Testimony in Support of Bill Relating to Minimum Wage: HB5802
House Committee on Finance
March 11, 2021

The **Economic Progress Institute** supports Representative Lombardi's bill **H5802**, which would limit the harms of deferred deposit transactions that drive the payday loan industry in Rhode Island. *This bill would cap payday loans with APRs of 28 percent, in contrast to the 260 percent rates charged currently.* This bill also helps by extending the repayment period and limits excessive fees.

Payday loans, such as those permitted in Rhode Island, are high-cost loans structured to perpetuate an ongoing cycle of debt. The **debt trap** is integral to the success of the payday lending model, with "75% of all payday loan fees… generated from borrowers with more than 10 loans a year."[1] The federal **Consumer Financial Protection Bureau** (CFPB) has done extensive research on payday lending practices, finding that the average payday loan consumer gets caught in **a cycle of debt** (see *Figure 1*), taking out 10 loans per year due to an inability to pay off the balance with the constantly growing fees.[2] In brief, , the **Center for Responsible Lending** (CRL) explains, "payday lenders are actually providing access to debt, not credit."[3]

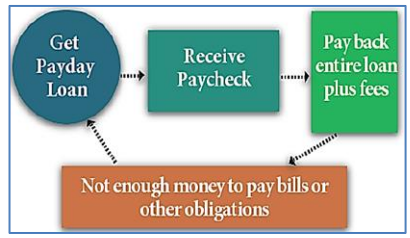

Figure 1: The Payday Loan Cycle of Debt

Consumers relying on payday lenders face considerable harm associated with payday loans, including increased difficulty paying bills, delayed medical spending, involuntary bank account closure, higher likelihood of filing for bankruptcy, and decreased job performance.

Payday lenders also increase wealth disparities by disproportionately targeting people of color, as *Figure 2* demonstrates.

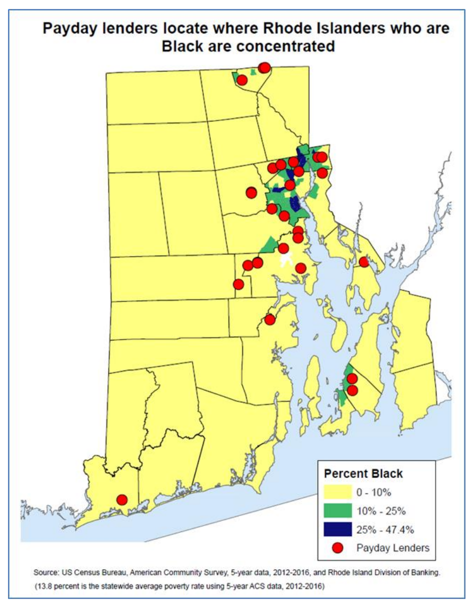

Figure 2: Locations of Payday Lenders in RI

Industry advocates claim that payday lending meets a need that is not otherwise adequately addressed. However, there exist <u>better options</u>. Bank of America recently introduced a new product, short-term loans of up to $500, with only a flat $5 loan fee and no overdraft fees, and effective APRs between 6 and 30 percent.[4] It seems likely that other large banks will follow with similar products.

Also in Rhode Island, the **Capital Good Fund**, with its mission "to create pathways out of poverty through equitable financial services," offers emergency loans valued between $300 and $500 with an APR of 10 percent, as well as monthly repayment over one year and no closing fee. This stands in stark contrast with payday loans and their APRs of up to 260 percent. Even putting money on a credit card, with an APR of 23.74 percent, compares favorably with payday loans.[5]

Nationally, 17 states and the District of Columbia enforce laws with rate caps of 36 percent or lower, protecting close to 100 million consumers from the predatory lending practices of payday lenders. Among the states in the Northeast, only Maine, Delaware, and Rhode Island still allow payday lending (*Figure 3*). In recent years, the CFPB has been moving to enact regulations extending protections to all states, but as CFPB's commitment to protecting consumers has shifted under new leadership, states wanting to protect their residents from payday lending practices need to take legislative action.

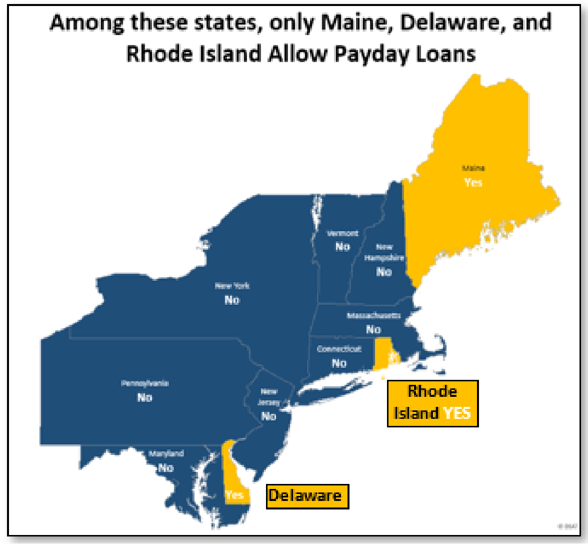

Figure 3: Source: Center for Responsible Lending, 2017

The **Center for Responsible Lending** estimated in 2019 that consumers in New England states that do not permit payday lending save a total of $252.7 million each year. Conversely, in Rhode Island, consumers face fees of **$7.6 million a year** due to payday lending, accounting for 93 percent of all payday lending fees in New England.

After the U.S. Defense Department determined that predatory lending "undermines the military readiness," **Congress acted in 2006 to protect active duty military personnel by capping loans to such individuals at 36 percent.**

Rhode Island should follow the lead of the Defense Department and cap loans at least at 36 percent. Payday loans are harmful to consumers and hurt the economy. HB5802 would provide Rhode Islanders with valuable protections from the predatory loan industry, and we urge you to pass this bill.

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[1] Diane Standaert, Delvin Davis, and Charla Rios, *Payday and Car Title Lenders Drain $8 Billion in Fees Every Year*, 2019. (Center for Responsible Lending).

[2] Consumer Financial Protection Bureau, *Payday loans and deposit advance products: a white paper of initial data findings*, 2013. Cited in Delvin Davis and Susan Lupton, *States without Payday and Car-title Lending Save Over $5 Billion in Fees Annually*, 2017. (Center for Responsible Lending). For a Rhode Island example of the cycle of debt, see Derek Thompson, "When You're Poor, Money is Expensive," *The Atlantic*, July 2014, https://www.theatlantic.com/business/archive/2014/07/its-expensive-to-be-poor-money/374361/: The article begins with the story of Alex and Melissa, from Scituate, Rhode Island. A sudden medical emergency pushes them to succumb to the payday lending trap. After seeking an initial loan of just $450, they soon found themselves "trapped in a cycle of dependency…[facing] more than $1,700 in fees."

[3] Center for Responsible Lending, "Fact v. Fiction: The Truth about Payday Lending Industry Claims," January 1, 2001, https://www.responsiblelending.org/research-publication/fact-v-fiction-truth-about-payday-lending-industry-claims.

[4] Lisa Rowan, "New Small-Dollar Loans From Bank Of America Offer Alternative To Expensive Payday Loans," Forbes, October 14, 2020, https://www.forbes.com/sites/advisor/2020/10/14/new-small-dollar-loans-from-bank-of-america-offer-alternative-to-expensive-payday-loans/?sh=2bbba8d92306.

[5] The national organization Bank On, with 74 coalition members in 30 states and the District of Columbia, works to increase the range and number of safe and affordable banking options for low-income borrowers. Bank On's goal "is to ensure that everyone has access to a safe and affordable bank or credit union account." See https://joinbankon.org/.