Testimony of

Rob Norcross

CONSUMER SERVICE ALLIANCE OF TEXAS

February 22, 2011

Senate Business and Commerce Committee

SB 251 and SB 253

Mr. Chairman, and members, thank-you for the opportunity to present our views on Senate Bills 251 and 253.

My name is Rob Norcross. I represent the Consumer Service Alliance of Texas ("CSAT"). CSAT is a trade association advocating for the protection of financial choice based on personal responsibility for Texas consumers and Credit Service Organizations (CSO).

CSOs provide retail financial products and services to Texas consumers. One of the services a CSO provides is locating and securing an independent third-party lender for customers who need small, short term loans. CSOs do not provide loans to consumers. The small, short term loans are underwritten using the criteria of an unaffiliated third-party lender.

CSAT member companies operate 2,400 offices across the state employing over 7,800 Texans. Members pay over $220 million in salaries and benefits to Texas employees. CSAT stores pay over $18.5 million in franchise and property taxes and $61 million in rent to Texas landlords.

There are CSAT member stores in every legislative district in the state of Texas. The customer base reflects that diversity. In one significant way --- **education** --- small, short-term loan borrowers are *atypical* Texans (56% have at least some college education compared to 52% of adult Texas residents).

Small, short-term loan customers are younger than Texans on the whole (71% fall between the ages of 26 and 55). Only six per cent (6%) of small loan customers are seniors. Nearly half (44%) of all small, short-term loan customers own homes.

In 2004, the United States Fifth Circuit Court of Appeals ruled CSOs were authorized to offer financial services in retail stores across the state under Chapter 393 of the Texas Finance Code. CSOs and the third-party lenders must comply with no less than twenty (20) federal and state laws and regulations applicable to small, short-term loans, including the Deceptive Trade Practices, Truth in Lending, and Debt Collection Practices Acts. Borrowers may file complaints against CSOs or lenders with the Attorney General, the Federal Trade Commission and against the surety bond held by the Secretary of State.

In 2010, Congress enacted the Dodd-Frank financial industry reform bill. A key part of the legislation was the creation of the Consumer Financial Protection Bureau (the "Bureau"). The Bureau has exclusive rulemaking, examination and enforcement authority over virtually every consumer lender and consumer credit transaction. Bureau organizers are currently hiring over 1,000 examiners and analysts to be fully operational by July.

Two of the Bureau's initial priorities are collecting and analyzing detailed loan and financial product data from consumer lenders and creating a nationwide consumer-complaint center. The law also establishes a government-backed loan loss reserve fund to encourage banks and credit unions to make small, short-term loans. Money appropriated by Congress to the fund will subsidize bank loan losses for small loans.

SB 251 and 253 eliminate access to credit through small, short-term loans to hard working Texans. By eliminating the ability to offer small, short-term loan services to their customers, SB 251 and 253 effectively and practically put all CSOs out of business.

The rate structure authorized in Chapter 342 of the Texas Finance Code is not sustainable for a business entity whose primary product is small, short-term loan services.

Chapter 342 authorizes a charge of $11.87 for a $100 loan with a 14 day term. With nationwide pre-tax costs averaging $13.70 per $100 loaned (store operating expenses, rent or property taxes, employee salaries and benefits, corporate expenses and loan loss reserves), CSOs would be forced to operate at a loss.

As loan amounts increase, the projected loss per loan increases substantially. Chapter 342 authorizes a charge of $15.60 for a $300 loan with a 14 day term. Pre-tax operating costs would be at least $42 (applying available national data) for the loan.

Thank you again for the opportunity to testify. I will try to answer any questions you may have.

CSAT CONSUMER SERVICE ALLIANCE OF TEXAS

CSAT State of Texas Profile

CSAT Member Stores:	2400
Employees:	7,800
Salaries and Benefits:	$220 million
Taxes (franchise and property) Paid:	$18.5 million
Rent Paid on Store Locations:	$61 million

www.consumerserviceallianceoftexas.org

Consumer Service Alliance of Texas

The *Consumer Service Alliance of Texas* (CSAT) is a trade association advocating for the preservation of financial choice based on personal responsibility for Texas consumers. CSAT represents the interests of consumers and Credit Service Organizations (CSO) across Texas.

Credit Service Organizations

Credit Service Organizations provide retail financial products and services to Texas consumers. From stores in neighborhoods across the state, hard-working Texans have access to small, short term loans; money orders; pre-paid telephone and debit cards and other services to help them manage their finances.

One of the services a CSO provides is locating and securing an independent third-party lender for customers who need small, short term loans for immediate financial needs. CSOs do not provide loans to consumers. The small, short term loans are underwritten using the criteria of the unaffiliated third-party lender.

Many CSOs also help consumers improve and rebuild their credit ratings by providing the opportunity for the successful repayment of their loans to be reported favorably to the Payment Reporting Builds Credit (PRBC ™) credit bureau.

Products and Services Offered at CSAT Stores: small, short term loans; money orders; prepaid phone and debit cards

Figures based on estimates for 2008 calendar year. Space limitations prohibited listing all community contributions. Not all products and services available at every store.

CSAT CONSUMER SERVICE ALLIANCE OF TEXAS

www.consumerservicealllianceoftexas.org

Consumer Protection Laws
Texas Credit Services Organizations

Credit Service Organizations provide retail financial products and services to Texas consumers. From stores in neighborhoods across the state, hard-working Texans have access to credit services to obtain to small, short term loans; money orders; pre-paid telephone and debit cards; and other services to help them manage their finances.

One of the services a CSO provides is locating and securing an independent third-party lender for customers who need small, short term loans for immediate financial needs. CSOs do not provide loans to consumers. The small, short term loans are underwritten using the criteria of the unaffiliated third-party lender, and are typically secured by the CSO's letter of credit or guaranty that backs up the consumer's promise to pay the lender.

Many CSOs also help consumers improve and rebuild their credit ratings by providing the opportunity for the successful repayment of their loans to be reported favorably to the Payment Reporting Builds Credit (PRBC)™ credit bureau.

Both the CSO and unaffiliated third-party lender must comply with an extensive array of federal and state consumer protection laws. Under these laws, a consumer may file complaints with the Texas Attorney General, the Federal Trade Commission, and against the bond or surety account on file with the Texas Secretary of State. Examples of these consumer protection laws are provided below:

Texas Credit Service Organization Act (*Tex. Fin. Code Chapter 393*). Under this statute, a credit service organization must register with the Secretary of State, post a $10,000 bond or surety account for each location if the CSO accepts any compensation in advance, provide full disclosure of fees and services before entering in a credit services contract with the consumer, and provide the consumer with a 3-day right to cancel the transaction without penalty or charge. Remedies include actual damages, potential punitive damages, attorneys' fees, and piggy-back application of the Texas Deceptive Trade Practices Consumer Protection Act.

Texas Deceptive Trade Practices – Consumer Protection Act (*Tex. Bus. & Comm. Code § 17.41 et seq.*). Chapter 17 of the Texas Business and Commerce Code provides consumers with special rights and remedies for damages or other relief, including potential economic damages and mental anguish under a standard of producing cause, treble damages in certain circumstances, and attorney's fees. Treble economic damages and damages for mental anguish may be awarded for knowing violations. Treble damages for mental anguish may be awarded for intentional violations.

