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CRIMINAL LAW

Tellers admit scamming Georgia bank out of $1.6 million

Two former bank tellers are facing up to 30 years in prison after admitting in federal court to embezzling more than $1.6 million from a Georgia bank and falsifying records to cover the thefts.

United States v. Mize et al., No. 18-cr-16, plea agreements filed, 2018 WL 6444968, 2018 WL 6445179 (M.D. Ga. Dec. 4, 2018).

Brandy Mize and Vicky Martin appeared before U.S. District Judge Tillman E. Self of the Middle District of Georgia on Dec. 4 and pleaded guilty to one count of conspiracy to defraud a financial institution, U.S. Attorney Charles Peeler said in a statement the next day.

Mize and Martin admitted that while working at Eatonton, Georgia-based The Peoples Bank they took cash from their teller drawers, issued themselves cashier's checks, transferred bank funds into their own accounts and made fake ledger entries to hide the thefts.

Mize also admitted she stole cash from the vault, Peeler said.

Mize, as the head teller, and Martin, as the assistant head teller, were responsible for

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Robert M. Jaworski of Holland & Knight discusses the short-term payday loan industry and whether banks should enter this lending market.

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Charles B. Jimerson of Jimerson & Cobb discusses factors creditors' attorneys in Florida should consider when attempting to obtain an assignment of a debtor's interest in a pending lawsuit or a judgment.

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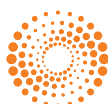
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Banks and short-term, small-dollar loans: Is now the time?

By Robert M. Jaworski, Esq.
Holland & Knight

Recent financial news reports announced a new short-term, small-dollar consumer loan offering by U.S. Bank that appears intended to compete with traditional payday loan products. Will it be successful? Is the time ripe for other banks to develop such products? Can technological innovations make these products feasible for banks to offer? What hurdles will banks face?

PAYDAY LOANS

Paydays loans offered by nondepository institutions are generally marketed as a way for consumers to bridge unexpected financial shortfalls they face while awaiting the receipt of paychecks, benefits or other sources of income. They provide consumers ready access to funds for a short period of time with very limited underwriting. In return, consumers pay a set fee based on the amount borrowed.

Most payday loans are repayable in two weeks by means of a single balloon payment. The average fee is $15 per $100 borrowed, which works out to an annual percentage rate of almost 400 percent. Customers who cannot repay the loan by the due date can usually have the deadline extended for additional two-week periods, i.e., have the loan "rolled over," but they must pay an additional fee for each rollover.

Online payday lenders, which tend to charge higher fees than their storefront counterparts, require customers to agree to repay the loans through the ACH network by means of an automatic debit from their checking account. If an automatic debit is transmitted to but rejected by a customer's bank because there are insufficient funds in the account, the customer may have to pay additional fees to the bank.

Borrowers can typically qualify for a storefront payday loan by providing some verification of income (typically a pay stub) and evidence of a personal deposit account. Online payday lenders are more concerned about fraud and typically require borrowers to verify their identity and the existence of a bank account in good standing.

Payday lenders do not generally consider borrowers' other financial obligations or require collateral for the loan.

Payday lenders do not generally consider borrowers' other financial obligations or require collateral for the loan. Nor do they typically obtain traditional credit reports or credit scores on borrowers before making a loan, or report information about borrowers' payday loan borrowing history to any of the nationwide consumer reporting agencies. Moreover, the process of applying for and obtaining a payday loan is typically simple and fast, two attributes that make it very attractive to consumers who need money in a hurry.

Until the passage of the Dodd-Frank Act and the creation of the Consumer Financial Protection Bureau, the federal government essentially ceded regulation of payday loans to the states.

The states took different approaches to regulating payday loans. Some states essentially banned them, believing they harmed consumers by leading them into a cycle of debt that is often difficult and costly to escape.

Others attempted to regulate some of the loans' most onerous aspects by limiting rollovers, setting limits on fees and taking other similar steps. Still others allowed the free market to operate with respect to payday loans.[1]

DEPOSIT ADVANCE PRODUCTS

More than a decade ago, several banks tried to tap into the short-term, small-dollar market by offering deposit advance products. DAPs are small-dollar, short-term credit products, typically open-end lines of credit, that are offered to customers who maintain a deposit account (or deposit-related vehicle such as a reloadable prepaid card) and use direct deposit. They allow customers to obtain funds in advance of their next direct deposit based on their history of recurring deposits.

Like payday loan fees, DAP fees are typically charged as a set dollar amount that is based on the amount borrowed. Repayment occurs when the next qualifying direct deposit is made to the customer's account. If no such deposit is made within 35 days following the advance, the customer's account is debited by the amount due (even if that results in the account being overdrawn).

Since the repayment date is not set at the time of the advance and will vary depending on the amounts and timing of the customers' direct deposits, the fee cannot be used to calculate an APR when the credit is extended.

