

**Testimony of Uriah King, Center for Responsible Lending
before the Ohio Financial Institutions, Real Estate, and Securities Committee
September 30, 2009**

Chair Koziura, Ranking Member Mandel, and members of the Committee, thank you for holding this hearing and inviting me to speak about the use of the Ohio Credit Services Organization Act by the payday lending industry. I serve as Senior Policy Associate at the Center for Responsible Lending (CRL), a nonprofit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices.

CRL is an affiliate of Self-Help, the nation's largest nonprofit community development financial institution which consists of a credit union and a non-profit loan fund. For close to thirty years, Self-Help has focused on increasing ownership opportunities for low-wealth families, primarily through financing home loans to low-income and minority families who otherwise might not have been able to get affordable home loans. We also work to strengthen communities by financing nonprofits, childcare centers, community health facilities, public charter schools and residential and commercial real estate projects. And we recognize the importance of the entrepreneur's critical role in revitalizing underperforming economies by financing nearly \$400 millions in small business loans, making us the largest SBA 504 lender in North Carolina. In total, Self-Help has provided over \$5.6 billion of financing to families, small businesses and nonprofit organizations across America, including \$271.6 million dollars in mortgage financing here in Ohio.

For my short testimony today, I will provide a brief overview of "traditional" credit service organizations (CSOs) and the laws intended to regulate them. Next, I will provide a summary of our initial data collection and our findings of how payday lenders are attempting to use the Ohio CSO statute. Finally, I will provide a short legal analysis of the Ohio CSO law and its implications for HB 209.

Ohio, like most states, has adopted a credit services organization act to address concerns raised by the growth of credit repair organizations.¹ Like most state credit repair laws, Ohio's law complements the Federal Credit Repair Organizations Act (FCROA), both of which were enacted in 1996. The passage of the federal act provides important context about the law which payday lenders are now using. The federal act was enacted in response to the growing abuses by entities promising to help consumers with their credit history, but in reality, were charging high fees and providing little, if any, remedy for credit blemishes. Congress formally found that "certain advertising and business practices of some companies engaged in the business of credit repair services have worked a financial hardship among consumers, particularly those of limited economic

¹ Ohio Rev. Code § 4712.01(C)(1)(Ohio Credit Services Organization Act "credit services organization" is comprehensively defined as "any person that, in return for the payment of money or other valuable consideration readily convertible into money for the following services, sells, provides, or performs, or represents that the person can or will sell, provide, or perform, one or more of the following: (a) improving a buyer's credit record, history, or rating; (b) obtaining an extension of credit by others for a buyer; (c) providing advice or assistance to a buyer in connection with [the above]...").

means and who are inexperienced in credit matters.”² FCROA explicitly states that the purpose is “to protect the public from unfair and deceptive advertising and business practices by credit repair organizations.”³ By offering loans via Ohio’s CSO Act, payday lenders are turning its original purpose on its head.

Enacted by the Ohio General Assembly in 2008 and later affirmed by the Ohio voters as Issue 5, essentially HB 545 sought to address the well-documented payday loan “debt trap” by reforming the relatively monolithic payday loan business model.⁴ Primarily, this would be done by giving borrowers more time, cutting the costs of the loan, reducing the loan size (i.e. the size of the balloon payment) and establishing a suitability standard that annually limits payday lenders to four “short-term” loans per borrower. Unfortunately, some of the largest payday lenders in the country have registered as credit services organizations, making short-term, high-cost loans at even worse terms than under the old payday loan statute repealed by HB 545, all under the guise of “credit repair.” These lenders include CashNet USA, Check N Go, Advance America (in partnership with CashNet), and PaydayOne. Ironically, about a third of all active CSO licensees are now actually payday lenders.⁵

This latest form of subterfuge is a variation of an older ruse, the so-called “rent-a-charter” model. Here is how it worked: under the standard rent-a-charter arrangement, payday lenders courted national and state chartered banks to act as “conduits” for loans in a blatant attempt to avoid the application of the state usury cap. Payday lenders provided banks with a kickback in exchange for the use of their charter.⁶ After receiving criticism from state and federal regulators, rent-a-charter was substantially curtailed, if not effectively prohibited, by the OCC, Federal Reserve, the Office of Thrift Supervision, and most recently the FDIC.⁷