Texas Constitution Art. XVI, §11 and *Texas Finance Code Chapter 302.* These laws provide lenders with stand-alone authority to make loans at a rate of 10% per annum or less, but subject to various consumer protection laws as outlined in this summary.

Federal Truth in Lending Act (15 USC § 1601 et seq.) and Regulation Z (12 CFR part 226). The CSO fee is included in the Finance Charge and Annual Percentage Rate disclosed by the lender to the consumer before a contract is entered into, not because the CSO fee any way compensates the lender for the use, forbearance or detention of the lender's short-term loan to the consumer, but because it is a cost of the loan for purposes of the federal statute's "comparison shopping" disclosures.

Texas Debt Collection Practices Act (Tex. Fin. Code Chapter 392) and Federal Debt Collection Practices Act (15 USC § 1692 et seq). These laws regulate debt collection practices.

Federal Equal Credit Opportunity Act (15 USC § 1691 et seq.) and Regulation B (12 CFR part 202). These laws prohibit discriminatory practices.

Federal Fair Credit Reporting Act (15 USC § 1681 et seq.) and Regulation V (12 CFR part 222). These laws regulate the use of credit information and require accurate credit reporting.

Federal Trade Commission Act. (*15 USC § 41 et seq.*). These laws authorize the Federal Trade Commission to regulate trade practices.

Federal Gramm-Leach-Bliley privacy laws (15 U.S.C. §§ 6801 et seq. & 6821 et seq.) and Federal Trade Commission Regulations (16 CFR part 313 and 16 CFR part 314). These laws provide for the protection of consumer non-public information.

CSAT CONSUMER SERVICE ALLIANCE OF TEXAS

Best Practices

CSAT Members follow these best practices for all Credit Service Organization ("CSO") transactions:

Full disclosure. A contract between a member and the customer must fully outline the terms of the credit services provided by the Member including the cost of the service. To the extent required by the Federal Truth in Lending Act, Members agree to ensure that the cost of the service is disclosed both as a dollar amount in the finance charge and as a component of the annual percentage rate ("APR") for any loan that a customer obtains through the Member's credit services.

Compliance. Members will comply with all applicable laws and regulations including registration with the Texas Secretary of State

Truthful advertising. Members will not advertise credit services in any false, misleading, or deceptive manner, and will promote only the responsible use of financial products and services.

Encourage consumer responsibility. Members will implement procedures to inform consumers of the intended use of their credit service.

Right to rescind. Members will give customers the right to rescind, at no cost, credit service transactions on or before three calendar days after the date of the credit service transaction.

Appropriate collection practices. Members must collect past due accounts in a professional, fair and lawful manner. Members will not use unlawful threats or intimidation to collect accounts. CSAT believes that the collection limitations contained in the Texas and federal Fair Debt Collection Practices Acts (FDCPA) should guide a member's practice in this area.

No criminal action. Members will not threaten or pursue criminal action against a customer as a result of the customer's default on a credit service agreement.

Enforcement. Members will participate in self-policing the industry. A member will be expected to report violations of these Best Practices to CSAT, which will investigate the matter and take appropriate action.

Military. To the extent that any Member does business with a Military "Covered Person" as defined by federal law, Members will comply with any federal and Texas laws on doing business with the military and related "Covered Persons."

Internet lending. Members that offer credit services to Texas consumers through the Internet must comply with the Texas Credit Services Organization statute and any other applicable laws and regulations applicable to the Member's business.

Display of the CSAT Membership Seal. Members shall prominently display the CSAT Membership Seal in all business locations to alert customers to the store's affiliation with the association and adherence to the association's Best Practices.

Notice Requirements. Members shall post a copy of CSAT's Best Practices in all business locations in a visible and conspicuous location.

Complaint Handling. Members will implement and maintain complaint handling procedures that include a timely review and response to customer complaints and concerns. Each member company agrees to maintain and post its own toll-free consumer hotline number in each of its business locations.

Consumer Financial Literacy. Members will make consumer financial literacy materials available to consumers in all business locations in any form prescribed by CSAT.

Addendum. There is an addendum of additional best practices for any CSAT Member who takes an auto title as security for a CSO transaction.

Auto Equity Best Practices

Any CSAT Member who takes an auto title as security for a CSO transaction also follows these additional best practices:

Collateral. Members will specifically inform the consumer that if the consumer pledges a vehicle as collateral, the consumer could lose the vehicle if the transaction is not fully repaid. This notice language will be presented in bold, conspicuous type in the loan documents. Alternatively, consumers will be required to initial this provision in the loan documents or on a separate notice.

Appraisal standards. Members will utilize nationally and or regionally recognized auto appraisal standards in valuing a vehicle.

Proper filing of liens. When perfecting a security interest in any auto title collateral, members will comply with all laws and regulations regarding the pledge of a vehicle as collateral, including:

- The proper filing of liens with the Texas Department of Transportation through the appropriate county assessor-collector's office; and
- The statutory duties in Chapter 9 of the Texas Business and Commerce Code regarding the disposition of collateral.

Notice about return of vehicle. Members will inform consumers in writing they can get their vehicle back at any time after default/repossession and before a sale by paying the amount owed.

Compliance. Members will comply with the Texas Business and Commerce Code and other applicable law when collecting vehicle-secured accounts, including:

- **Commercially reasonable manner.** Members will act in a commercially reasonable manner, without breaching the peace, in all aspects of the repossession and sale of the vehicle.

- **Written notice of opportunity to redeem vehicle.** Members will give consumers at least 15 days after repossession to redeem their vehicle prior to it being sold. Members will send a written notice to consumers informing them how and when their vehicle will be sold and what consumers need to pay to redeem their vehicle.

- **Reasonable expenses actually incurred**. With respect to expenses related to collection, repossession, and sale of the vehicle, Members will only charge reasonable expenses actually incurred.

- **Timely release of title.** Members will release the vehicle title to the consumer in a timely manner when the transaction is paid.

- **No personal liability.** Borrowers have no personal liability for auto equity loans, other than in instances of borrower fraud. Members shall not pursue legal action against borrowers if the amount owed exceeds the value of the collateral.

- **Refund of surplus sales amount.** Members will account for the proceeds of sale in a timely fashion, including refunding any surplus sales amount to the consumer.

- **Telephone number for more information.** Members shall provide a telephone number and address for consumers to call, or write, to get more information about the sale of their vehicle.

www.consumerservicealliance oftexas.org

FREQUENTLY ASKED QUESTIONS (FAQS)

What is the Consumer Service Alliance of Texas ?

The Consumer Service Alliance of Texas (CSAT) is a trade association advocating for the protection of financial choice based on personal responsibility for Texas consumers. CSAT represents the interests of consumers and Credit Service Organizations (CSO) across Texas.

What are Credit Service Organizations?

Credit Service Organizations provide retail financial products and services to Texas consumers. From stores in neighborhoods across the state, hard-working Texans have access to small, short term loans; money orders; pre-paid telephone and debit cards and other services to help them manage their finances.

