

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 1425 Nonrecourse Loans

SPONSOR(S): Lopez-Cantera

TIED BILLS: IDEN./SIM. BILLS:

| REFERENCE | ACTION | ANALYST | STAFF DIRECTOR |
|---|--------|---------|----------------|
| 1) Insurance, Business & Financial Affairs Policy Committee | | Barnum | Cooper |
| 2) Civil Justice & Courts Policy Committee | | | |
| 3) General Government Policy Council | | | |
| 4) | | | |
| 5) | | | |

SUMMARY ANALYSIS

The Office of Financial Regulation (OFR) has regulatory authority over consumer finance loans authorized under Chapter 516, as well as title loans (Chapter 537), and deferred presentment transactions or payday loans (Chapter 560). Each of these loan programs provide an exception from the 18 percent per year simple interest cap that is set forth in s. 687.02, F.S.

The Truth in Lending Act is intended to assure a meaningful disclosure of credit terms so that the consumer will be able to make comparisons. To protect the consumer against inaccurate and unfair credit billing, it requires creditors to disclose the cost of credit as a dollar amount (finance charge) and as an annual percentage rate.

HB 1425 creates the new "nonrecourse loan" category within ch. 516, F.S. A nonrecourse loan may not exceed \$5,000 and is term-limited to not more than 3 years. Interest is limited to 48 percent per year as compared to the 30 percent per year maximum for consumer finance loans authorized under ch. 516, F.S. By definition, "nonrecourse loan" could be interpreted to include other types of loans regulated under different Florida Statutes.

The bill authorizes a monthly "administrative fee" of up to 10 percent per month on the unpaid principal for all offerings under ch. 516, F.S. A prohibition against such fees currently exists for consumer finance loans. The bill does not delineate the types of activities or services which might be included in the administrative fee.

Provisions within the bill potentially could conflict with state and federal law. For nonrecourse loans, a borrower's liability is limited to the collateral provided as security. This could conflict with permissible creditor actions involving deficiency claims authorized elsewhere in ch. 516, F.S. The bill requires the reporting of positive information, but prohibits the licensee from reporting any adverse information about the borrower to a major credit reporting agency unless fraud is involved. This prohibition may create conflict with federal requirements for credit reporting under the Fair Credit and Reporting Act.

A precise fiscal impact can not be determined because information is not available regarding the number of potential applicants. Based upon OFR's assumption there would be 500 applicants during Fiscal Year 2009-2010, over the next three fiscal years the bill would have a combined negative fiscal impact of \$57,244.

This bill is effective July 1, 2009.

HOUSE PRINCIPLES

Members are encouraged to evaluate proposed legislation in light of the following guiding principles of the House of Representatives

- Balance the state budget.
- Create a legal and regulatory environment that fosters economic growth and job creation.
- Lower the tax burden on families and businesses.
- Reverse or restrain the growth of government.
- Promote public safety.
- Promote educational accountability, excellence, and choice.
- Foster respect for the family and for innocent human life.
- Protect Florida's natural beauty.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

Background:

The Truth in Lending Act (TILA) is intended to assure a meaningful disclosure of credit terms so that the consumer will be able to compare the various credit terms available, avoid the uninformed use of credit, and protect the consumer against inaccurate and unfair credit billing and credit card practices.¹ Regulation Z, adopted by the Board of Governors of the Federal Reserve System, implements TILA which requires creditors to disclose the cost of credit as a dollar amount (finance charge) and as an annual percentage rate. Finance charges include any charges or fees payable by the consumer and imposed by the creditor incident to or as a condition of an extension of consumer credit.

The Office of Financial Regulation (OFR) has regulatory authority over small consumer loan programs authorized under Chapter 516 (consumer finance), Chapter 537 (title loans), and Chapter 560, (deferred presentment transactions or payday loans). Each of these loan programs provide an exception from the 18 percent per year simple interest cap that is set forth in s. 687.02, F.S.

