St. Louis, voted to regulate short term loan establishments.[5] The city defines short term loan establishments as payday loan stores, check cashing stores and car title loan stores. Within 60 days of March 7, these short term loan establishments had to obtain a permit to operate with St. Louis. The permit is valid for 1 year and must be renewed annually. The fee for the permit is $5,000 per year or $2,500 if less than 6 months remain in the calendar year. Establishments applying for the new permits will also have to comply with zoning regulations in that they cannot be within 500 feet of churches, homes and schools and not within a mile of a similar establishment.[6]

Inspectors are allowed to inspect these establishments to investigate compliance at any time during business hours. If violations of the short term lending code are found, the person convicted shall be fined no less than $100.00 and no more than $500.00. The short term lending code is described within the "Good Neighbor Plan." The "Good Neighbor Plan", establishes rules for the establishment to follow to prevent illegal activity such as loitering, drug use, indecent exposure, etc. from occurring but also to inform consumers that the establishment is not a federally chartered bank, savings and loan association or a credit union. Signs must be posted informing consumers in no less than 24 point, bold font. The signs must also list the interest rate and fees charged, the annual percentage rate (APR) per $100.00 borrowed, computations of amounts that would be paid on an original loan renewed after expiration without any payment of principal or interest up to six times. Lastly, the sign must list that defaulting on the loan could result in a loss of property.

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[2] https://www.municode.com/library/mo/kansas_city/codes/zoning_and_development_code?nodeId=ZODECOKAMI_800_SERIESTEME_88-810DE_88-810-1580SHRMLOES

[3] https://www.municode.com/library/mo/kansas_city/codes/zoning_and_development_code?nodeId=ZODECOKAMI_300_SERIESUSRE_88-325SHRMLOES

[4] https://data.kcmo.org/Regulated-Industries/Checklist-For-Short-Term-Loan-Establishment-New-Bu/k3kw-zqpr

[5] https://www.stlouis-mo.gov/internal-apps/legislative/upload/Ordinances/BOAPdf/BB69CSAA-AS%20AMENDED%20ON%20FLOOR%20ON%202016-11-04-wd20.pdf

[6] http://www.stltoday.com/opinion/editorial/editorial-yes-on-proposition-s-to-regulate-payday-lending-in/article_a82b8d17-1cd1-5848-a24e-6ef5396c6cb8.html

State Legislation

Within the state of Missouri, loans of up to $500 given by short term lending establishments are regulated by the Department of Insurance, Financial Institutions and Professional Registration. All short term lending establishments must register with the state and are subject to inspection to ensure they are following the rules established.[7] Short term lenders must pay an annual license fee of $300 to the state of Missouri and can be prorated. The lender must post the license within the lobby of their building. A sign, in no less than 10 point, bold type font, must state, that the establishment offers short term loans and the borrower can cancel the loan without costs by returning the full amount of the loan by the close of the following business day. The APR of the loans must be posted in at least 14 point, bold font. The loan can be renewed up to six times as long as the borrower is lowering the amount of the original loan by 5%, until it is paid off. The short term loan establishment is responsible for considering the financial ability of the borrower to pay back the loan. The definition of determining the financial ability of the borrower is not further defined and left up to the lender to decide. Most often short term loan establishments require the borrower to present identification and documentation of income and have a personal deposit account.[8] The borrower also cannot use another loan from the same establishment to pay off a loan and the borrower should not have more than $500 in loans.

There have been attempts in 2015 (HB91) and 2016 (HB1881) to expand the current standards to apply to loans of up to $750 and raise the annual license fee to $500. These past House Bills are identical to the most recent, HB 120, introduced by Representative Charlie Davis. HB120 limited the borrower to only having one short term loan from all lenders in the state at a time and limited the amount of times a loan can be rolled over to twice instead of the current 6 times. Borrowers would not be allowed to have more than $750 in outstanding loans from short term lenders in the state and could not receive another loan of $750 or less within one day of paying off another. Short term loan establishments would have also been required to provide borrowers at the time of the loan establishment: the exact duration, amount and date of payments and amount of interest and fees throughout the loan. The only remedy that lenders would have against borrowers who defaulted on their loan would have been a breach of contract claim instead of the current possibility of civil action. The Division of Finance would have been responsible for either, A) creating and maintaining or B) contracting with a third party to develop a real-time, statewide compliance system for short term lenders to record each loan transaction. The system would have been required to be implemented by January 2018. HB120 was referred to the House Financial Institutions Committee in February 2017. As of May 2017, there were currently no hearings scheduled.[9]