One of the services a CSO provides is locating and securing an independent third-party lender for customers who need small, short term loans for immediate financial needs. CSOs do not provide loans to consumers. The small, short term loans are underwritten using the criteria of the unaffiliated third-party lender.

Many CSOs also help consumers improve and rebuild their credit ratings by providing the opportunity for the successful repayment of their loans to be reported favorably to the Payment Reporting Builds Credit (PRBC)™ credit bureau.

Does the CSO Charge Interest for These Services?

No. The CSO provides its services based on a fee schedule, which is predetermined and described in a written agreement signed by both the consumer and CSO. Fees for all retail financial services are determined by competition in the marketplace.

Is the Third-Party Lender Limited in the Amount of Interest or Fees Charged?

Yes. The maximum rate of interest for a small, short term loan is 10% per annum. A borrower is entitled, free of charge, to a ten day grace period before a late fee can be assessed for failure to repay. Late fees, if any, are capped at 5% of the amount unpaid. All additional fees associated with these loans are regulated by Chapter 302 of the Texas Finance Code.

What Is the Application Process for a small, short term loan?

A consumer begins the small, short term loan process by filling out a credit application at a CSO location. The information is then sent to the lender, who determines eligibility and approves or denies the loan based upon its underwriting criteria. Documents are signed and the loan funds are given to the consumer. Consumers have the option of repaying a small, short term loan in cash or by an ACH debit to a bank account.

Are There Consumer Protections in Place When Purchasing Retail Financial Products or Services from a CSO?

Yes, many. CSOs in Texas:

- Disclose the cost of the service they provide both as a dollar amount and as part of an annual percentage rate;
- Comply with all applicable laws and regulations including Chapter 393 of the Texas Finance Code;
- Allow consumers to change their mind about obtaining a small, short term loan for three days without charge;
- Only collect past due loans in a professional, fair and lawful manner; and
- Never threaten or pursue criminal action against a borrower because of a default.

What Consumer Safeguards Apply to Small, Short Term Loans from a Third-Party Lender?

An independent, third-party lender must comply with the all of the state and federal laws that govern unsecured consumer loans. These loans are subject to Article 16 of the Texas Constitution, Chapter 302 of the Texas Finance Code, the standards of the federal Truth in Lending Act, the Equal Credit Opportunity Act, the Fair Credit Reporting Act, the Debt Collection Practices Act, the federal regulations promulgated pursuant to those Acts along with the other laws that apply to consumer loans.

Can These Loans Be Issued to Military Personnel?

No. Recent changes to federal law prevent almost all forms of outside credit for military personnel and their families. Small, short term loans fall in that category.

Small, Short-Term Loan Talking Points

Jobs

- Consumer Service Alliance of Texas (CSAT) members operate 2,400 offices across the state employing over 7,800 Texans. Members pay over $220 million in salaries and benefits to Texas employees. CSAT member companies pay over $18.5 million in franchise and property taxes and $61 million in rent to Texas landlords.

Duplicate Federal Regulation

- Despite the need to focus on critical priorities including the budget deficit and redistricting, some members of the legislature are advocating for new, burdensome regulations for the small, short-term loan industry. These duplicative efforts are being pursued despite recent federal legislation enacting sweeping changes to accomplish the same results.

- The responsibilities and priorities of the new federal Consumer Financial Protection Bureau (CFPB) should be carefully evaluated before allocating state resources on duplicative activities.

Sunset Review

- The Texas Finance Commission will undergo sunset review during the 2011-2012 interim. Perceived gaps, if any, in the comprehensive federal regulatory scheme can be readily addressed during the sunset review process.

New Federal Agency

- The CFPB is the centerpiece of the recently enacted federal "Wall Street - financial industry reform" legislation. It was created to consolidate the responsibility for making consumer rules for financial products --- including home mortgages, student loans, small, short-term loans (including "payday loans"), credit cards, etc. --- under one federal agency.

- The CFPB has:

    - **Exclusive rulemaking authority** to prescribe rules to prevent "abusive practices" under every federal consumer financial law;

    - **Exclusive examination authority** over consumer lenders and financial services providers; and

    - **Exclusive enforcement authority** with respect to all consumer financial laws, subject to coordination with the Federal Trade Commission with respect to enforcement actions by each agency.

- Elizabeth Warren, a Harvard Law School professor and recognized consumer advocate, has been appointed to launch the CFPB.

- Warren and her staff are currently hiring over **1,000 examiners and analysts**.

- While staffing, data and complaint collection and planning activities are continuing, enforcement activity will begin in **July of 2011.**

- One of the first CFPB priorities is **collecting and analyzing detailed loan and financial product data** from consumer lenders and financial services providers.

- The law requires the CFPB to create a nationwide consumer-complaint center.

- The law also establishes a **government-backed loan loss reserve fund** to encourage banks to make small, short-term loans. A recent two-year FDIC pilot project proved banks cannot make small consumer loans profitably at 36% APR. The loss reserve fund will cover bank losses --- establishing a government subsidy for bank small loan programs.

Military

- CSAT member companies have processes and procedures (which are subject to internal, periodic audits) in place to ensure loans are not being made to active duty military personnel (or other "covered persons" as defined by federal law).

Finance Code – Chapter 342

- The rate structure authorized in Chapter 342 of the Texas Finance Code denies access to credit for hard-working Texan small, short-term loan borrowers.

  Data from U.S. Securities and Exchange Commission reports filed by publically traded companies offering small, short-term loans illustrates the costs of providing access to credit for hard-working Texans. Store operating expenses, corporate expenses, loan loss reserves and interest expense offset over 86% of the pretax revenue earned on every $100 loaned.

  Chapter 342 authorizes a charge of $11.87 for a $100 loan with a 14 day term. With costs averaging $17.24 per $100 loaned, borrowers would be denied access to small, short-term loans under Chapter 342 rates because costs exceed permitted charges.

  As loan amounts increase, projected Chapter 342 imposed losses increase. Chapter 342 authorizes a charge of $15.60 for a $300 loan with a 14 day term. With costs averaging $52.17 on a $300 loan, the projected loss increases substantially.

Background

The Consumer Service Alliance of Texas (CSAT) is a trade association advocating for the protection of financial choice based on personal responsibility for Texas consumers. CSAT represents the interests of consumers and Credit Service Organizations (CSO) across Texas.

Credit Service Organizations provide retail financial products and services to Texas consumers. From stores in neighborhoods across the state, hard-working Texans have access to small, short term loans; money orders; pre-paid telephone and debit cards and other services to help them manage their finances.

One of the services a CSO provides is locating and securing an independent third-party lender for customers who need small, short term loans for immediate financial needs. CSOs do not provide loans to consumers. The small, short term loans are underwritten using the criteria of the unaffiliated third-party lender.

1. **The rate structure authorized in Chapter 342 of the Texas Finance Code denies access to credit for hard-working Texan small, short-term loan borrowers.**

Data from U.S. Securities and Exchange Commission reports on the expenses of publically traded companies offering small, short-term loans illustrates the costs of providing access to credit for hard-working Texans. Store operating expenses, corporate expenses, loan loss reserves and interest expense offset over 86% of the pretax revenue earned on every $100 loaned.