Under ch. 516, F.S, the Florida Consumer Finance Act, a consumer can borrow up to \$25,000. Licensees may charge a maximum interest rate of 30 percent per year, computed on the first \$2,000 of the principal amount; 24 percent per year on that part of the principal amount exceeding \$2,000 but not exceeding \$3,000; and 18 percent per year on that part of the principal amount exceeding \$3,000. The annual percentage rate must be computed and disclosed as required by the Truth in Lending Act and Regulation Z. The act allows a licensee to charge a borrower up to \$25 for the costs of a credit check and an annual fee of \$25 on the anniversary date of the line-of-credit account. In addition, other charges are permissible under specific circumstances. The license fees under the act are \$625 for the initial application, plus a \$200 investigation fee, and \$625 for a renewal. A licensee must maintain evidence of liquid assets of at least \$25,000. OFR is authorized to examine and investigate any licensee, and take disciplinary actions against licensees violating the act. Currently, there are 372 licensed locations in Florida.

A title loan is a loan secured by bailment of a certificate of title to a motor vehicle. OFR is responsible for enforcing the act under the provisions of ch. 537, F.S. Prior to engaging in title loan lending, a person must secure a license through the OFR by submitting a nonrefundable application fee of \$1,200, plus a \$200 investigation fee, and \$1200 for a renewal. Licensees must maintain a bond, certificate of deposit, or letter of credit of \$100,000 per location. The maximum interest rate is 30

¹ Section 102 of title I of the Act of May 29, 1968 (Pub. L. No. 90--321; 82 Stat. 146), effective May 29, 1968, as amended.

percent per year, computed on the first \$2,000 of the principal amount; 24 percent per year on that part of the principal amount exceeding \$2,000 but not exceeding \$3,000; and 18 percent per year on that part of the principal amount exceeding \$3,000. No other fee may be charged for a title loan, and a title loan lender is expressly prohibited by the act from advertising the loans as "interest free" or "no finance charge." The law provides for a 30-day loan term with unlimited rollovers of the loan. The same rates of interest as described above apply to rollover transactions. All loans require a written contract, which includes certain information about the borrower and the terms of the loan. Currently, there are no licensed title loan lenders in Florida.

Pawnbroking transactions are regulated under ch. 539, F.S.² A pawn is defined to mean ". . . any advancement of funds on security of pledged goods on condition that the pledged goods are left in the possession of the pawnbroker for the duration of the pawn and may be redeemed by the pledgor . . ."³ The pawnbroker is entitled to pawn service charged in which the interest component of such charge is 2 percent of the amount financed for each 30-day period. The pawnbroker may charge any amount of pawn service charge, so long as the total amount, inclusive of the interest rate, does not exceed 25 percent of the amount financed for each 30-day period, except that a pawnbroker is entitled to receive a minimum pawn service charge of \$5 for each 30-day period.

A deferred presentment transaction, or payday loan, is another small consumer loan product. It is available under part IV of Ch. 560, F.S. A consumer can obtain a payday loan by providing a personal, postdated check. When the loan is due, the lender cashes the check or, if the borrower cannot repay the loan, (s)he may renew the loan. The check is held for a minimum of 7 days, but not longer than 31 days. The amount of the loan may not exceed \$500. The fees allowed for a payday loan are 10 percent of the loan amount plus a verification fee, which may not exceed \$5. Payday lenders are prohibited from taking additional collateral and engaging in rollover transactions.⁴ Other consumer protections for payday loans include a 24-hour waiting period between transactions and a detailed deferred presentment agreement. There is also a 60-day grace period if the consumer notifies the vendor before the due date that the consumer is unable to make the check good. In these cases, the consumer must participate in credit counseling in order to be afforded the grace period. OFR maintains a statewide database to ensure that consumers do not have more than one outstanding payday loan at any one time and that they adhere to the 24-hour waiting period. In order to transact business as a deferred presentment provider, a person must be licensed under Part II (funds transmitters and payment instrument sellers) or Part III (check cashers and foreign currency exchangers) of Chapter 560, F.S. In addition to the licensing fee and renewal fees associated with a Part II or Part III license, the person must pay a \$1,000 fee to file a notice of intent to engage in deferred presentment transactions, and must renew the notice of intent biennially. The renewal fee is \$1,000. There are over 1,200 payday lender locations in Florida.

Current Situation:

Chapter 516, F.S. is the governing statute for consumer finance loans.⁵ It provides for a maximum interest rate of 30 percent per year, computed on the first \$2,000 of the principal amount; 24 percent per year on that part of the principal amount exceeding \$2,000 but not exceeding \$3,000; and 18 percent per year on that part of the principal amount exceeding \$3,000. In addition to interest, current law allows for specified other charges, such as delinquency, insurance premiums, and costs associated with property pledged as security. "Administrative fees" are neither defined nor permitted. Rather, aside from clearly defined exceptions, no other charges or amount for any examination, service, commission, or other thing shall be directly or indirectly charged, contracted for, or received as a condition to the grant of a loan.⁶ Currently, there are 372 licensed locations in Florida.

