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United States Senate

WASHINGTON, DC 20510-2309

December 18, 2014

The Honorable Richard Cordray
Director
Consumer Financial Protection Bureau
1700 G Street NW
Washington, DC 20552

Dear Director Cordray,

I write to urge the Consumer Financial Protection Bureau (CFPB) to protect consumers from harmful practices in the payday lending industry. While payday loans may fulfill the borrower's immediate need for cash, too often consumers using payday loans become trapped in a cycle of high-interest debt. I ask that the CFPB propose effective rules that promote reasonable standards for lending and limit the misuse of short-term debt.

The debt burden of payday loans is a growing problem in communities throughout Minnesota. Between 2007 and 2012, the number of payday loans taken out by Minnesotans more than doubled. Repeated use of high-interest payday loans means more Minnesotans are getting pulled deeper and deeper into debt. While payday loans may be billed as short-term credit for emergency cash needs, the reality is that most consumers who use payday loans are repeat borrowers covering ordinary expenses. According to Minnesota Department of Commerce data, the average payday borrower in my state takes out ten loans per year. The CFPB's own data show that 80 percent of payday loans are rolled over or followed by another loan. Furthermore, when borrowers have a sequence of loans, the last loan in the sequence is the same size or larger than the original loan more than 80 percent of the time.

I thank the CFPB for including payday loans on its rulemaking agenda, and I strongly encourage the agency to move forward with reforms in this area. The CFPB should encourage better standards for underwriting small-value, short-term loans and verifying the borrower's ability to repay. Some payday lenders principally rely on information such as a form of identification, paystub, and bank statement to apply when the borrower applies for a loan. This information may be insufficient to determine an individual's creditworthiness. Assessing loans' riskiness should be based on evaluation of the borrower's income and expenses.

At the same time, some payday lenders require the borrowers to provide postdated checks or electronic access to their bank accounts. Access to a borrower's bank account does not guarantee loan quality. However, access to the account does enable the lender to debit funds, which can run up bank fees on that consumer. These fees, coupled with the already high interest rates charged on the loan, can worsen the consumer's financial situation. Responsible lending is affordable for the long term. Loan requirements should be rooted in the borrower's ability to repay, not just the lender's ability to collect.

In addition, the cost and structure of certain loans may be ill-suited to borrowers' circumstances. The Federal Deposit Insurance Corporation (FDIC) concluded in 2005 that payday loans are "not appropriate" if a consumer has already used payday loans for more than three months in the past year. Instead, the FDIC recommended, consumers should be directed toward longer-term loan products better suited to their financial needs. The performance of short-term loans needs to be evaluated. Limitations on rollover or repeat lending of high-cost, short-term loans may be necessary to protect consumers from excessive fees and help steer them toward better financial alternatives.

More generally, I ask the CFPB to design a rule of adequate scope. At both the state and federal level, payday lenders have managed to circumvent laws and regulations that were crafted too narrowly. In Minnesota, the largest payday lenders have registered as Industrial Loan and Thrift Organizations to avoid coming under the state's Consumer Small Loan Lender Act. Currently, the Department of Defense is moving to correct narrow language in its original regulations under the Military Lending Act that have allowed lenders to sidestep protections for our servicemembers. These experiences should be instructive as new rules are crafted. Rules can only be effective if they apply to the products and institutions that they are meant to regulate.

Borrowers need strong protections as they seek to meet their immediate financial needs. I look forward to the CFPB's future efforts to address problems in the payday lending industry. Thank you for your ongoing commitment to protect American consumers.

Sincerely,

Al Franken

Al Franken
United States Senator