Chapter 342 authorizes a charge of $11.87 for a $100 loan with a 14 day term. With costs averaging $17.24 per $100 loaned, Texans would be denied access to small, short-term loans under Chapter 342 rates.

As loan amounts increase, projected Chapter 342 losses for lenders and CSOs increase. Chapter 342 authorizes a charge of $15.60 for a $300 loan with a 14 day term. With costs averaging $52.17 on a $300 loan, the projected loss increases substantially.

2. **The CSO Act is recognized by the courts as appropriate for small, short-term consumer credit. The Act is not a loophole to evade state consumer lending laws.**

The United States Fifth Circuit Court of Appeals ruled CSOs were authorized to offer financial products and services in retail stores across the state under Chapter 393 (the "CSO Act") of the Texas Finance Code [Lovick v. Ritemoney, 378 F.3d 433 (5^{th} Cir. 2004)].

Under the Act:

- A $10,000 bond per store location is required.
- CSOs must register with the Secretary of State.
- CSOs must disclose all fees and charges for financial products.

- CSOs give every customer three days to change their minds without penalty or charge.
- Customers are entitled to actual damages, potential punitive damages, and attorneys' fees in actions against CSOs for violations of the Act.

Violations of the Act are also specifically subject to the Texas Deceptive Trade Practices Consumer Protection Act.

3. <u>CSOs and the lenders must comply with an extensive array of federal and state consumer protection laws, including</u>:

Texas Credit Service Organization Act (Texas Finance Code Chapter 393)
Texas Deceptive Trade Practices Consumer Protection Act
(Texas Business and Commerce Code Chapter 17)
Texas Constitution, Article 16
Texas Finance Code Chapter 302
Texas Business and Commerce Code, Article 9
Federal Truth in Lending Act
Regulation Z (12 CFR part 226)
Texas Debt Collection Practices Act (Texas Finance Code Chapter 392)
Federal Debt Collection Practices Act
Federal Equal Credit Opportunity Act
Regulation B (12 CFR part 222)
Federal Fair Credit Reporting Act
Regulation V (12 CFR part 222)
Federal Trade Commission Act
Federal Gramm-Leach-Bliley privacy laws
Federal Trade Commission Regulations (16 CFR parts 313 and 314)

4. <u>The costs of realistic alternatives for short term credit expressed in terms of APR are higher than those associated with small, short-term loans.</u>

<u>14 day term</u>	<u>APR</u>
$100 small, short-term loan with $15 fee	391%
$100 small, short-term loan with $20 fee	521%
$29 late fee on $100 credit card balance[1]	756%
$100 utility bill with $47 reconnect fee[2]	1,225%
$100 check with $30 NSF charge and $24 merchant fee[3]	1,408%
<u>10 day term</u>	
$100 utility bill with 5% late charge after 10 days[4]	1,825%
<u>1 day term</u>	
$100 ATM withdrawal with $1.44 fee[5]	526%

1 Consumer Action News, www.consumer-action.org
2 Utility Industry Survey
3 Sheehan, Scott, "Supply and Demand for Short-Term Loan Services" (2008).
4 See Sheehan
5 Bankrate.com

The maximum rate of interest for a small, short-term loan is 10% per annum (Texas Constitution, Article 16).

CSOs assist consumers in obtaining small, short-term loans from unaffiliated, third-party lenders. These loan services are considered "costs of the loan" under the Federal Truth-in-Lending Act and are included in the finance charge and APR (annual percentage rate) disclosed to the consumer before the loan is made.

The fees are not usurious. Interest rates are subject to usury laws. Fees are not. Fees for financial services are determined by competition in the marketplace.

Fees charged by banks, credit unions and utilities are not limited or capped. They are determined by competition in the marketplace. Those fees are not, however, required by law to be disclosed to consumers in an APR calculation for comparison shopping purposes because they are not considered "costs of a loan". They are the only realistic alternatives for consumers with an immediate financial need other than borrowing from family or friends.

The costs of realistic alternatives for short term credit expressed in terms of APR calculations are never discussed by those pushing for the elimination of the small, short-term loan market.

5. <u>Consumers are protected from unfair and deceptive business practices.</u>

A consumer may file a complaint against a CSO with the Federal Consumer Financial Protection Bureau, the Texas Attorney General's Office, the Federal Trade Commission and against the bond on file with the Texas Secretary of State.

Customers are entitled to actual damages, potential punitive damages, and attorneys' fees in actions against CSOs for violations of the Act. **Violations of the Act are also specifically subject to the Texas Deceptive Trade Practices Consumer Protection Act.**

6. <u>CSO retail locations provide thousands of jobs, with benefits, and contribute significantly to their local and state economy.</u>

• Employees:	7,800
• Salaries and Benefits Paid to Employees:	$220,000,000
• Taxes (franchise and property) Paid:	$18,500,000
• Rent Paid on Store Locations	$61,000,000

CSAT CONSUMER SERVICE ALLIANCE OF TEXAS

Banks and Credit Unions are *NOT* Realistic Alternatives to Small, Short-Term ("payday") Loans

Banks

In February 2008, the FDIC began a two-year pilot project on small dollar loan programs. The pilot was a case study designed to determine whether banks could offer small dollar loans at 36% APR, or less, as an alternative to higher-cost credit products such as payday loans and fee-based overdraft protection.

- **Given the small loan amounts, interest at 36% APR and fees charged are not sufficient to achieve profitability.**
- Most pilot banks sought to generate profitability by using small loans to cross sell additional products to the new small loan customers.
- Seventy-five percent (75%) of pilot bankers used small dollar loans to create goodwill in the community, not profits.
- Other pilot banks used small dollar loans as a strategy to generate favorable Community Reinvestment Act (CRA) ratings, not profits --- (high CRA ratings are required for bank acquisition and merger approval, among other strategic initiatives requiring regulator approval).
- Several small dollar loan programs featured "guarantees" in the form of loan loss coverage or linked, low-cost deposits provided by local governments (taxpayers) or charities.

[Source: FDIC Quarterly; 2010, Volume 4, No. 2]

Federal Legislation: Wall Street and Financial Services Reform - 2010

Congress has recognized banks cannot make small dollar loans at 36% APR profitably.

The new federal financial services reform law establishes a **government-backed loan loss reserve fund** to encourage banks to make small, short-term loans. The loss reserve fund will cover bank losses --- establishing a government (taxpayer) subsidy for bank small loan programs. Congress is expected to appropriate $7.5 million to start the fund.

[Source: Dodd-Frank Wall Street Reform and Consumer Protection Act, 2010]

Credit Unions

The Texas Credit Union League has launched the REAL Solutions short–term loan program for participating credit unions. Interest rates are capped at 18% APR and borrowers will be forced to put at least 10% of their loan proceeds into a savings account. As apart of the alliance, all credit unions will offer the same product and share in the pool of loans default risk.

- National data shows very few credit unions offer small loan products as an "alternative" to payday loans.

- Industry reports suggest those few credit unions offering small loan products seem unwilling or unable to undercut substantially the prices set by payday lenders.

- Industry reports also reveal that --- compared to standard payday loans --- the small dollar loans offered by credit unions generally carry greater restrictions on approval and repayment, meaning that the risk-adjusted prices for credit union payday loan alternatives may not be lower at all.