² Pawnbroking is regulated by the Department of Agriculture and Consumer Services.

³ s. 539.001(2)(h), F.S.

⁴ s. 560.402(6), F.S. - "Rollover" means the termination or extension of a deferred presentment agreement by the payment of an additional fee and the continued holding of the check, or the substitution of a new check by the drawer pursuant to a new deferred presentment agreement.

⁵ s. 516.01(2) defines "consumer finance loan" as a loan of money, credit, goods, or provision of a line of credit, in an amount or to a value of \$25,000 or less at an interest rate greater than 18 percent per annum.

⁶ s. 516.031(3)(a), F.S.

To the extent that a lender furnishes information to a major credit reporting agency, it is required by the Fair Credit and Reporting Act to provide complete and accurate information and to provide notice to consumers about negative information to be placed on the credit report in addition to providing explanations in the event that a consumer disputes the information. The Fair Credit and Reporting Act regulates the collection, dissemination, and use of consumer credit information. Under the Fair Credit and Reporting Act, "creditor" means "any person who regularly extends, renews, or continues credit; any person who regularly arranges for the extension, renewal, or continuation of credit; or any assignee of an original creditor who participates in the decision to extend, renew, or continue credit."⁷

The Fair Credit and Reporting Act provides that generally the act does not annul, alter, affect, or exempt any person subject to the provisions of the act from complying with the laws of any state, except to the extent that those laws are inconsistent with any provision of the act, and then only to the extent of the inconsistency.⁸ The Federal Trade Commission has enforcement responsibility for the Fair Credit and Reporting Act.

Effect of Proposed Change:

HB 1425 creates a new "nonrecourse loan" category within ch. 516, F.S. The nonrecourse loan may not exceed \$5,000 and is term-limited to not more than 3 years. The loan can, but need not, be secured by personal property. Interest is limited to 48 percent per year and a monthly "administrative fee" of up to 10 percent per month on the unpaid principal is permitted. In addition, while requiring the reporting of positive information, the bill prohibits the licensee from reporting any adverse information about the borrower to a major credit reporting agency unless fraud is involved.

The definition of "nonrecourse loan" could be interpreted to include other types of loans currently regulated under other Florida Statutes. Such interpretation could lessen the legal and practical relevance of other Florida Statutes dealing with financial transactions.⁹ Personal property, which could include a car or a watch, can be used to secure a nonrecourse loan. If a car, then ch. 537, F.S., which governs title loans, could also be applicable. Title loan lender licensees are required to have a bond, certificate of deposit, or irrevocable line of credit of \$100,000 while the nonrecourse loan lender is required to have evidence of liquid assets of \$25,000. The maximum interest on a title loan is 30 percent, with no provision for administrative fees, whereas the maximum interest on a nonrecourse loan is 48 percent and other charges, including up to a 10 percent administrative fee, are permitted. If a watch was the personal property used to secure a nonrecourse loan, then ch. 539, F.S., which governs pawn brokers, could also be applicable. A pawn broker licensee is required to have a net worth of \$50,000 or a \$10,000 surety bond while the nonrecourse loan lender is required to have evidence of liquid assets of \$25,000.

HB 1425 does not define or describe the types of activities or services comprising the administrative fee. There exists no requirement to justify or delineate how the lender deduces the administrative fee. Absent guidelines, nonrecourse loan lenders could characterize a myriad of activities, including routine record keeping, as administrative in nature and thus charge the borrower an additional fee for a normal business activity.

The bill may create internal ambiguity within ch. 516, F.S. It would place in law that, for nonrecourse loans, a borrower's liability is limited to the collateral provided as security. By definition a nonrecourse loan could be up to \$5,000 and secured by personal property. Section 516.31, F.S. applies to every consumer finance loan or other contract authorized by Ch. 516, F.S., in which any form of credit is extended to an individual to purchase or obtain goods or services for use primarily for personal, family, or household purposes. This would include nonrecourse loans. It permits creditors to seek deficiency claims when the outstanding balance at the time of default is \$2,000 or more, with certain limitations. The new language applicable to nonrecourse loans prohibits such action.

⁷ Equal Credit Opportunity Act, Section 702 of title VII of the Act of May 29, 1968 (Pub. L. No. 90--321), as amended.