The Division of Finance is required by Missouri law to submit a bi-annual report based on surveys to payday lenders across the state.[10] There was a 90.1% return rate of surveys from the lenders. The numbers from the report have been put into charts below. Most of the charts show a decline in the numbers of Payday Lenders, Payday Loans and Defaulted

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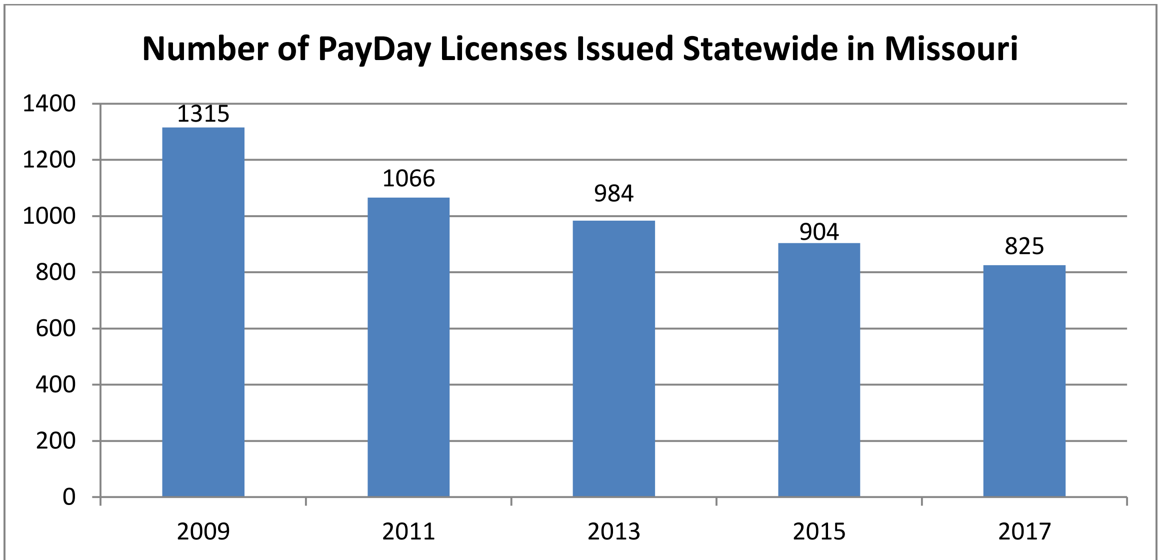
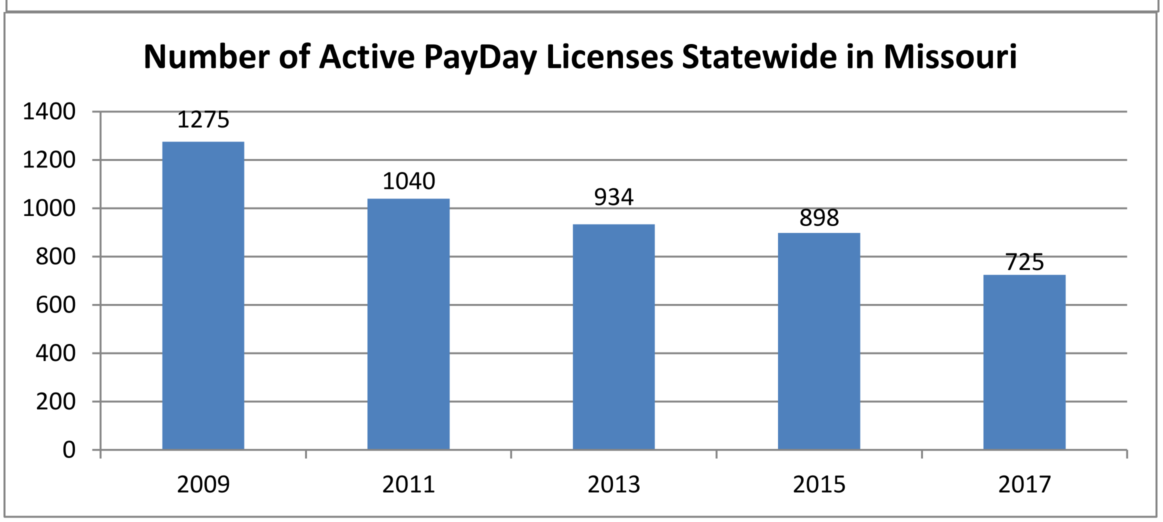
[7] http://finance.mo.gov/consumercredit/documents/500ApplicationPacket-tempLH.pdf
[8] http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf
[9] http://www.house.mo.gov/billtracking/bills171/hlrbillspdf/0203H.01I.pdf
[10] http://finance.mo.gov/reports/documents/SurveyReport2017_001.pdf

Loans in Missouri. There is speculation that although these numbers are falling they are due to the industry switching to offering installment loans, which are not reported on by the Division of Finance.