- To offset low APR requirements, credit unions do three things:

  (1) they offset low explicit APRs with per-loan processing fees or annual loan program fees;

  (2) they require "forced savings" where borrowers have to put part of their loan proceeds into an account, but still pay interest on the entire amount borrowed even though they do not have access to all of the money they have "borrowed"; and

  (3) impose restrictions on loan terms and customer access --- lowering default risk for the credit unions, but making substantially less credit available for Texas consumers.

- <u>A majority of current payday loan customers would prefer to borrow from pay day lenders even if a bank or credit union offered an identical product.</u>

- <u>There is little evidence that credit unions can offer a payday loan with competitive terms at lower prices.</u>

- There is no compelling evidence to suggest that risk-adjusted prices on standard payday loans are any higher than those on credit union payday loans.

  [Source: "Are Credit Unions Viable Providers of Short-Term Credit?"; Associate Professor Victor Stango, Graduate School of Management, University of California, Davis; February 3, 2010]

CSAT CONSUMER SERVICE ALLIANCE OF TEXAS

FACT BOOK

Table of Contents

17. Do customers complain about the small, short-term loan process?
18. Are CSOs and small, short-term loan lenders predatory?
19. Can CSOs be affiliated with the lenders that make small, short-term loans?
20. Is a 36% APR cap realistic, or would it effectively ban small, short-term loans?

2-15-09

FACT BOOK 1.

What are Credit Service Organizations?

Credit Service Organizations provide retail financial products and services to Texas consumers. From stores in neighborhoods across the state, hard-working Texans have access to small, short term loans; money orders; pre-paid telephone and debit cards and other services to help them manage their finances.

One of the services a CSO provides is locating and securing an independent third-party lender for customers who need small, short term loans for immediate financial needs. CSOs do not provide loans to consumers. The small, short term loans are underwritten using the criteria of the unaffiliated third-party lender.

Many CSOs also help consumers improve and rebuild their credit ratings by providing the opportunity for the successful repayment of their loans to be reported favorably to the Payment Reporting Builds Credit (PRBC)™ credit bureau.

FACT BOOK 2.

Are Credit Service Organizations (CSOs) authorized to offer retail financial products and services in Texas?

The United States Fifth Circuit Court of Appeals ruled CSOs were authorized to offer financial products and services in retail stores across the state under Chapter 393 of the Texas Finance Code [Lovick v. Ritemoney, 378 F.3d 433 (5^{th} Cir. 2004)].

CSOs must register with the Secretary of State under the Texas Credit Service Organization Act (Chapter 393 of the Texas Finance Code). Under the Act:

- A $10,000 bond per store location is required.
- CSOs must disclosure all fees and charges for financial products.
- CSOs give every customer three days to change their minds without penalty or charge.
- Customers are entitled to actual damages, potential punitive damages, and attorneys' fees in actions against CSOs for violations of the Act.
- Violations of the Act are also specifically subject to the Texas Deceptive Trade Practices Consumer Protection Act.

CSOs offer retail financial products and services, including assisting customers in obtaining small, short-term loans for immediate financial needs from independent, third-party lenders. The CSO issues a standby letter of credit or other surety arrangement that guarantees the customer's repayment of the loan.

The unaffiliated, third-party lender follows the provisions of Chapter 302 of the Texas Finance Code. Under Chapter 302, compensation to a lender is limited to an effective rate of interest not to exceed 10% per annum.

FACT BOOK 3.

What is the application process for a small, short term loan?

A consumer begins the small, short-term loan process by filling out a credit application at a CSO location. The information is then sent to an unaffiliated, third-party lender who determines eligibility and approves or denies the loan based upon its underwriting criteria.

The prices for all retail financial services, including small, short-term loans, are prominently displayed in all CSO stores. Disclosures of all fees and charges for small, short-term loans are in the written documents customers sign.

Small, short-term loan customers are not *un-banked* or *under-banked*. All applicants must have:

- A checking account;
- A photo ID; and
- A verifiable source of repayment.

Employment references are verified when listed as the source of repayment.

The underwriting criteria used to approve or deny a loan application varies from lender to lender. Applicants may not have more than one loan at a time and maximum loan amounts are based on an applicant's income or other verified sources of repayment.

Upon approval by the lender, documents are signed at the CSO store and the loan funds are given to the consumer. The loan funds are supplied by the lender and disbursed by the CSO. Consumers have the option of repaying a small, short-term loan in cash at a CSO store or by an automatic ACH debit to a checking account.

FACT BOOK 4.

What are typical terms of a small, short-term loan?

Loan amounts typically range from $50 to $1,750.

Loan terms typically range from 10 to 40 days. Borrowers have the option of repaying a small, short-term loan in person in cash, or by authorizing an ACH debit to a bank account.

Interest rates are limited to 10% per annum.

Fees for loan services provided by CSOs are market-based and typically range from $15 to $22 per $100 borrowed.

Borrowers may not have more than one loan at a time and maximum loan amounts are based on a borrower's income or other verified sources of repayment.

<u>Example – Terms of a Small, Short-Term Loan</u>

- $100 loan amount
- 14 day term
- $20 CSO fee (loan services, issuance of letter of credit)
- $0.46 interest at 10% per annum
- $120.46 due at maturity

FACT BOOK 5.

Are there existing consumer safeguards in place to protect CSO customers?

Both the CSO and unaffiliated third-party lender must comply with an extensive array of federal and state consumer protection laws. Under these laws, a consumer may file complaints with the Texas Attorney General, the Federal Trade Commission, and against the bond or surety account on file with the Texas Secretary of State. Examples of these consumer protection laws are provided below:

- *Texas Credit Service Organization Act (Tex. Fin. Code Chapter 393).* Under this statute, a credit service organization must register with the Secretary of State, post a $10,000 bond or surety account for each store location, provide full disclosure of fees and services before entering in a contract with a consumer, and provide the consumer with a 3-day right to cancel the transaction without penalty or charge. Remedies include actual damages, potential punitive damages, attorneys' fees, and piggy-back application of the Texas Deceptive Trade Practices Consumer Protection Act.

- *Texas Deceptive Trade Practices – Consumer Protection Act (Tex. Bus. & Comm. Code § 17.41 et seq.).* Chapter 17 of the Texas Business and Commerce Code provides consumers with special rights and remedies for damages or other relief, including potential economic damages and mental anguish, treble damages in certain circumstances, and attorney's fees.

- *Texas Constitution Art. XVI, §11 and Texas Finance Code Chapter 302.* These laws provide lenders with stand-alone authority to make loans at a rate of 10% per annum or less, subject to various consumer protection laws as outlined in this summary.

- *Federal Truth in Lending Act (15 USC § 1601 et seq.) and Regulation Z (12 CFR part 226).* The CSO fee is included in the Finance Charge and Annual Percentage Rate disclosed by the lender to the consumer before a contract is entered into, not because the CSO fee in any way compensates the lender for the use, forbearance or detention of the lender's short-term loan to the consumer, but because it is a cost of the loan for purposes of the federal statute's "comparison shopping" disclosures.