⁸ Section 625, Fair Credit Reporting Act

⁹ Office of Financial Regulation Bill Analysis and Fiscal Impact Statement dated March 21, 2009 on file with the Insurance, Business and Financial Affairs Policy Committee.

The bill may create conflict with federal requirements for credit reporting.^{10,11, 12} It requires nonrecourse loan licensees to report a borrower's satisfactory repayment of a nonrecourse loan to a major credit reporting agency, and prohibits reporting any adverse information about the borrower, except in the event of fraud on the part of the borrower. To the extent that a nonrecourse lender furnishes information to a major credit reporting agency, it is required by the Fair Credit and Reporting Act to provide complete and accurate information. The bill provides that the only adverse information a nonrecourse lender would be permitted to report is fraud on the part of the borrower. If a consumer disputes a report of fraud, or the Fair Credit and Reporting Act requires additional disclosures and protections from the creditor, the bill does not provide OFR the authority to intervene since the Fair Credit and Reporting Act is enforced by the Federal Trade Commission.

B. SECTION DIRECTORY:

Section 1. Amends s. 516.01, F.S., by incorporating and defining the term "nonrecourse loan".

Section 2. Amends s. 516.031, F.S., by incorporating maximum nonrecourse loan finance charges.

Section 3. Amends s. 516.15, F.S., by clarifying the duties of a licensee.

Section 4. Provides an effective date of July 1, 2009.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:¹³

1. Revenues:

Indeterminate. Information is not available regarding the number of potential applicants. Based on an assumption that there would be 500 applicants during Fiscal Year 2009-2010 and 50 new applicants in Fiscal Year 2010-2011.

| | (FY 09-010) | (FY 10-11) | (FY 11-12) |
|--|------------------|------------------|------------------|
| Recurring | | | |
| Application fees (500 x \$625) | \$312,500 | \$ 31,250 | \$ 31,250 |
| Investigative Fee (500 x \$200) | \$100,000 | \$ 10,000 | \$ 10,000 |
| Renewal fees (75% - \$625 due 12/31 even years) | | | \$257,500 |
| Total | \$412,000 | \$ 41,250 | \$288,750 |

2. Expenditures:

Based on an assumption that there would be 500 applicants during Fiscal Year 2009-2010 and 50 new applicants in Fiscal Year 2010-2011.

| | (FY 09-010) | (FY 10-11) | (FY 11-12) |
|-------------------|-------------|------------|------------|
| Recurring – 4 FTE | | | |
| Salary & Benefits | \$221,680 | \$221,680 | \$221,680 |
| Expense | \$ 36,700 | \$ 36,700 | \$ 36,700 |
| Transfer to DMS | \$ 1,652 | \$ 1,652 | \$ 1,652 |

¹⁰ Fair Credit Reporting Act (FCRA), 15 U.S.C. § 1681 et seq.

¹¹ Fair and Accurate Credit Transactions Act of 2003, Pub. L. No. 108-159 effective Dec. 4, 2003.

¹² See also: Office of Financial Regulation Bill Analysis and Fiscal Impact Statement dated March 21, 2009 on file with the Insurance, Business and Financial Affairs Policy Committee.

¹³ Assumptions and fiscal impact as reported in Office of Financial Regulation Bill Analysis and Fiscal Impact Statement dated March 21, 2009 on file with the Insurance, Business and Financial Affairs Policy Committee.

| | | | |
|-----------------------|-----------|-----------|-----------|
| Recurring Total | \$260,032 | \$260,032 | \$260,032 |
| Non-recurring Expense | \$ 13,648 | | |
| OCO | \$ 5,500 | | |
| Non- recurring Total | \$ 19,148 | | |
| Total | \$279,180 | \$260,032 | \$260,032 |

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

D. FISCAL COMMENTS:

Based upon the assumptions, for Fiscal Years 2009-2012, combined revenue would be \$742,000 vs. an expenditure of \$799,244.¹⁴

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. This bill does not appear to: require counties or municipalities to spend funds or take an action requiring the expenditure of funds; reduce the authority that counties or municipalities have to raise revenues in the aggregate; or reduce the percentage of a state tax shared with counties or municipalities.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

None.

C. DRAFTING ISSUES OR OTHER COMMENTS:

IV. AMENDMENTS/COUNCIL OR COMMITTEE SUBSTITUTE CHANGES

¹⁴ Id.