

# Legislative Analysis



## DEFERRED PRESENTMENT SERVICE TRANSACTIONS (OR "PAYDAY LENDING")

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House Bill 4834

Sponsor: Rep. Bill McConico

Committee: Banking and Financial Institutions

Complete to 6-7-05

### A SUMMARY OF HOUSE BILL 4834 AS INTRODUCED 5-26-05

The bill would create a new act, the Deferred Presentment Service Transactions Act. The act would define a deferred presentment service transaction as **a transaction between the licensee and a customer under which the licensee agrees to 1) pay to the customer an agreed-upon amount in exchange for a fee and 2) hold a customer's check for a period of time before negotiation, redemption, or presentment of the check.** This kind of transaction is sometimes referred to as payday lending or check advance.

Under the new act, a business engaging in these transactions would need a license from the Commissioner of the Office of Financial and Insurance Services (OFIS). A separate license would be required for each location where business was conducted. By July 1, 2006, the commissioner of OFIS would have to establish an application process and timeline for businesses to seek licensure, as well as establish an application fee. Licenses would have to be renewed annually.

A licensee engaged in deferred presentment service transactions could enter into one transaction with a customer [at a time] for up to \$500 and could charge a service fee up to 15 percent of the transaction, plus an additional amount not to exceed \$5 for loan verification. A maturity date could not exceed 31 days. A transaction would have to be documented with a written agreement signed by both the customer and the licensee. An agreement could not be renewed, although it could be extended if no additional fee was charged and if the balance owed did not exceed the amount owed on the original agreement.

The bill would specify the contents of the written agreement, which would have to include an itemization of fees, a calculation of the cost of the fees and charges expressed as a percentage rate per year, and a notice of warnings and rights, including notice that the licensee could not use any criminal process to collect on the agreement.

The bill would refer to a customer who had entered into a transaction with a licensee as a "drawer." A drawer would be allowed to rescind a service agreement without cost and for any reason by delivering to the licensee by the close of the business day following the date of the transaction an amount equal to the amount of cash received in the transaction.

In that instance, the licensee would have to return the check received in the transaction and any service fee paid by the drawer.

Among the other major provisions are the following.

- The commissioner would be required to establish annually a schedule of license fees sufficient to pay but not exceed OFIS's reasonably anticipated costs of administering the act. The fees would be based on a licensee's business volume, number of locations, and other reasonable business factors. Licensees would also have to furnish a \$50,000 surety bond.
- To obtain a license, an entity would need to have and maintain a net worth of at least \$50,000 for each location, with a maximum of \$250,000 of net worth for any one licensee, and would have to demonstrate to the commissioner sufficient financial responsibility, financial condition, business experience, character, and general fitness to reasonably warrant a belief that the company would conduct its business lawfully and fairly.
- A company engaged in the business currently could continue to engage in the business without a license until the commissioner acted upon its application for a license or until the deadline for an application passed without an application being submitted.
- A license would not be transferable or assignable. The prior written approval of the commissioner would be required for the continued operation of a licensee when there was a change in control of the licensee. Written notice would be required at least 15 days before a licensee could open a new location or discontinue an existing location.
- A licensee could not enter into a transaction with a customer if the customer had an open transaction with the licensee or had more than one open transaction with any other licensee. A licensee would be required to verify the existence of open transactions, either by using a statewide database or, if no database had been implemented, by relying upon the written verification of the customer.
- The commissioner of OFIS would be required, by December 31, 2006, to develop, implement, and maintain a statewide common database with real-time access through an Internet connection that would be available to licensees and to the commissioner. The commissioner could contract with a third party provider to serve as the database provider. The database provider could charge licensees a verification fee for access to the database. Licensees could rely on the information in the database as accurate and could not be penalized for relying on inaccurate information.
- Upon implementation of the database, as determined by the commissioner, licensees would be required to put into the database all transactions entered into with customers from the effective date of the act until the implementation date of the database. From then on, licensees would be required on an ongoing basis to submit to the database

information on customer transactions, including a customer's name, social security number, address, driver license number, amount of transaction, and the customer's check number. When a transaction was closed, the licensee would have to immediately notify the database provider. There would be a \$100 per day administrative fine for failing to notify the database of a closed transaction.

- If a statewide database was not operational, a licensee would be required to provide an annual written report of its business operations and report quarterly (in February, May, August, and November) the number of customers who had notified the licensee of violations of the act, the number of occasions the licensee agreed or did not agree there had been a violation, and the amount of restitution paid to customers.
- A licensee would be required to prominently post a notice containing certain specified statements about the nature of deferred presentment service in an area designed to be seen by the customer before entering into a deferred presentment service transaction, and would also be required to post prominently a schedule of all fees and charges.
- A customer complaint process would be put in place that would allow a customer to notify a licensee if the customer believed the licensee had violated the law. If the licensee agreed with the complaint, the licensee would return the check it had received from the customer and any service fee and make restitution in an amount equal to five times the service fee but not less than \$15 or more than the face amount of the customer's check. If a licensee disagreed but the customer filed a complaint with the commissioner that was upheld, the restitution would equal three times the amount that would have been made if the licensee had concurred originally, but not less than \$45 or more than three times the face amount of the customer's check.
- The commissioner of OFIS would have to investigate written complaints from customers and could investigate and conduct examinations on his or her own initiative as considered necessary. The commissioner would be authorized to issue cease and desist orders; to suspend and revoke licenses; to investigate or conduct examinations and hold hearings to determine if the act had been violated, and could subpoena witnesses and evidence.
- The commissioner could impose a civil fine on a person who violated the act, state or federal law, or applicable rules or regulations, of not less than \$1,000 or more than \$10,000 for each violation. However, if the person knew or reasonably should have known of the violation, the commissioner could order a civil fine of not less than \$5,000 or more than \$50,000 per violation and could order the person to pay the costs of investigation.
- If the commissioner finds a person has engaged in fraud, the person could be prohibited from being employed by, being an agent of, or being an officer of a licensee; and if a person was convicted of a felony involving fraud, dishonesty, or breach of trust, the person could be suspended or prohibited from being a licensee or

an employer, agent, or officer of a licensee. A person subject to either kind of order could apply to the commissioner for termination of the order after five years.

The new act would not apply to a state or nationally chartered bank or a state or nationally chartered savings and loan, savings bank, or credit union whose deposits or member accounts are insured by an agency of the United States government.

## **FISCAL IMPACT:**

This bill gives the Commissioner of the Office of Financial and Insurance Services (OFIS) the authority to establish license fees annually in order to generate funds to administer the regulation of the deferred presentment service industry. However, estimating the amount needed will be difficult initially. This industry is characterized by low barriers to entry, so predicting the new firms requiring licenses will require some history to develop accurate annual estimates. Existing firms will be required to submit an application, but identifying all such firms may be a costly and time-consuming process.

No estimates of potential costs and associated fee structure were available from the Department at the time this analysis was written. Another issue will be the amount of such fees relative to the size of the firms in this industry. Fees levied to regulate a relatively new industry with many small firms may need to be so great that such fees will lessen competition.

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