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New York City Department of Consumer Affairs

Before the
New York State Banks and New York State Assembly Banks and Consumer Protection Committees

Hearing on
Online Lending

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Introduction and Background

The New York City Department of Consumer Affairs (DCA) submits this testimony for the consideration of the Senate and Assembly. We thank both bodies for the opportunity to comment about the growth of online lending, an issue that DCA, as the largest municipal consumer protection agency in the country, has been monitoring.

DCA's mission is to protect and enhance the daily economic lives of New Yorkers to create thriving communities. We serve New York City's consumers, businesses, and working families, enforcing laws and providing services that address the needs of New Yorkers, from their wallets to their workplaces.

Within DCA, the Office of Financial Empowerment (OFE) educates, empowers, and protects residents and neighborhoods with low incomes so they can improve their financial health and build wealth. We use data and research, policy development, and engage in partnerships to advance our mission. OFE also operates the City's Financial Empowerment Centers (Centers) that offer free, high-quality, one-on-one counseling and coaching. Since inception, our counselors have served over 40,000 clients; helping them reduce their overall debt by more than $50 million and helping them increase their savings by more than $4 million.

Through our financial empowerment work, as well as our regulatory and enforcement work in the consumer protection context, we know that lending – a critical lifeline for millions that also helps grow and sustain our economy – can be a double-edged sword. While on one hand, it enables New Yorkers to buy their first car or home; or pay for school or other necessities, it often takes very predatory forms, as well.

Predatory loans often have unclear or confusing terms. High-pressure sales tactics, especially targeting those in need of money in short order – often leave consumers saddled with loans they don't understand and often can't afford. Victims of predatory lending may be forced to forego educational opportunities and delay or abandon other necessary investments in their careers, families, and futures. Ruined credit scores can prevent victims from accessing mainstream financial products, purchasing a home, or, in many jurisdictions, securing new employment opportunities, robbing them of the chance to improve their lives and deepening the cycle of debt. Predatory lenders also often target minority communities where use of alternative financial services is higher, English proficiency is lower, and more individuals are likely to lack access to a bank account or other basic mainstream financial services.

DCA's Approach

As part of our mission, DCA employs a multi-pronged approach of education, enforcement, and education to protect New Yorkers from predatory and deceptive business practices across a variety of industries, including banking, credit, debt collection, used car dealerships, student loans, and rent-to-own purchases. Our goal is to promote systems and policies that work for all consumers and provide meaningful pathways to financial security and opportunities for financial inclusion.

I. *Education*

The first step to tackling predatory lending is arming consumers with the knowledge they need to protect themselves from scams and make informed decisions. DCA has a strong history of direct outreach, consumer education, earned and paid media investments, and partnerships with community organizations. To this end, DCA has developed a community strategy that will educate constituents on how best to protect themselves against predatory practices. We plan to use this experience to engage further with communities and stakeholders to raise the alarm about common predatory practices and educate consumers before they end up on the hook for unfair and predatory loans.

II. *Enforcement*

Businesses and lenders who prey on vulnerable consumers and use deceptive practices must be held accountable. DCA is using its legal authority and investigatory resources to root out consumer harm and punish companies who break the law. Rigorous enforcement of the law through targeted legal actions will put unscrupulous businesses, lenders, and debt collectors on notice and promote a culture of compliance among other businesses. Last year, DCA took action against debt collectors who were attempting to collect on usurious loans and secured over $1.1 million in restitution for victims. More recently, DCA has brought several high-profile cases against secondhand automobile dealers engaged in predatory financing practices and we continue to take complaints from consumers harmed by this industry.

III. *Legislation*

DCA is always looking for opportunities to share our experience as a consumer protection agency with lawmakers who are crafting nuanced, thoughtful approaches to combating predatory lending. To address widespread predatory lending practices in the used car industry, DCA partnered with New York City Council Member Rafael Espinal in April of this year to introduce two groundbreaking bills that will greatly increase disclosure, consumer protections, and contract flexibility for New Yorkers who buy and finance used cars at dealers in the city.

We will now turn to observations and concerns we have about the online lending marketplace.

Online Lending Marketplace

I. *Observations and Concerns*

DCA believes that online marketplace lending has the potential to encourage the development of innovative financial products while increasing access to credit for small businesses and traditionally underserved markets. Given, however, that online lenders have not been regulated like traditional financial services institutions, and can often take advantage of lax regulation in one state to peddle loans across state lines, even to consumers or businesses who are in states with more stringent laws, it is imperative that the State of New York do all that it can to ensure that the online lending marketplace is carefully monitored.