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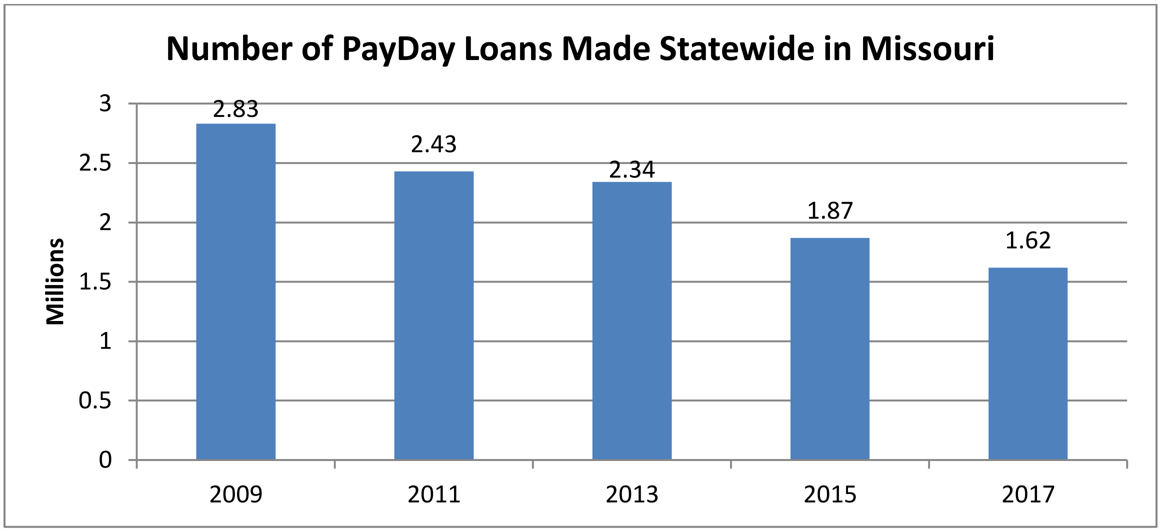