Qualifications for a DAP typically include a deposit account with the bank that is in good standing and has been open for a specified

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period, a history of recurring direct deposits above a minimum amount, and additional requirements that the bank may impose. Credit limits are generally set as a percentage of the total monthly direct deposits made to the account.[2]

HOSTILITY TOWARD PAYDAY LOANS AND DAPS

Over the years, payday loans' negative aspects have attracted considerable attention from state and federal legislators and regulators as well as consumer advocacy groups. This attention has focused on, among other things, the extremely high APRs attached to payday loans, internet payday lenders' widespread use of lead generation companies to funnel consumers to their websites, the fact that many payday loan customers are financially unsophisticated, the ease with which consumers can obtain and extend payday loans, and the often-harsh consequences suffered by borrowers when their accounts lack sufficient funds to cover checks or payment requests presented to their bank (often multiple times) by the lender.

In response, states have passed laws prohibiting or restricting payday loans, regulatory enforcement actions have been undertaken against payday lenders and federal bank regulators have attempted to dissuade banks from being involved in this type of lending.[3]

THE U.S. BANK LOAN PRODUCT

Against this backdrop, U.S. Bank has introduced a new offering called the "Simple Loan." It is described on the bank's website as a "high-cost product," but it appears to be significantly more consumer-friendly than a typical payday loan.

The fee is $12 per $100 borrowed (which works out to an APR of approximately 70 percent) for customers who agree to use autopay to make their payments. If autopay is not used, the fee is $15 per $100 borrowed (which is an APR of approximately 88 percent).[4] The maximum loan amount is $1,000.

Repayment is required in three monthly installments (which cannot exceed 5 percent of the customer's gross monthly income), and the loan cannot be rolled over. There must be at least a 30-day cooling off period between the time one loan is paid off and the customer applies for another one.

Only consumers who maintain a checking account with U.S. Bank and have a credit history are eligible, and U.S. Bank has indicated that it intends to report data about the loans to credit agencies so borrowers can build up their credit profile.[5]

PROSPECTS FOR OTHER BANKS DEVELOPING SIMILAR PRODUCTS

Recent actions by the CFPB and the Office of the Comptroller of the Currency signify a less hostile attitude toward bank involvement in short-term, small-dollar lending, and this development may encourage other banks to consider similar programs.

To be successful, they will likely need to streamline the processes they use to originate these types of loans, partly by embracing the use of technology. Nevertheless, hurdles will remain.

CFPB PAYDAY LOAN RULE

The CFPB adopted its final Payday, Vehicle Title and Certain High Cost Installment Loans Rule in October 2017, shortly before then-Director Richard Cordray resigned from the bureau to campaign for governor of Ohio.[6]

> Over the years, payday loans' negative aspects have attracted considerable attention from state and federal legislators and regulators as well as consumer advocacy groups.

The significance of the Payday Rule, assuming it is not materially revised by the bureau or overturned by a court before its August 2019 effective date, lies in the fact that it imperils the existing payday loan origination model.

The Payday Rule declares that it is an unfair and abusive practice for nonbank lenders to make short-term, small-dollar loans to consumers without reasonably determining that they have the financial capacity to make the required loan payment(s) while also fulfilling their major financial obligations and paying for their basic living expenses.

Moreover, the Payday Rule requires lenders to adhere to specific policies and procedures when making this determination, including that they:

- Obtain a written statement of the consumer's net income and the amount the consumer must pay to meet his/her major financial obligations.
- Verify, from their own records, a national consumer report or a report from a registered information system, the consumer's net monthly income and major debt obligations.
- Determine ability to repay based on projections of the consumer's monthly residual income or debt-to-income ratio and the required (highest) monthly loan payment.
- Ensure that, within 30 days before applying for the loan, the customer has not had a sequence of three short-term, small-dollar (or longer-term balloon payment) loans (defined to include rollovers), each of which was paid off less than 30 days before applying for the next one. (The Payday Rule requires a 30-day cooling off period before a consumer can obtain an additional short-term, small-dollar loan under such a circumstance.)

Alternatively, under the Payday Rule lenders may offer some consumers a closed-end "principal step-down" short-term, small-dollar loan. Such a loan may not exceed $500. The amount of a second or third short-term, small-dollar loan obtained by the borrower within 30 days after payoff of the principal step-down loan may not exceed two-thirds and one-third, respectively, of the amount of the initial loan.

The lender may not take a security interest in the consumer's motor vehicle. And the lender must provide the consumer with a written disclosure explaining these restrictions, both at the time of the initial loan and before the lender makes a third loan in a sequence.

Adherence to the Payday Rule's mandates will necessitate a drastic overhaul of the loan origination model presently utilized by most, if not all, payday lenders and will entail considerable effort and expense on their part. The result of any such overhaul, moreover, will be a more time-consuming, involved and expensive process going forward.