- *Texas Debt Collection Practices Act (Tex. Fin. Code Chapter 392) and Federal Debt Collection Practices Act (15 USC § 1692 et seq).* These laws regulate debt collection practices.

- *Federal Equal Credit Opportunity Act (15 USC § 1691 et seq.) and Regulation B (12 CFR part 202).* These laws prohibit discriminatory practices.

- *Federal Fair Credit Reporting Act (15 USC § 1681 et seq.) and Regulation V (12 CFR part 222).* These laws regulate the use of credit information and require accurate credit reporting.

- *Federal Trade Commission Act.* (15 USC § 41 et seq.). These laws authorize the Federal Trade Commission to regulate trade practices.

- *Federal Gramm-Leach-Bliley privacy laws (15 U.S.C. §§ 6801 et seq. & 6821 et seq.) and Federal Trade Commission Regulations (16 CFR part 313 and 16 CFR part 314).* These laws provide for the protection of consumer non-public information.

FACT BOOK 6.

Does a CSO charge interest for the retail financial services it provides?

No. A CSO provides its services based on a fee schedule, which is predetermined and described in a written agreement signed by both the consumer and the CSO. Fees and charges for a products and services are prominently displayed in all CSO locations.

Fees for all retail financial services are determined by competition in the marketplace.

FACT BOOK 7.

Is a lender limited in the amount of interest it can charge for a small, short-term loan?

Yes. The maximum rate of interest for a small, short-term loan is 10% per annum (Texas Constitution, Article XVI). A borrower is entitled, free of charge, to a ten day grace period before a late fee can be assessed for failure to repay. Late fees, if any, are capped at five per cent of the amount unpaid (Texas Finance Code, Chapter 302).

FACT BOOK 8.

Why are fees charges by CSOs for retail financial services provided included in the APR calculation for a small, short-termed loan?

CSOs assist consumers in obtaining small, short-term loans from unaffiliated, third-party lenders. These loan services, including issuing a standby letter of credit or other surety obligation to guarantee the repayment of the loan, are considered "costs of the loan" under the Federal Truth in Lending Act and Regulation Z.

The CSO fee is included in the Finance Charge and Annual Percentage Rate (APR) disclosed by the lender to the consumer before a contract is entered into, not because the CSO fee in any way compensates the lender for the use of its funds, but because it is a cost of the loan for purposes of the calculations required by the federal statutes "comparison shopping" disclosures.

FACT BOOK 9.

Who is the typical small, short-term loan customer in Texas?

The Cypress Research Group conducted a survey of over 400 randomly selected recent small, short-term loan borrowers in Texas in August and September of 2008.

In one important way --- **education** --- small, short-term loan borrowers are typical Texans (56% have at least some college compared to 52% of adult Texas residents).

Small, short-term loan customers are younger than Texans on the whole (71% fall between the ages of 26 and 55). Only six per cent (6%) of small loan customers are seniors.

Forty-four per cent (44%) of small, short-term loan customers own homes compared to 66% of all Texas adults.

More small, short-term loan customers are single when compared with all adult Texans (60% to 44%). However, while only one-third of Texas households have children living in them, nearly half (48%) of small, short term loan customer households have children.

Small, short-term loan customers earn less than all other Texans on average (43% earn between $25,000 and $50,000 compared to 27% of all Texans).

- 20% of small loan borrowers have household incomes in excess of $50,000
- 9% have household incomes in excess of $75,000

FACT BOOK 10.

What options do borrowers have if they cannot repay a small, short-term loan when it is due?

Small, short-term loan borrowers are much more financially astute than they are often portrayed in the media and by certain consumer advocacy groups. Most carefully weigh their options before applying for a small, short-term loan. **Over ninety per cent (90%) of small, short-term loans in Texas are paid when due, and ninety-five percent (95%) are eventually paid in full.**

If a borrower is unable to repay the entire loan amount when due, he or she can apply to refinance the outstanding balance with a new loan at the CSO store. The interest and fees from the original loan must be paid to be eligible to refinance.

Most borrowers make a partial repayment of the amount due and refinance the balance with a new loan. The amount of the principal repayment is determined solely by the borrower. The flexibility to decide how to repay the original amount borrowed helps borrowers manage their family budgets when unexpected financial needs arise.

Another option for borrowers is to request a repayment plan from their CSO.

Most CSOs offer similar types of repayment plans to their customers. The loan balance outstanding is typically divided into four equal payment amounts. No additional interest or fees are charged. The borrower is responsible for making payments after each of their next four pay periods.

FACT BOOK 11.

What is the economic impact of the small, short-term loan industry in Texas?

The Consumer Service Alliance of Texas (CSAT) is a trade association advocating for the preservation of financial choice based on personal responsibility for Texas consumers. CSAT represents the interests of consumers and CSOs across Texas.

Over ninety percent (90%) of the CSO stores in Texas are operated by CSAT member companies.

There is a CSAT member store in every legislative district in Texas.

- Number of CSAT Member Stores: 2,400
- Employees: 7,800
- Salaries and Benefits Paid to Employees: $220,000,000
- Taxes (franchise and property) Paid: $18,500,000
- Rent Paid on Store Locations $61,000,000

FACT BOOK 12.

What are the costs of other options for consumers with immediate financial needs compared to small, short-term loans?

Consumers have choices when faced with an immediate need for money:

- Borrow from family or friends;
- Pay utility or other bills late (and eventually incurring late charges);
- Bounce a check or overdraw a debit card (and eventually incurring NSF fees);
- Bounce a check on an account with overdraft protection (and eventually incurring fees);
- Use a credit card;
- Obtain a loan from a pawnshop;
- Obtain a small, short-term loan from a CSO and a third-party lender; or
- Do without (if possible).

The Cypress Research Group conducted a survey of over 400 randomly selected recent small, short-term loan borrowers in Texas in August and September of 2008. According to the study, **85% of the consumers considered at least one other viable option before choosing a small, short-term loan**, the most common being "allowing bills to be late" (35%), "asking friends or family" (15%), or bouncing a check and using overdraft protection (15%).

Claims that small, short-term loan customers are "desperate", "have no where else to turn", and "are taken advantage of by predatory practices" are simply untrue. **Choosing a short-term loan service is a <u>valid</u> and <u>reasonable</u> <u>choice</u> based upon both economic and personal factors of importance to consumers.**

[Next page for APR Cost Comparison]

APR Cost Comparison of Options for Immediate Financial Needs

14 day term

$100 small, short-term loan with $15 fee	391%
$100 small, short-term loan with $20 fee	521%
$29 late fee on $100 credit card balance[1]	756%
$100 utility bill with $47 reconnect fee[2]	1,225%
$100 check with $30 NSF charge and $24 merchant fee[3]	1,408%

10 day term

$100 utility bill with 5% late charge after 10 days[3]	1,825%

1 day term

$100 ATM withdrawal with $1.44 fee[4]	526%

[1] Consumer Action News, www.consumer-action.org
[2] 2002 Utility Industry Survey
[3] Sheehan, Scott, "Supply and Demand for Short-Term Loan Services" (2008).
[3] See Sheehan.
[4] Bankrate.com

FACT BOOK 13.

Is the typical small, short-term loan borrower "trapped in a cycle of debt" repaying on average $793 for a $325 loan?