This type of subterfuge has been adapted in a handful of states with CSO statutes like Ohio, Texas, and Maryland. Under this arrangement payday lenders are not seeking

² 15 U.S.C. § 1679(a)(2)

³ 15 U.S.C. § 1679(b)(2)

⁴ Payday lenders are dependent upon borrower “churning,” converting the infrequent short-term loan into long-term, high cost debt. For example: “[t]he financial success of payday lenders depends on their ability to convert occasional users into chronic borrowers.” Michael Stegman and Robert Faris, University of North Carolina. *Economic Development Quarterly*, Vol. 17, No. 1, 8-32 (2003). “And the theory in the business is you’ve got to get that customer in, work to turn him into a repetitive customer, long-term customer, because that’s really where the profitability is.” Dan Feehan, CEO of Cash America. Remarks made at the Jeffries Financial Services Conference. June 20, 2007. Transcript on file with the author. Also, see generally <http://www.responsiblelending.org/payday-lending/research-analysis/>

⁵ See Appendix I

⁶ Federal Deposit Insurance Corporation, Guidelines for Payday Lending (Financial Institutions Letters 14-2005)(Explaining the exportation doctrine)(“Federal law authorizes federal and state-chartered insured depository institutions making loans to out of state borrowers to “export” favorable interest rates provided under the laws of the state where the bank is located. That is, a state chartered bank is allowed to charge interest of loans to out of state borrowers at rates authorized by the state where the bank is located, regardless of usury limitations imposed by the state laws of the borrower’s residence.”)

⁷ See generally, Remarks of John D. Hawke, Jr., Comptroller of the Currency, Before the Women in Housing and Finance, Washington, D.C., Feb. 12, 2002. <http://www.occ.gov/ftp/release/2002-10a.doc> at 10 (In 2002, then Comptroller of the Currency John Hawke described this practice by national banks as “an abuse of the national charter.”).

to export the favorable interest rates provided by charter of the third party lender, but instead seek out a partnership to engage in fee packing.

Using this arrangement, payday lenders register under the state credit services organization act and offer to assist borrowers in repairing their credit by obtaining them a payday loan. Payday lenders contend that they are not acting as the lender, but are merely connecting consumers with third party lenders. As a result, these payday lenders charge a CSO or broker fee (typically \$25 per \$100) plus a 28% interest which can equate to annual percentage rates (APR) *twenty-four times greater* than contemplated by Issue 5.

	Cash Net/Advance America ⁸	Check 'n Go ⁹	Payday One ¹⁰	Issue 5/HB 545 ¹¹
Minimum Loan Term	8 days	10 days	8 days	31 days
Maximum Loan Size	\$1500	\$1500	\$1000	\$500
Maximum APR (assuming 14 day term)	683%	677%	612%	28%
“Suitability” standard, i.e. short-term loan cap	<u>None</u> (this means that Ohioans can be indebted to a “short-term” lender for the entire year)	<u>None</u> (this means that Ohioans can be indebted to a “short-term” lender for the entire year)	<u>None</u> (this means that Ohioans can be indebted to a “short-term” lender for the entire year)	4 loans per year

Based on our initial factual and legal analysis (1) loans made via the CSO act are subject to the 28% rate cap, and (2) entities that "make or collect" loans are precluded from using the statute entirely. Payday lenders operating as CSOs are indistinguishable from other payday lenders, as are their loans. Slapping on the “credit repair” label should not entitle payday lenders to a free pass to ignore Ohio law.

Since 2005, Michigan, Florida, and California have all taken steps to address payday industry’s exploitation of CSO statutes through both legislation and regulatory enforcement. The Michigan Department of Labor and Economic Growth found that CSO fees are “deceptive subterfuge designed to extract impermissible fees from a borrower”

⁸ See <http://www.cashnetusa.com/fee-schedule-ohio.html>. Accessed September 29, 2009.

⁹ See <https://www.checkngo.com/resources/state-center/states/OH.rates>. Accessed September 29, 2009.

¹⁰ See <http://www.paydayone.com/ohio-loan-cost-and-terms.aspx>. Accessed September 29, 2009.