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By making it more difficult and costly for payday lenders to operate, the Payday Rule — which does not apply to depository institutions — may create an opening for such institutions to develop competitive products.

OCC actions

Almost immediately after the CFPB adopted the Payday Rule, the OCC announced it was rescinding its 2013 guidance concerning DAPs.[7] That guidance, together with similar guidance issued by the Federal Deposit Insurance Corp. in 2007,[8] had effectively stifled the DAP lending programs then being operated by several banks and discouraged other institutions from entering the market.

The OCC's rescission of this guidance sent a signal — though an ambiguous one — that the agency may have changed its mind concerning the appropriateness of banks offering DAPS and perhaps other types of short-term, small-dollar loans as well.

In May 2018 the OCC put out a much clearer signal to that effect in OCC Bulletin 2018-14, announcing its Core Lending Principles for Short-Term, Small-Dollar Installment Lending.[9] The OCC Bulletin encouraged national banks to consider developing plans to offer short-term, small-dollar loans with maturities greater than 45 days, no required balloon payments, and reasonable pricing and repayment terms.

The bulletin also recommended that banks develop these plans in consultation with their OCC portfolio manager, examiner-in-charge or supervisory office, particularly in cases where entering into such a program would constitute a substantial deviation from the bank's existing business plans.

In addition, the OCC Bulletin instructed banks choosing to develop such a lending program to adhere to the following core lending principles:

- All products should be consistent with safe and sound banking, treat customers fairly, and comply with applicable laws and regulations.
- Banks should effectively manage the risks associated with the products they offer, including credit, operational, compliance and reputation risks.
- All credit products should be underwritten based on reasonable policies and practices, including guidelines governing the amounts borrowed, frequency of borrowing and repayment requirements.

Further, the OCC Bulletin indicated that, in the agency's view, reasonable policies and practices for a short-term, small-dollar installment lending program would generally include the following characteristics:

- Loan amounts and repayment terms that promote the fair treatment and access of applicants and support borrower affordability and successful repayment of principal and interest in a reasonable time frame.
- Loan pricing that complies with applicable state laws and reflects overall returns reasonably related to product risks and costs.
- Analysis that uses internal and external data sources, including deposit activity and nontraditional credit data, to assess a consumer's creditworthiness and effectively manage credit risk. Transparent, accurate and consumer-friendly marketing and disclosures that comply with applicable consumer protection laws and regulations.
- Loan servicing processes and workout strategies that help customers avoid continuous cycles of debt and costs disproportionate to the amounts borrowed.
- Timely reporting of borrowers' repayment histories to credit bureaus, so that borrowers can build positive credit profiles and transition into mainstream financial products.

Finally, the OCC stated in the bulletin that it would not look favorably at entities partnering with banks if their sole objective in doing so is to evade a lower interest rate cap to which they would be subject if they made the loans themselves.

The role of technology

Some of the principal reasons people use payday lenders to meet their short-term credit needs include the ease with which they can obtain the loans, the flexibility the loans afford them and the convenient locations in which storefront payday lenders operate (mostly in inner cities where bank offices are few and far between).[10] As indicated above, if applicants can supply a pay stub or verification of identity and evidence of a bank account, they can obtain a payday loan very quickly and with very little fuss.

Many payday lenders, including virtually all online payday lenders, perform virtually instantaneous checks to make sure the loan applications are not fraudulent and the applicants are who they say they are, and then approve the loans and tender or deposit the funds into the customers' bank account within minutes. If borrowers are unable to repay their loans when due, many payday lenders allow them to extend their loans for an additional period or periods, each time by simply paying another fee.

> The Payday Rule declares that it is an unfair and abusive practice for nonbank lenders to make short-term, small-dollar loans to consumers without reasonably determining that the borrowers have the financial capacity to make the required loan payments.

To gain significant market share, banks will need to rely on technology to a great extent to make their loan application and funding processes as efficient and user-friendly as possible. Otherwise, customers are likely to stay with the payday lender (or lenders) they have used in the past, even if those loans are more expensive.

However, no matter how banks streamline their processes, the regulatory regime under which they operate will likely prevent those processes from being as simple, easy and flexible for consumers as the processes currently employed by payday lenders. This is where the Payday Rule, if retained in its present form, may help banks bridge this gap because it requires payday lenders to make their processes more rigorous.

Continuing hurdles

The FDIC's 2007 Financial Institution Letter, which has not been withdrawn or revised, continues to be an impediment to the development by state-chartered banks of

short-term, small-dollar installment lending programs.

While the letter encouraged banks "[a]s permitted by state law, to offer small-dollar credit," it also strongly urged them to ensure that the APR on these loans be no greater than 36 percent and to utilize sound underwriting criteria focused on a borrower's history with the institution and ability to repay the loan. These conditions are likely to negatively impact the profitability and market share any such program may achieve.