No. Data compiled from millions of small, short-term loans made across the country in the last several years simply does not support this assertion about fees paid made by the Center for Responsible Lending ("CRL") in its report on payday lending.

According to Veritec[5] in its analysis of the CRL Report, **"The CRL conclusion above is based on an assumption that borrowers in these states never pay off their first payday loan and that the loan is somehow "extended" by the lender for the entire year."**

For example, the typical small, short-term loan borrower in Oklahoma pays, on average, $44.75 to borrow $357.44.

The average Oklahoma borrower during the one-year reporting period took out or refinanced a small, short-term loan 8.9 times per year. Total annual fees for the average Oklahoma borrower were approximately $402.75 to gain access to an average loan of $357.44 at nine different times during the year.

Veritec concludes, **"Consideration of the above information may indicate that the typical borrower "moves in and out of the product" with several loans taken out over a period of a few months followed by a period when the borrower is out of the product for several weeks or months."**

---

[5] Veritiec Solutions LLC is a regulatory services company that manages the statewide lender compliance programs in state with statewide databases containing data about small, short-term loans. Veritec does not supply any products or services to the small, short-term loan industry and its primary customers are state regulatory agencies.

Veritec's white paper analysis of the CRL small loan report concluded, **"Veritec is concerned certain conclusions derived in the CRL Report are a misinterpretation of statistical information published by Veritec as referenced.**

FACT BOOK 14.

Do CSOs make huge profits gouging customers?

No. CSO profits are consistent with other retail industries with multiple storefront locations spread across wide geographic areas. Stiff competition within the small, short-loan industry also keeps the market-based fees comparatively low.

Average Publically Traded CSO[6] Expenses Expressed per $15 Fee

	Dollars
Revenue	$15.00
Provision for Doubtful Accounts (Bad Debt)	$2.53
Operating Salaries and Related Payroll	$4.09
Occupancy Costs	$1.66
Other Selling Expenses	$2.43
Total Store Expenses	**$10.71**
Corporate Overhead Expenses	$2.42
Income Before Income Taxes	$1.87
Income Tax Expense	$0.88
Net Income	**$0.99**

[6] Data from 2006 U.S. Securities and Exchange 10K Reports

FACT BOOK 15.

How do CSO profits compare to other businesses?

CSO profits are consistent with other retail industries with multiple storefront locations spread across wide geographic areas. Stiff competition within the small, short-loan industry also keeps the market-based fees comparatively low.

Comparison of Net Income as a Percentage of Revenues
Recognizable Companies and CSOs[7]

Stock Symbol	Company	Percent of Revenues	For the Period Ending
HLT	**Hilton Hotels Corp.**	**7.0%**	12/31/06
HRB	**H & R Block, Inc.**	**10.1%**	04/30/06
APPB	**Applebee's Intl.**	**6.0%**	12/31/06
LUV	**Southwest Airlines Co.**	**5.5%**	12/31/06
HBI	**HanesBrands, Inc.**	**3.3%**	07/01/06
HD	**Home Depot, Inc.**	**6.3%**	01/28/07
HPQ	**Hewlett-Packard Co.**	**6.8%**	10/31/06
SJM	**The J.M. Smucker Company**	**6.7%**	04/30/06
JBHT	**JB Hunt Transport Services, Inc.**	**6.6%**	12/31/06
TM	**Toyota Motor Corp.**	**6.5%**	03/31/06
LOW	**Lowe's Companies, Inc.**	**6.7%**	02/03/07
KSS	**Kohl's Corp**	**7.1%**	01/28/06
DBRN	**Dress Barn, Inc.**	**6.1%**	07/29/06
JCP	**J C Penney Corporation**	**5.8%**	01/28/06
66258	**Self-Help Credit Unions**	**22.0%**	12/31/06
Average of 12 Select Credit Unions (including Military-focused CU's)		**16.0%**	
Average of Top Ten Bank Holding Companies		**27.0%**	
Average of Five Publicly Traded CSOs		**7.2%**	

[7] Data from 2006 U.S. Securities and Exchange Commission 10K Reports for five publicly traded CSOs

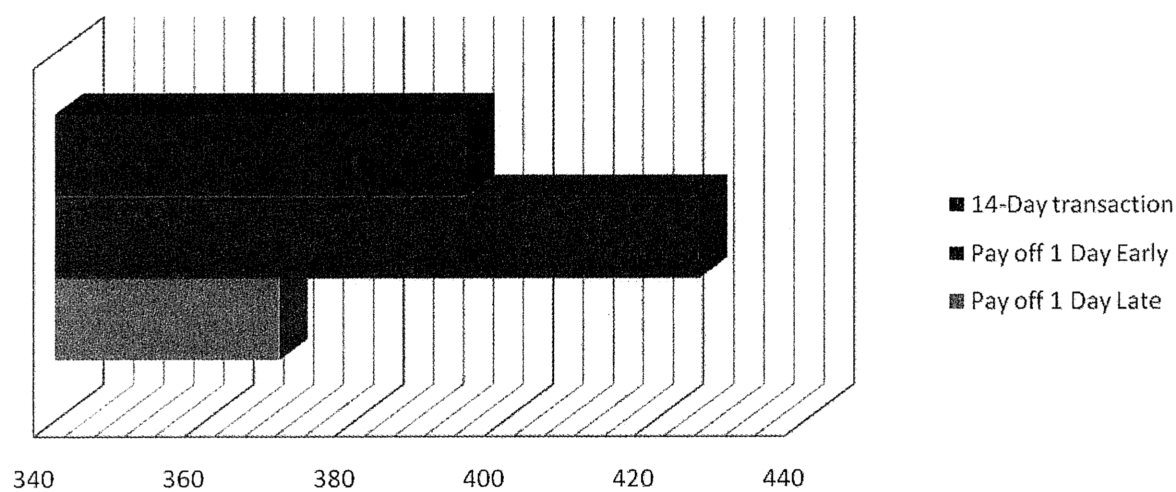
FACT BOOK 16.

Is an Annual Percentage Rate (APR) calculation an accurate representation of the cost of a small, short-term loan?

No. APR disclosures, while required by federal law, are misleading for short term loans and other extensions of credit. For example, a typical small, short-term loan with a $15 fee and a term of $14 days results in an APR calculation of 391% (blue bar in the chart below).

In fact, the loan would have to be renewed every two weeks for an entire year to actually realize an *annual* rate of return. If the loan was paid off one day early, the APR would jump 30 percentage points to 421% (red bar in the chart below). If the loan was repaid one day late, the APR would decrease 26 percentage points to 365% (green bar in the chart below). **However, in all three instances, the fee is still $15.**

Fees and interest paid per $100 borrowed is a more understandable way to represent the costs of short term loans, bounced check fees, debit card charges and ATM fees.



Take for example, the real cost of a fishing rod at WalMart. If a fishing rod has a 30% mark-up on top of a wholesale price of $100, it sells for $130. If the rod stays on the store shelp for two weeks before being purchased, WalMart would realize a 728% APR yield. If the fishing rod was purchased after seven days on the shelf, WalMart would have an APR return on its investment of 1564% --- which is very misleading.

It is still "*Always Low Prices, Always*" because the $30 mark-up does not change.