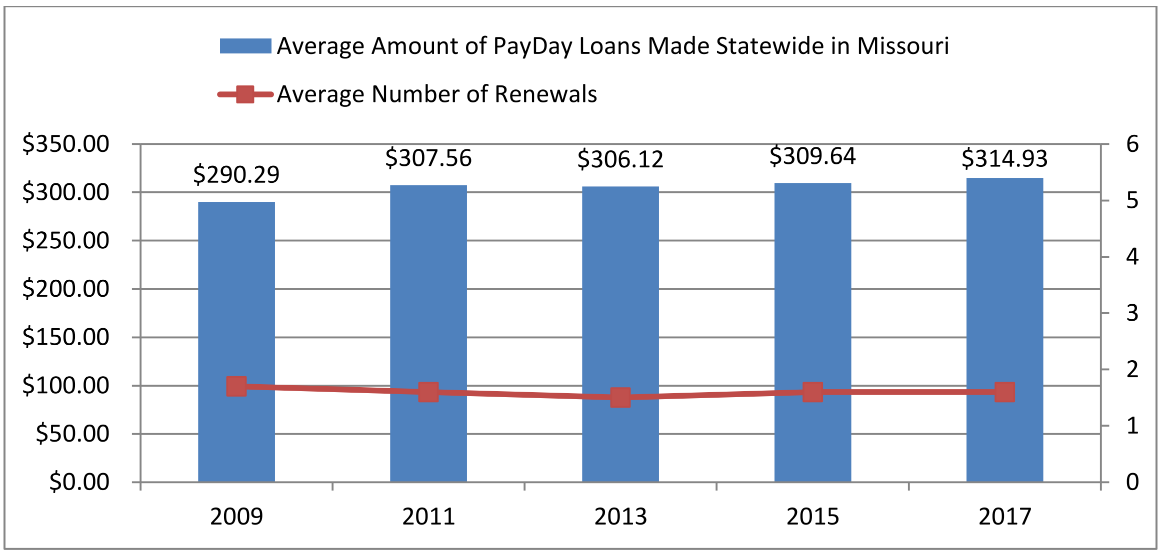

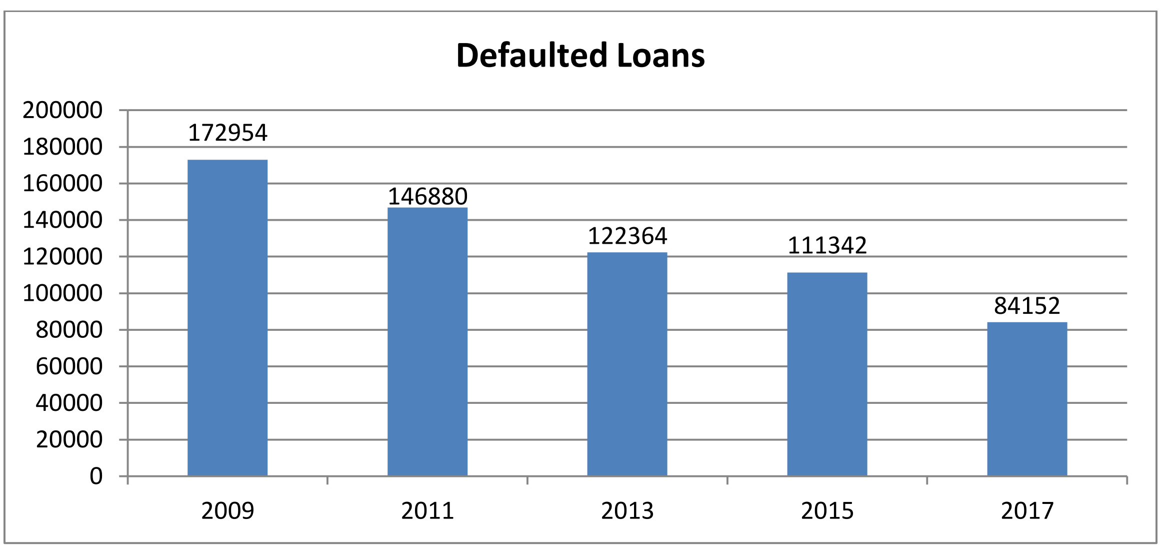

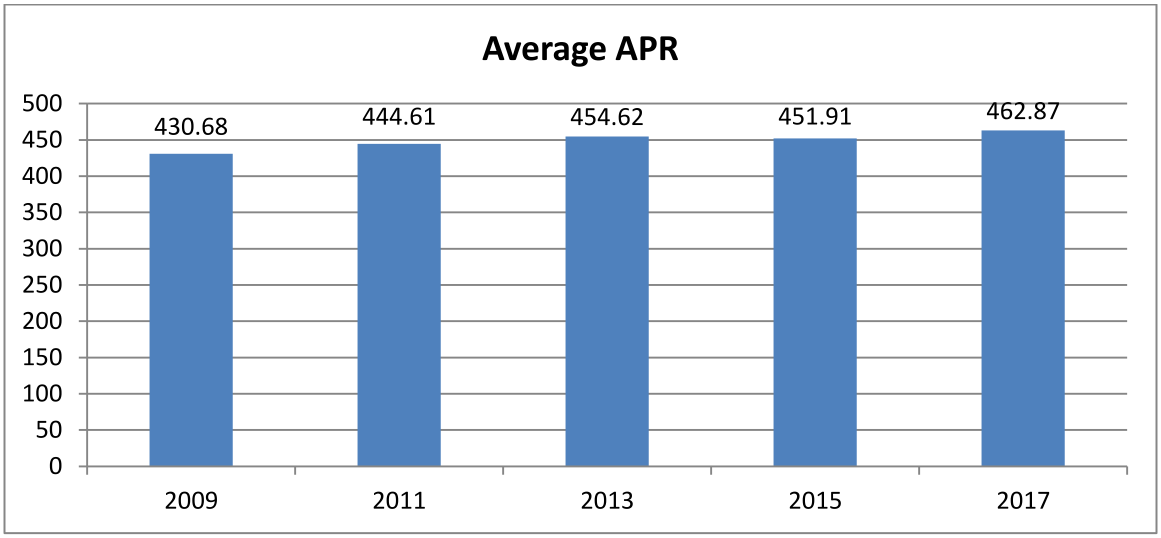

Installment Loans

The Consumer Financial Protection Bureau, states and local governments began focusing on regulating businesses offering payday loans and although the number of payday loans is falling in the state of Missouri, some payday lenders have switched to offering installment loans instead[11]. These installment loans differ from payday loans in that they offer longer financing terms no less than 120 days instead of 2 weeks and the amounts of the loans are usually larger. Installment loans also require the lender to set up at least four equal payments for the consumer to pay. Unlike payday loans, there are no caps on the interest rates for installment loans. However, both of these short term loans have high interest rates. Interest rates can range from 36% to triple digits. The Division of Finance produces a biannual report on payday lenders within the state of Missouri but does not report on installment lenders, making it difficult to know how much the numbers have risen in this industry.

According to the Division of Finance Website, Installment lenders must pay the State of Missouri an annual fee of $300 to operate.[12] This fee can be prorated depending on the time of year they apply. Installment lenders are required to produce an annual report to the Division of Finance that includes: the names and addresses of the lender and each branch, the names and addresses of the officers and directors, a balance sheet which shows the financial condition of the lender, the total amount of loans and each principal amount, the number of garnishments and the number of security agreements. Contracts with borrowers must include the name and address of the lender and borrower, the schedule of payments, the type of instrument securing the loan, the principal amount of the loan and the rate of interest, and that if the loan is paid early the interest is subject to refund. Fees for the loans cannot exceed $75. A payment that is more than 15 days late can have a late charge added of no more than $50. Consumers are able to defer the loan payment if the loan is

[11] http://www.stltoday.com/news/local/govt-and-politics/missouri-payday-lenders-shift-to-installment-loans/article_ca8d5c45-d05d-59f9-ace9-b67b339ba0c4.html
[12] http://finance.mo.gov/consumercredit/documents/510ApplicationPacket-tempLH.pdf

more than $600, the lender agrees and the consumer has made the first full installment payment. Fees for deferring payments will be no more than $50 per deferment.

Consumer Financial Protection Bureau