¹¹ See Appendix II for a copy of the official Issue 5 ballot language that was provided for all voters. HB 545 is codified at O.R.C. 1321.35 to 1321.48

and evade the state's applicable usury law.¹² In an action against EZPAWN, Florida's Office of Financial Regulation found that CSO fees are to be considered part of the loan and therefore subject to the Florida's rate cap on consumer loans.¹³ California adopted legislation that bars CSOs from obtaining an extension of credit from a third party lender for whom the CSO provides underwriting, billing, payment processing, or debt collection services.¹⁴ Conversely, in Texas, a judicial opinion, distinguishing CSO fees from fees attributable to the lender, has allowed the business model to flourish in that state.¹⁵

Ohio has had a deep history of broad, aggressive enforcement of its CSO act. For example, in 1997, one year after the act's passage, the Ohio Supreme Court found that operating as an unlicensed credit service organization constituted a predicate offense under the state's RICO state. In that case, *State v. Schlosser*,¹⁶ a for-profit entity soliciting consumers to inform them of credit cards for which they were eligible was found to meet the definition of a credit service organization. As another example, in 1999, an older version of the Ohio law was found to cover car dealers who arranged financing for the consumers as long as the dealer received *any* fee from the consumer regardless if the fee was associated with the extension of credit itself.¹⁷ In light of this decision, the legislature amended the statute to require that the consumer's payment be for the actual credit services and exempted car dealers. Nevertheless, it still highlights the broad construction of the credit services act in favor of the consumer, which is consistent with the federal CROA and other state decisions.

While Ohio's Credit Services Organization Act lacks many of the loopholes of other state CSO statutes, its enforcement would be greatly expedited by the passage of House Bill 209, avoiding a potentially protracted and costly litigation effort.¹⁸ Much of the recommended anti-brokering and other types of anti-subterfuge language contained in HB 209 are based on tested measures found in other states. This means, perhaps most importantly, that HB 209 will enable the Attorney General and the Department of Commerce to effectively respond to the next permutation of abuses as they emerge.

¹² Michigan Department of Labor and Economic Growth Bulletin 2006-06-CF (June 21, 2006), www.michigan.gov/dleg/0,1607,7-154-10555_12900_12919--,00.html

¹³ Office of Fin. Reg. v EZPAWN Florida, Inc. Case No. 07—3953 (Fla. Div. of Admin. Hearings Mar. 25, 2008), www.nclc.org/unreported

¹⁴ Cal. Civ. Code § 1789.13.

¹⁵ *Lovick v. Ritemoney*, 378 F.3d 433 (5th Cir. 2004) (The Fifth Circuit Court of Appeals interpreted Texas law in a case involving an auto title loan. The storefront operated as a "broker," registered under the Texas Credit Services Organization Act (TCSOA), charging the consumer a \$1,500 fee to "arrange" a loan of \$2,013 (the consumer received only \$500). Meanwhile, the "lender" charged interest at the rate of 10%, the legal rate under Texas usury law. The court held, over a dissent, that the TCSOA trumped the state's usury law. Because the TCSOA places no limits on the "broker" fee, the \$1,500 charge was legal).

¹⁶ 79 Ohio St. 3d 329, 681 N.E.2d 911 (1997)

¹⁷ *Sannes v. Jeff Wyler Chevrolet, Inc.* 107 Ohio Misc.2d 6, 736 N.E.2d 112 (1999).

¹⁸ Ohio Rev. Code § 4712.01(C)(2)(a) (Much of the debate about enforcement centers on the issue of whether payday lenders operating under CSO licenses are in fact making payday loans. However, the Ohio Credit Services Organization Act nullifies this issue entirely, expressly excluding from the definition of CSO, "any person that makes or collects loans.")