FACT BOOK 17.

Do customers complain about the small, short-term loan process?

There are very few customer complaints about small, short-term loans, CSOs or the unaffiliated third-party lenders.

Both the CSO and unaffiliated third-party lender must comply with an extensive array of federal and state consumer protection laws. Under these laws, a consumer may file complaints with the Texas Attorney General, the Federal Trade Commission, and against the bond or surety account on file with the Texas Secretary of State. Some consumers also contact the Office of the Texas Consumer Credit Commissioner with questions or complaints. With hundreds of thousands of transactions per year, the agencies have consistently logged less than 50 complaints per year.

CUSTOMER COMPLAINTS BY STATE
(Statistics Derived From State-Specific Regulatory Agencies)

Arizona: In 2006, there were 11 complaints involving small, short-term loans

Colorado: The state does not distinguish between individual types of consumer lenders. However, in 2005 there were 253 total complaints against consumer lenders.

Florida: The state does not distinguish between individual types of consumer lenders. However, in 2005 there were 215 total complaints against consumer lenders.

Idaho: In 2006 there were 43 complaints filed against small, short-term loan lenders. The majority of these complaints were regarding unlicensed lenders.

Indiana: In 2006 there were 19 complaints involving small, short-term loans.

Kentucky: In 2005 there were 12 complaints involving small, short-term loans.

Michigan: The state does not distinguish between individual types of consumer lenders. However, in 2005 there were 986 total complaints for all consumer lenders.

Missouri: In 2006 there were an estimated 10 calls per day involving small, short-term loans. Most of these calls were answered by explaining the law to the caller. While the Office does not distinguish between "questions" and "complaints", the complaints received involved such issues as collection tactics, proper crediting of payments and "customers being unable to make payments due to the store location being closed".

Montana: In 2006, there were 10 complaints involving small, short-term loans. Two complaints were against licensed small, short-term loan lenders and 8 complaints were against internet small, short-term loan lenders that were unlicensed.

New Mexico: In 2005, there were 11 complaints against small, short-term loan lenders.

North Dakota: In 2006, there was 1 complaint against a small, short-term loan lender. The customer was upset because his loan application was denied. However, his requested loan amount was over the allowable loan limit.

Oklahoma: In 2006, there were 68 complaints against small, short-term loan lenders.

Ohio: In 2006, there were 13 complaints against small, short-term loan lenders.

Tennessee: The 2005 DFI Annual Report shows that no complaints were filed against small, short-term loan lenders.

Virginia: In 2006, there were 53 total complaints; 39 with licensed lenders; and 14 for unlicensed lenders.

Wisconsin: The state does not maintain this information for specific industries. They group all consumer loans under the category of mortgages and are unable to distinguish small, short-term loan lenders from others.

South Carolina: The state does not maintain this information for specific industries. They group all businesses together and are unable to distinguish small, short-term loan lenders from others.

Washington: In 2005, there were 64 complaints against small, short-term loan lenders.

FACT BOOK 18.

Are CSOs and small, short-term loan lenders predatory?

No.

"These short-term financial services are *not predatory*, provide meaningful benefits, are subject to price competition, and taking them away harms consumers."

Donald P. Morgan, Federal Reserve Bank of New York

"You cannot call [small, short-term loan] companies predatory unless you compare their bottom-line percentage profits to other industries' bottom-line profits. **In that case, you'd also have to call Wrigley's Chewing Gum, General Electric, Mattel, and the International House of Pancakes predatory!"**

Allan Jones, Founder and CEO of Check Into Cash

In 2006, Jones released a study comparing the earnings of five publicly traded CSOs to the earnings of other publicly traded retail product and service providers. Jones commissioned the study in response to claims by the Center for Responsible Lending that CSOs and small, short term loans lenders are "predatory and their profits exorbitant".

- In 2006, IHOP Corp earned a 12.6% profit, nearly double that of the average of the five publicly traded CSOs (6.6%).
- The average profit margins of the top banks were 26.52% in 2006, four times higher and 301% greater than those of the publicly traded CSOs.

Jones calls the Center for Responsible Lending claims, "unfounded and irresponsible".

"CRL is a well-funded, anti-free enterprise group that disguises itself as a consumer advocacy organization. **The truth is that CRL was created by the Self Help Credit Union, a credit union that stands to make huge monetary gains** (from bounced check fees, debit card fees and ATM fees) **if [small short-term loans] are banned,"** adds Jones.

FACT BOOK 19.

Can Consumer Credit Organizations (CSOs) be affiliated with the lenders that make small, short-term loans?

No. CSOs and third-party lenders must be unaffiliated with no common ownership; no common directors, officers and employees; and no financial relationship of any kind between the two entities.

The CSO business model is based upon established Texas law that distinguishes between loan services by the CSO (e.g., assisting to arrange a loan, issuing a letter of credit, or guarantying a loan) and a loan by an independent third-party lender at the constitutionally capped rate of 10% per annum.

- All loans must be evaluated and approved based on criteria established by the lender.
- The lender's loan documents must conform to the requirements of Chapter 302 of the Texas Finance Code.
- The lender's funds must be the funds lent.
- The lender may not share directly or indirectly in CSO fees or other permitted charges.
- The CSO may not share directly or indirectly in the lender's interest charges or other permitted charges.
- The CSO is not authorized to act as the lender's general agent. However, the CSO may act solely as a special limited agent of the lender related to specific matters expressly approved in writing by the lender.

FACT BOOK 20.

Is a 36% APR cap realistic, or would it effectively ban small, short-term loans?

A thirty-six percent (36%) annual percentage rate (APR) cap would ***ban*** small, short-term loans in Texas.

CSOs assist consumers in obtaining small, short-term loans from unaffiliated, third-party lenders. The loan services provided by a CSO, including issuing a standby letter of credit or other surety obligation to guarantee the repayment of the loan, are considered "costs of the loan" under the Federal Truth in Lending Act and Regulation Z.

The CSO fee is included in the APR calculation because it is a cost of the loan for purposes of the "comparison shopping" disclosures required under the federal law.

It costs a small, short-term loan customer $15 to $22 in interest and fees to borrow $100 for anywhere from fourteen to forty days. **A 36% APR cap would limit the amount a customer could repay for a loan of $100 for fourteen days to $1.38**. If the customer only needed the money for seven days, the maximum amount the customer could repay under a 36% APR cap would be $0.69.

The chart below illustrates how a modest return on a typical small, short-term loan becomes a ***significant loss*** under a 36% APR cap.

	Small Short-Term Loan	Capped at 36% APR
Annual Percentage Rate (APR)	*391%*	*36%*
Revenue	**$15.00**	**$1.38**
Provision for Doubtful Accounts (Bad Debt)	$2.53	$2.53
Operating Salaries and Related Payroll	$4.09	$4.09
Occupancy Costs	$1.66	$1.66
Other Selling Expenses $2.43 $2.43		
Total Store Expenses	**$10.71**	**$10.71**
Corporate Overhead Expenses	$2.42	$2.42
Income Before Income Taxes	$1.87	($11.75)
Income Tax Expense	$0.88	$0.00
Net Income / (Loss)	**$0.99**	**($11.75)**