In addition, some states and states' rights advocates oppose the CFPB's Payday Rule, believing that regulation of payday lending is best left to the states.[11]

Also, consumer advocacy groups and representatives have expressed concerns on behalf of their constituencies about both the U.S. Bank Simple Loan and the OCC's Bulletin. They have argued that the APR on U.S. Bank Simple Loans is too high, i.e., that it should not exceed 36 percent, and that the OCC Bulletin should contain more substantial guardrails around ability to repay and price.[12]

These reactions, coupled with the possibility of negative press reports and the reputation risk that such reports can generate, might discourage other banks from following U.S. Bank's lead.

CONCLUSION

It seems clear that the introduction of banks into the short-term, small-dollar loan market has the potential to improve the financial well-being of a sizable segment of the nation's population. The loans banks would offer would likely be less costly than those currently offered by payday lenders, and banks are in a better position to help customers migrate to more mainstream bank products and services.

However, it also seems clear that a rigid regulatory regime can stifle banks' efforts to develop innovative new products, processes and procedures that might enable them to compete effectively with payday lenders.

For example, if regulators were to heed consumer advocates' calls for interest rate caps that would render the risk/reward relationship for banks unpalatable or require banks to undertake unduly burdensome ability-to-repay analyses before making these types of loans, banks would likely find it difficult to convince their directors and stockholders to support such initiatives.

Needless to say, it will be interesting to see how all of this plays out during the coming months and years. WJ

NOTES

[1] The information provided in this section about payday loans can be found in the preamble to the Consumer Financial Protection Bureau's final Payday, Vehicle Title and Certain High-Cost Installment Loans regulation published at 82 Fed. Reg. 54472, 54474-54503 (Nov. 17, 2017).

[2] *See* CFPB report entitled Payday Loans and Deposit Advance Products – A White Paper of Initial Data Findings (April 2013), *available at* https://bit.ly/NssoJ1, at p.11.

[3] *See, e.g.*, discussion in the preamble to the Payday Rule at pp. 54474-54503 concerning state regulation of payday lending and state and federal enforcement actions involving payday lenders; FDIC FIL Guidelines for Payday Lending, (Revised Nov. 2015), available at https://bit.ly/2QjSK5f, discouraging bank partnerships with payday lenders; Consumer Federation of America's information resource on payday lending for consumers and advocates, *available at* https://bit.ly/2SCOlXL.

[4] Section 85 of the National Bank Act, 12 U.S.C.A. § 85, together with OCC regulations, specifically, 12 CFR 7.4001, authorize national banks to charge interest at the maximum rate permitted by the law of the state in which the national bank is located.

[5] The information provided in this section about the U.S. Bank Simple Loan was obtained from the bank's website at https://bit.ly/2Qj0xjM.

[6] *See* note 1. The Payday Rule is not scheduled to become effective until August 2019 (21 months after publication in the Federal Register). However, the CFPB announced Oct. 26, 2018, that it will issue a Notice of Proposed Rulemaking in January 2019 to reconsider the Payday Rule's ability-to-repay provisions and address its compliance date. The announcement is available at https://bit.ly/2EJWGGZ. In addition, the Payday Rule has been challenged in court. *See, e.g.*, *Cmty. Fin. Servs. Ass'n of Am. Ltd. v. Consumer Fin. Prot. Bureau*, No. 18-cv-295, *complaint filed* (W.D. Tex. Apr. 9, 2018).

[7] OCC Press Release (Oct. 5, 2017), *available at* https://bit.ly/2yIG3Hn.

[8] FDIC FIL-50-2007, *available at* https://bit.ly/2AYtWoD.

[9] The bulletin can be found at https://bit.ly/2AYExjv.

[10] *See, e.g.*, How Payday Loans Work, John Barrymore, available at https://bit.ly/2UqLhzu ("Ease and convenience fuel the allure of payday loans. One of the biggest advantages that payday lenders have over banks is their flexibility. Payday lenders have more locations and longer hours than most banks. Some lenders, such as some Currency Exchange locations in Illinois, are open 24 hours a day. … Payday lenders rarely check your credit. Coupled with the privacy and expediency of the process, this open-mindedness makes payday lenders very attractive to people with poor credit. In addition, the loan application process is fast. You can usually be out the door, off the phone or away from your keyboard in less than half an hour. Furthermore, you get the money in no time — if the lender doesn't hand you a check when you apply, the money is usually electronically deposited in your account within a day.").

[11] *See* the discussion in the preamble to the final Payday Rule concerning such submitted in response to the BCFP's proposed rule, beginning at 82 Fed. Reg. 54515.

[12] *See, e.g.*, American Banker (Oct. 4, 2018), R. Borne, High-cost bank loans a step in the wrong direction, 2018 WLNR 30584094.

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