**APPENDIX I: ACTIVE CREDIT SERVICE ORGANIZATION ACT
LICENSEES**

Contact Name	License Number	Type	License Issue Date	DBA
BURHILL FINANCIAL SERVICES, LLC	CS.900038.000	CSO	10/11/2005	
CREDIT IMPROVERS, INC.	CS.900016.000	CSO	02/10/1995	
MONEY MANAGEMENT INTERNATIONAL, INC.	CS.900028.000	CSO	10/31/2003	
RESTORED SOLUTIONS, LLC	CS.900039.000	CSO	03/07/2007	
TODD F. WARD	CS.900002.000	CSO	02/09/1994	TR & ASSOCIATES CREDIT SERVICES
URGENTCASH, INC.	CS.900092.000	CSO	07/14/2009	URGENTCASH
SIMPLETUITION, INC.	CS.900047.000	CSO	12/21/2007	
ADVANTAGE CREDIT COUNSELING SERVICE, INC.	CS.900050.000	CSO	08/29/2007	
INCHARGE INSTITUTE OF AMERICA INC.	CS.900057.000	CSO	05/01/2008	
FAMILY FINANCIAL EDUCATION FOUNDATION	CS.900064.000	CSO	05/01/2008	
CREDIT REPAIR RESOURCES, LLC	CS.900074.000	CSO	06/30/2008	
CREDIT REPAIR CLINIC, LLC	CS.900067.000	CSO	03/26/2008	THE CREDIT REPAIR CLINIC
COMPASS CREDIT SERVICES, LLC	CS.900069.000	CSO	06/04/2008	
CREDIT MENTORING AND CONSULTING, INC.	CS.900070.000	CSO	06/30/2008	
CLEAR CREDIT CORP.	CS.900071.000	CSO	05/23/2008	
JSA CREDIT SERVICES, LLC	CS.900072.000	CSO	05/19/2008	JSA CREDIT REPAIR
OHIO SPECIALTY FINANCE, INC.	CS.900077.000	CSO	10/16/2008	CHECK 'N GO
HRB TAX GROUP, INC.	CS.900075.000	CSO	08/11/2009	
OHIO CONSUMER FINANCIAL SOLUTIONS, LLC	CS.900076.000	CSO	05/29/2009	CASHNETUSA
PAYDAY ONE EXPRESS OF OHIO, LLC	CS.900086.000	CSO	10/24/2008	PAYDAY ONE
BUCKEYE CREDIT SOLUTIONS, LLC	CS.900087.000	CSO	04/01/2009	CHECKSMART
OVERLOOK DEVELOPMENT CO.	CS.900089.000	CSO	06/18/2009	ADVANCE PAY USA
URGENTCASH, INC.	CS.900091.000	CSO	07/14/2009	URGENTCASH
URGENTCASH, INC.	CS.900093.000	CSO	07/14/2009	URGENTCASH
URGENTCASH, INC.	CS.900094.000	CSO	07/14/2009	URGENTCASH
WALLACE FINANCIAL CONSULTING, LLC	CS.900095.000	CSO	09/01/2009	
911 CREDIT REPAIR AND CONSULTING, LLC	CS.900096.000	CSO	09/01/2009	

**APPENDIX II: OFFICIAL BALLOT LANGUAGE ISSUE 5
(2008/Formatted for MS WORD)**

**ISSUE #5
REFERENDUM**

**REFERENDUM ON LEGISLATION MAKING CHANGES TO CHECK
CASHING LENDING, SOMETIMES KNOWN AS “PAYDAY LENDING,”
FEES, INTEREST RATES AND PRACTICES**

Substitute House Bill 545 (H.B. 545), which was passed by the Ohio legislature and signed into law by the Governor, substantially changed the law regulating how certain lenders in Ohio operate. Under the referendum, voters must decide whether Section 3 of H.B. 545 should go into effect. Section 3 of H.B. 545 deletes the old provisions of the law regulating check cashing lenders, sometimes known as “payday lenders,” in favor of the new provisions.

1. If a majority of Ohio voters approve Section 3 of H.B. 545, all short term lenders, including check cashing lenders, would be subject to the following limitations:

- The maximum loan amount would be \$500;
- Borrowers would have at least 30 days to repay the loan; and
- The maximum interest rate would be 28% annual percentage rate (APR) on all loans.

2. If a majority of Ohio voters reject Section 3 of H.B. 545, check cashing lenders would be allowed to continue under previous law as follows:

- The maximum loan amount would continue to be \$800;
- There would continue to be no minimum repayment period; and
- Check cashing lenders could continue to charge rates and fees, resulting in a total charge for a loan that substantially exceeds an equivalent APR of 28%.

A “YES” vote means you approve of Section 3 of H.B. 545, and want to limit the interest rate for short term loans to 28% APR and change short term lending laws.

A “NO” vote means you disapprove of Section 3 of H.B. 545 and want to permit check cashing lenders to continue to be able to offer short term loans as currently permitted.

A majority “YES” vote is required for Section 3 of H.B. 545 to be approved.