The Consumer Financial Protection Bureau has performed a study which showed that people who use Payday or Title Loans often become trapped in a cycle of debt. After the study the CFPB has proposed new regulations for these types of lenders which would help regulate these lenders more closely. The CFPB found in their study that within a month almost 70% of borrowers end up taking out a second short term loan and 1 in 5 borrowers ends up taking out at least 10 or more loans.[13] Payday loans require the borrower to pay back the full amount on their next paycheck which requires them writing a postdated check or giving access to their bank account to the lender. When the date comes, the lender attempts to withdraw the money and if the borrower does not have the full amount to cover the loan then the bank charges overdraft fees as well as fees being added on to the loan. The lender keeps attempting to access the account costing the borrower more. On average, over half of borrowers were charged $185 in fees on the loans they took out. Payday loans do not require collateral to borrow unlike title loans. Title loans typically give the borrower 30 days to repay but if they do not repay or take out an additional loan they risk losing their vehicle. CFPB's study found that 1 in 5 title loan borrowers lose their vehicles.

The CFPB has proposed new regulations for these short term loans including payday, title and installment loans. CFPB rule change proposals go through 3 stages: Pre-rule, Proposed Rule and Final Rule. These regulations were proposed in July 2016 after research was done and were open for public comment until October 2016. The proposed rule changes will be examined for the potential impacts they could have and if adopted, the CFPB will provide support to stakeholders to ensure they are complying.

The proposed regulations are organized for shorter and longer term loans but do not include: (1) Loans extended solely to finance the purchase of a car or other consumer good in which the good secures the loan; (2) home mortgages and other loans secured by real property or a dwelling if recorded or perfected; (3) credit cards; (4) student loans; (5) non-recourse pawn loans; and (6) overdraft services and lines of credit.[14] Shorter term loans, which the CFPB defines as, loans typically less than 30 days would require the lender to

- Verify the consumer's net income;
- verify the consumer's debt obligations using a national consumer report and a consumer report from a "registered information system" as described below;
- verify the consumer's housing costs or use a reliable method of estimating a consumer's housing expense based on the housing expenses of similarly situated consumers;
- forecast a reasonable amount of basic living expenses for the consumer—expenditures (other than debt obligations and housing costs) necessary for a consumer to maintain the consumer's health, welfare, and ability to produce income;

