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TO: Special Committee on Financial Institutions and Insurance

FROM: Jennifer Cook, Deputy Commissioner
Consumer and Mortgage Lending Division
Office of the State Bank Commissioner

DATE: October 11, 2017

RE: HB 2267 and the Uniform Consumer Credit Code (UCCC)

The Office of the State Bank Commissioner (OSBC) appreciates the opportunity to provide testimony on HB 2267 regarding changes to the Uniform Consumer Credit Code (UCCC or Code). While the OSBC is neutral on HB 2267, the agency has significant concerns about amending the UCCC due to the CFPB's issuance of a final rule on October 5, 2017 that impacts certain consumer credit lenders nationwide. The OSBC believes it would be prudent to fully review the impact of the rule before proceeding with any changes to the Code.

The UCCC is the primary state law that governs consumer credit transactions, which include consumer loans, credit sales, and leases. A consumer loan is defined by statute as any loan made to an individual for personal, family or household use. Consumer loans may include auto loans; payday, title, and installment loans (also referred to as "small dollar loans"); open-end lines of credit such as home equity lines of credit (HELOCs); high loan-to-value mortgages and second mortgages. A consumer loan with an annual percentage rate (APR) over 12% is a supervised loan under the Code and non-bank companies offering such loans are required to license with the OSBC.

Non-bank companies that enter into consumer credit transactions (consumer loan, sale, or lease) when the APR is less than 12% or take assignment of the transaction and collect payments or enforce rights against debtors, are required to annually file with the OSBC. Known as "credit notification filers," these entities include buy here/pay here auto dealers, auto finance companies, furniture stores, jewelry stores, hospitals, dentists' offices, and other merchants that extend credit.

While certain products offered by depository institutions are subject to the Code depending on the characteristics of the product (e.g. consumer loans, credit sales, and leases), depository institutions are not required to license under the UCCC due to their chartered banking authority under state or federal law. A depository institution's primary regulator may be the OSBC, another state, or a federal agency.

The UCCC defines how credit transactions may be structured, specifies the information required to be provided to the consumer in writing, and sets limitations on fees, interest, and other charges. The UCCC authorizes the OSBC to regulate non-depository entities that offer products to which the UCCC applies. The agency's regulatory responsibilities are exercised in accordance with the parameters set by state law and regulation.

As drafted, HB 2267 presents potential challenges and ambiguities that would impact the OSBC's ability to appropriately regulate certain financial products authorized under the UCCC. The OSBC respectfully notes the following:

- The bill includes costs of "ancillary products" in the total cost of the loan. However, HB 2267 does not define this term and there is no definition in the UCCC. The UCCC under K.S.A. 16a-2-404(10) currently prohibits certain additional charges and the sale of any products in connection with a loan made pursuant to K.S.A. 16a-2-404. Absent a definition or clarification, the provision creates confusion about what, if any, ancillary products and related costs are permissible, which could also lead to unanticipated costs for consumers. Further, the ambiguity creates a scenario where the regulator, without statutory guidance, would be required to referee in this area.

- The bill provides multiple variables to set a loan term and maximum finance charges, which makes it difficult to determine which terms constitute a compliant transaction.

- In addition, the bill defines "instrument" to include "nonpurchase vehicle security." The bill further provides that a lender may hold the instrument for some period of time before depositing or negotiating the instrument. It appears this provision references an auto title in which a consumer's auto could be repossessed for non-payment of a loan taken under K.S.A. 16a-2-404.

- HB 2267 places new requirements on the OSBC to collect and publish data collected from lenders annually. The OSBC currently collects certain information at least annually from lenders, and could request additional information as directed. However, Sec. 2(14) contains terms that are not defined in the bill, in the UCCC, or in other state statutes. The lack of definitions may cause consumer and industry and confusion. Undefined terms include "average experienced annual percentage rate" and "other nonprivate information."

- The bill permits a payday lender to assess a return check charge the lesser of 5 percent of the original loan principal or $20 plus "any amount passed from another financial institution." Current law does not permit a return check charge passed on from a financial institution to be charged to the consumer. The language adds complexity to the amount allowed as well as burden to both the lender and the regulator to ensure compliance. "Any amount" allowed by a financial institution is not capped and is an unknown.

- Finally, HB 2267 directs the OSBC to develop rules and regulations to verify monthly income. The bill provides limited guidance in this area. The OSBC would respectfully request additional guidance about what constitutes satisfactory proof of monthly income. In addition, the agency would seek guidance as to whether any other documentation would be effective documentation of net monthly income. Restricting verification to a recent paycheck may not reflect other income available to the borrower, or may not take into consideration seasonal employment or other nontraditional means of employment or earnings. This provision is not as comprehensive, and potentially contradictory, to the ability-to-repay provisions required by the CFPB rule.

In addition, the OSBC has several broader observations. While the agency appreciates the opportunity to comment on HB 2267, and understands the interest in addressing this issue, several provisions in the bill add complexity to the Code, and it is not clear how HB 2267 would interact with the CFPB rule. The CFPB rule will make dramatic changes to the availability and type of small dollar loan products offered. The CFPB provides a 21 month implementation period, a recognition of the complexity of the rule and the significant changes that lenders will need to make to comply with the rule.

The UCCC is a complex statute that governs the activities of a broad range of consumer credit providers in the state from payday and small dollar lenders, to auto finance companies and providers of certain mortgage products. A number of the provisions of the UCCC interact with one another and impact multiple industries and consumer credit products.

Many types of consumer credit products exist today that were not contemplated when the UCCC was first enacted in 1974. The Code needs to be updated to reflect these changes in consumer borrowing, and to anticipate the evolving nature of consumer credit lending. Comprehensive modernization of the UCCC would benefit consumers and the many industries regulated by the statute, while also improving the ability to regulate consumer credit products that are offered under the UCCC.

Comprehensive UCCC modernization, which incorporates any necessary changes as a result of the CFPB rule, is the most prudent approach. This approach would allow the agency to consult with a range of stakeholders and develop a proposal that recognizes the significant changes that have occurred in consumer lending in recent years. Without a comprehensive approach to modernizing the Code, there is a risk of unintended consequences that could arise if only specific portions of the statute are amended, which have the potential to significantly disrupt, or create greater complexity for consumer borrowing in Kansas.

The OSBC appreciates the opportunity to offer testimony on HB 2267 and the UCCC. The OSBC seeks to carry out its regulatory responsibilities in a consistent manner, guided by clear statutory authority, in a way that ensures regulatory certainty and protects consumers.