While it seems as though the majority of online marketplace lenders target loans to prime or near-prime borrowers, recent research and responses to the U.S. Department of the Treasury's Request for Information on this topic indicate that new entrants to the market may be focusing on less creditworthy targets and that established players are considering the possibility of expanding their focus as well.[1] In addition, some online marketplace lenders are exploring expanding into lending spaces where we have traditionally observed predatory practices, like auto and mortgage lending.[2]

With respect to small business lending, we know that New York City's small businesses need better access to affordable credit and that online marketplace lenders may help provide this. Because small businesses, just like individual consumers, can also be victims of predatory lending, it is imperative that the Legislature carefully monitor attempts to facilitate access to online credit.

One such attempt came in the form of a dangerous piece of legislation introduced in both chambers last year – the Community Financial Services Access and Modernization Act. This bill would have made it much easier for storefront fringe financial services – such as check cashers – to facilitate small business loans, and potentially even individual loans. These loans would have been issued by online lenders chartered outside of the State of New York. As such loans would be originating in another state, this bill would have allowed online lenders to circumvent New York State's usury caps and peddle very high-interest loans, likely with unfavorable terms, such as very short repayment periods, to small businesses across the state. The types of small businesses in need of capital that would be seeking these loans might already be in financially vulnerable positions, which might be driving them to a check casher (versus a bank) in the first place. Fortunately, this attempt was thwarted in the Legislature, in no small part due to the advocacy of many consumer financial protection groups and community development financial institutions (CDFIs) across the state.

II. *Filling the Gap*

[1] Treasury report, 12-13.
[2] Id. at 37.

The CDFIs we've just mentioned can play an important role in filling the gap in the marketplace for small business lending. DCA is encouraged by the partnerships that some online marketplace lenders have formed with CDFIs; these partnerships, which allow online marketplace lenders to extend credit and services into traditionally underserved communities by leveraging the experience and networks of partner institutions, could be a powerful tool for educating unbanked and underbanked New Yorkers about the range of products and services available to them. In New York City, the private, non-profit, and public sectors have been working closely for years to ensure that economically distressed communities are being offered products and services that are safe and affordable. Spring Bank in the South Bronx, for example, is a United States Small Business Administration ("SBA")-certified lender, offering micro businesses loans and lines of credit. Neighborhood Trust Federal Credit Union in Washington Heights offers business loans as small as $500, with interest rates as low at 9.75%. Through its Express Loan Program, the Brooklyn Cooperative Federal Credit Union in Bedford-Stuyvesant offers promising businesses that might not otherwise qualify for credit the opportunity to get the financing they need to help their businesses grow. And in Queens, Grameen America's "small loan" program not only provides credit, but also trains business owners to carefully and successfully manage their money. In addition to these, there are dozens of financial institutions, from Carver Federal Savings Bank, to Amalgamated Bank, to the Lower East Side People's Federal Credit Union, that offer similar products and services.

Looking Ahead

DCA supports the development of regulatory framework that will assure consumers and businesses of adequate protection while preserving the innovation and increased access to credit that online marketplace lenders provide. Because commercial loans are not regulated by the Consumer Financial Protection Bureau, small business borrowers lack the same oversight and protections that consumers enjoy when using an online marketplace lender. To ensure that small businesses can also benefit from similar protections, we would urge the Legislature to ensure that any expansion of online lending in the State is accompanied by appropriate and necessary regulation.

The licensing proposal considered during this year's budget process offers one approach that could prove productive. Under that approach, most marketplace lenders would be required to obtain a license from the Department of Financial Services ("DFS"), which would allow DFS to more easily study industry practices and promote fair and uniform regulation of all lenders. DCA believes that this proposal merits close consideration by lawmakers.

In addition, localities should be empowered and appropriately resourced to conduct outreach and education to their residents about lending resources and financial protections. At DCA, we conduct hundreds of business and consumer outreach events a year in communities across the city to educate New Yorkers about their rights and responsibilities under the law. We have found that this type of outreach is a productive, cost-effective way to empower residents to make sound financial decisions by equipping them with the knowledge and resources they need.

Conclusion

We thank the committees for the opportunity to submit testimony today. We look forward to working with lawmakers from both chambers as the legislature continues its robust oversight of this important and growing industry and works to protect consumers and businesses.