[13] https://www.consumerfinance.gov/about-us/newsroom/the-cfpb-finds-payday-and-deposit-advance-loans-can-trap-consumers-in-debt/

[14] https://www.regulations.gov/document?D=CFPB-2016-0025-0001

- project the consumer's net income, debt obligations, and housing costs for a period of time based on the term of the loan; and
- determine the consumer's ability to repay the loan based on the lender's projections of the consumer's income, debt obligations, and housing costs and forecast of basic living expenses for the consumer.[15]

The lender could not lend to the borrower if the borrower had more than 3 short term loans within 30 days of each other. The lender could deviate from this if they could verify a change in the financial status of the borrower. The lender would be allowed to make 3 short term succession loans to the borrower if the first loan had a principal amount of $500 or less, the second loan was 1/3 less than the first loan and the third loan was 2/3 less than the first loan. Borrowers could not have more than 6 short term loans in less than 12 months or could not be in debt for more than 90 days in a 12 month period. Lenders would not be allowed to take vehicle titles as collateral for these loans.[16]

Longer term loans would require the lender to follow the same standards in assessing the borrower's ability to repay but with the added consideration of accounting for the possibility of volatility in the consumer's income, obligations, or basic living expenses during the term of the loan.[17] Ability to repay requirements could be avoided by the lender if the standards of the conditional exemption model from the National Credit Union Administration's Payday Alternative Loan program are followed. The standards include

- Loans may be for $200 to $1,000 to borrowers who have been credit union members for at least one month;
- Terms of one to six months;
- A maximum $20 application fee;
- No rollovers are allowed; and
- An interest rate of up to 28 percent APR if all other conditions are met.[18]

Ability to repay requirements could also be avoided if the lender set up for amortizing payments spread out between 46 days but not more than 24 months. The APR must be 36% or less and the fees for these loans could not be more than $50. The annual percent of loans which follow this standard cannot have a default rate of more than 5%. If the 5% default rate is succeeded, the lenders would have to repay the fees for all loans made within annual period to all borrowers.

All lenders would only be allowed to attempt to collect payments twice from a borrower's bank account and would have to notify the lender at least 3 days in advance of the payment being collected. If both attempts fail the lender must obtain authorization from the borrower to continue to attempt to collect payments. A registered information system would be required of all lenders which would collect information on borrowers recent and current accounts. Before making a loan the lenders would have to run a report on the borrower from the system.

[15] https://www.regulations.gov/document?D=CFPB-2016-0025-0001
[16] https://www.regulations.gov/document?D=CFPB-2016-0025-0001
[17] https://www.regulations.gov/document?D=CFPB-2016-0025-0001
[18] https://www.ncua.gov/newsroom/Pages/news-2016-oct-metsger-asks-exempt-payday-alternative-loans.aspx

The CFPB was founded under the Dodd-Frank Act after the 2008 housing crisis. The independent agency gains its funding from the Federal Reserve and was founded to protect consumers from deceitful banking practices. The rule changes regarding short term lenders proposed by the CFPB are currently on hold. On June 8, 2017 the House of Representatives passed the CHOICE Act which could dismantle the CFPB by giving Congress control of their funding.[19] There are doubts that this bill would pass the Senate.[20]

Columbia

According to the Division of Finance's website, the City of Columbia has approximately 23 short term lending establishments.[21] 15 businesses are registered as consumer installment lenders and 8 are registered as payday lenders. Below are maps which document the locations as well as overlay the average income for that area of the city. These maps were taken from a story from the St. Louis Post Dispatch and the income is based off of the American Community Survey data[22]. The maps do not list locations that are online lenders. Most locations within the City of Columbia are based in areas where the income is under $35,000. Locations of the short term lenders also appear to be in clusters in these neighborhoods.

The City of Columbia currently does not have any regulations for short term lenders other than standard business license practices.[23] Section 13-27 of the City Code requires that all businesses within Columbia pay annual license fees based on the number of employees or the fee schedule, whichever is higher. There are also currently no zoning standards for these businesses specifically regarding the distance they should be from one another or other types of zoning. If the City of Columbia chose to enact a similar measure, it would be the responsibility of the Office of Neighborhood Services to perform inspections of the businesses and make sure the codes were being followed. Business licensing would also be impacted due to the higher fees being associated with owning and operating these types of businesses within the city limits. Community Development and Planning and Zoning would need to update the codes regarding these businesses if location standards were enacted.

The regulation of short term lenders would align with the City of Columbia's Strategic Plan by addressing social equity issues. The concern from regulating these businesses comes from the demand for their services. Lower income individuals utilize these services because they may not have access to credit and banks tend to not lend money in this small of an amount.

[19] http://money.cnn.com/2017/05/04/news/economy/gop-dodd-frank-financial-reforms/index.html

[20] http://www.cnbc.com/2017/06/08/house-has-votes-to-pass-choice-act-that-would-gut-dodd-frank-banking-reforms.html

[21]http://finance.mo.gov/licensee/search?page=29&sort_type=zip&sort_asc_desc=asc&licensee_type=510&search_query=

[22] http://www.stltoday.com/news/opinion/columns/the-platform/editorial-yes-on-proposition-s-to-regulate-payday-lending-in/article_a82b8d17-1cd1-5848-a24e-6ef5396c6cb8.html

[23]https://www.municode.com/library/mo/columbia/codes/code_of_ordinances?nodeId=PTIICOOR_CH13LIPEMIBURE_ARTIIOCLI_S13-27LIFESC

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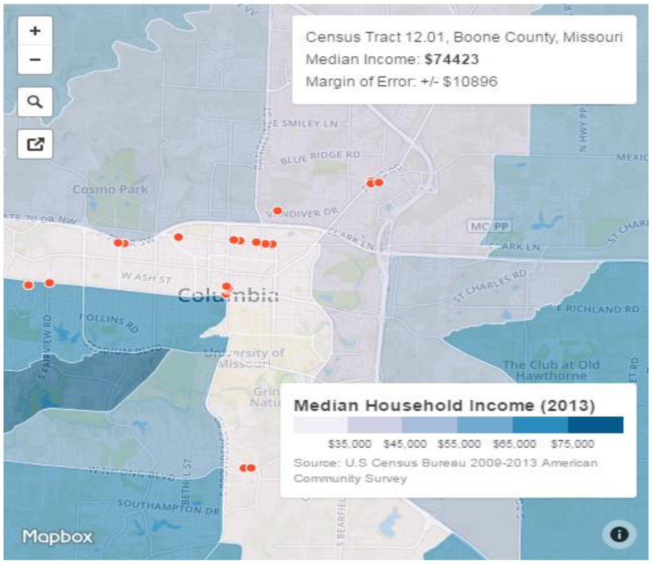

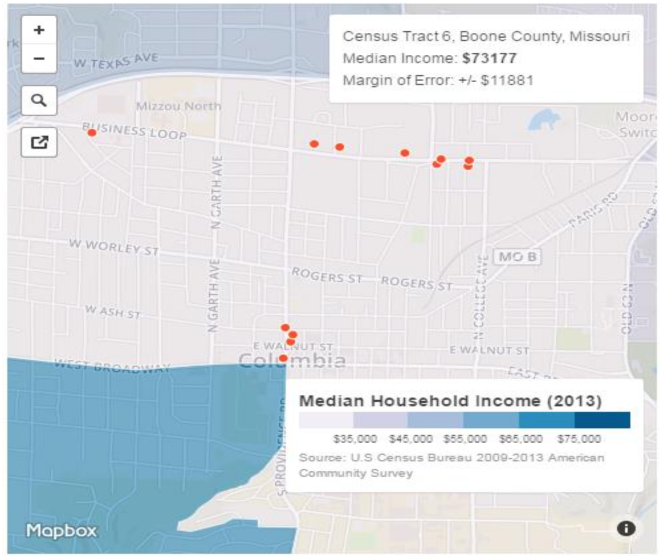

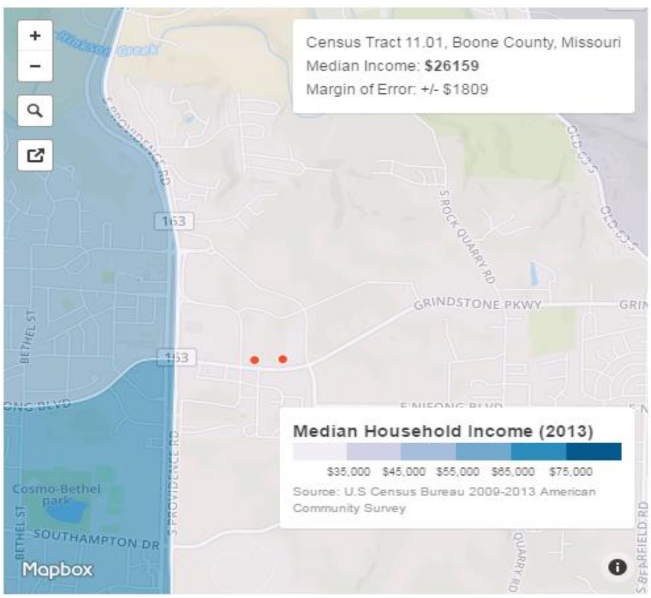

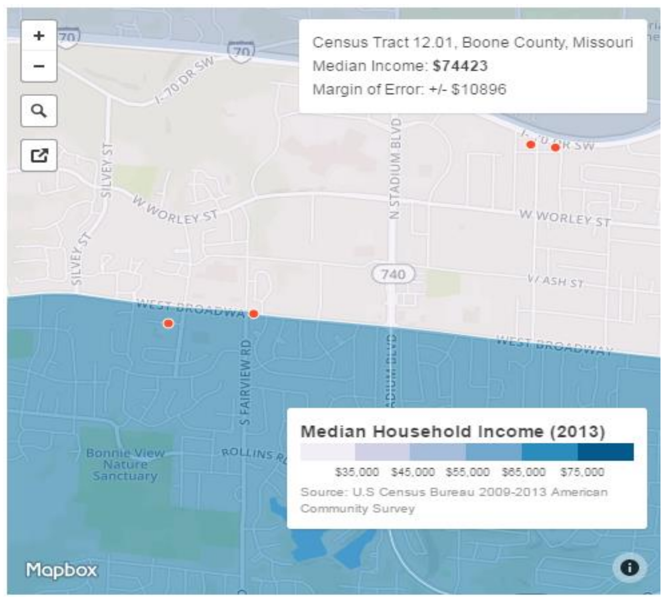

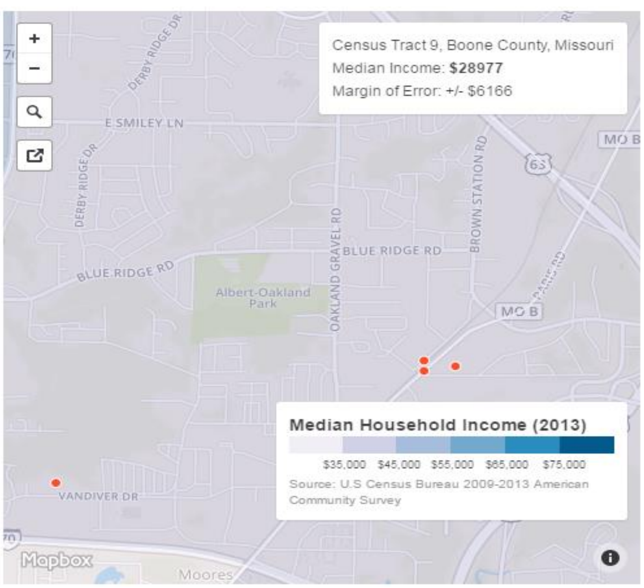

Conclusion/Concerns

The purpose of this research is to explore the impact that short term lenders could be having on Columbia's residents. These lenders do provide a service which is needed by some and has filled a gap that other financial institutions have not provided. Enacting this type of licensing for these short term lenders can bring significant work to several city departments. Paying for the increase in workload is important and could be offset through the increase in license fees for these types of lenders.

The Consumer Financial Protection Bureau has begun the process of implementing stricter standards for these establishments and it may be prudent to wait and see what changes the CFPB makes. Alternatively, the Council could take action and adjust local regulation to align with CFPB regulations, when and if they occur.

Fiscal Impact

Short-Term Impact: N/A
Long-Term Impact: N/A

Vision & Strategic Plan Impact

Vision Impacts:
Primary Impact: Not Applicable, Secondary Impact: Not Applicable, Tertiary Impact: Not Applicable

Strategic Plan Impacts:
Primary Impact: Social Equity, Secondary Impact: Not Applicable, Tertiary Impact: Not Applicable

Comprehensive Plan Impacts:
Primary Impact: Not Applicable, Secondary Impact: Not applicable, Tertiary Impact: Not Applicable

Legislative History

Date	Action
11/02/2009	Item B320-09 in the Council minutes. Council voted 5-2 in favor of a 6-month moratorium but the moratorium expired without any further Council direction or action.

Suggested Council Action

This report is for information only.