GEORGETOWN LAW

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May 15, 2019

Bureau of Consumer Financial Protection
1700 G Street, NW
Washington DC 20552

RE: Docket No. CFPB-2019-0006 (RIN 3170-AA80)

Dear Sir/Madam:

I write to strongly object to the Bureau's Notice of Proposed Rulemaking (the "NPRM") regarding Payday, Vehicle Title, and Certain High-Cost Installment Loans, Docket No. CFPB-2019-0006.[1] The NPRM proposes a repeal of the ability-to-repay requirement in the Bureau's November 2017 final regulation regarding Payday, Vehicle Title, and Certain High-Cost Installment Loans (the "2017 Final Rule").[2]

There is no basis for the Bureau repealing the ability-to-repay requirement or otherwise revising the 2017 Final Rule. No facts have changed, and no new evidence has been adduced regarding the 2017 Final Rule since its promulgation.[3] Instead, the only thing that has changed is the political leadership at the Bureau. The proposed repeal is based on faulty and contentious criticisms of a small part of the massive body of evidence supporting the 2017 Final Rule, and also deliberately ignores other evidence that is available to the Bureau as part of its supervisory and enforcement processes.

Moreover, the criticisms leveled by the Bureau (under new political leadership) in the NPRM of the 2017 Final Rule are internally inconsistent. Specifically, in the NPRM the Bureau criticizes those studies that support the 2017 Final Rule on the same basis that it then praises studies that it (erroneously) believes throw shade on the 2017 Final Rule. This inconsistent application of evaluation standards that tracks the Bureau's politically preferred outcome is the epitome of arbitrary and capricious behavior by an agency. As such, the

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[1] 84 Fed. Reg. 4252, Feb. 14, 2019.

[2] 82 Fed. Reg. 54472-54921, Nov. 17, 2017, *codified* at 12 C.F.R. Part 1041.

[3] The NPRM does discuss as an afterthought some studies that have been published since the 2017 Final Rule, but notes that "the new research described here supplements, and does not contradict, the research described in the 2017 Final Rule." 84 Fed. Reg. 4294, Feb. 14, 2019.

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Bureau's proposed rulemaking is illegal under the standard articulated by the Supreme Court in *Motor Vehicle Manufacturer's Association v. State Farm Insurance,* 463 U.S. 29 (1983).

Additionally, the Bureau's new political leadership is attempting through what is formally cast as a repeal of the ability-to-repay standard to promulgate a backdoor definition of the statutory terms "unfair" and "abusive" without going through a direct notice-and-comment rulemaking process. This too is forbidden by the Administrative Procedures Act, 5 U.S.C. § 553.

I urge the Bureau to abandon this proposal for a patently illegal rulemaking and return to its statutory charge of protecting consumers.

I. QUALIFICATIONS

By way of background, I am the Agnes N. Williams Research Professor and Professor of Law at Georgetown University Law Center, where I teach courses in Consumer Finance, Financial Regulation, Contracts, Commercial Law, and Bankruptcy. I have also previously served as the Bruce W. Nichols Visiting Professor of Law at Harvard Law School and as faculty for the Federal Trade Commission's Division of Financial Practices training program at a time when the FTC was the sole federal regulator with authority over payday, vehicle title, and short-term installment lenders. Among my publications is the first law school textbook on consumer finance, ADAM J. LEVITIN, *CONSUMER FINANCE: MARKETS AND REGULATION* (Wolters Kluwer 2018), which includes a chapter devoted to the economics, market structure, and regulation of payday, vehicle title, and other short-term, small-dollar lending products.

I am no stranger to the Bureau. From 2012-2015 I served on the Bureau's inaugural Consumer Advisory Board, including as a member of the Consumer Advisory Board's Small-Dollar Lending Committee. I have also subsequently been repeatedly retained by the Bureau as an expert on payday and vehicle title lending. These retentions have involved a (non-public) investigation of a vehicle title lender and retention to be a testifying expert on the payday loan industry in two cases.[4] One of these cases was prosecuted in coordination with a state regulatory enforcement action, the record from which was made available to the Bureau. Bureau staff has also recently approached me regarding retention in a third small dollar lending case. Put simply, the Bureau has enough confidence in my expertise regarding payday and vehicle title lending to be willing to present me as an expert in court, and the Bureau has even successfully defended a *Daubert* challenge against my testimony.[5]

Additionally, I have also served as an expert for the Illinois Attorney General in payday loan litigation and as an expert in a pair of private litigations relating to short-term, small-dollar lending. Based on this background, I am not only deeply familiar with the scholarly literature on short-term, small-dollar lending and the non-public workings of short-term,

[4] *CFPB v. All American Check Cashing*, No. 3-16-cv-356 (S.D. Miss.) and *CFPB v. NDG Financial Corp.,* No. 15-cv-5211 (S.D.N.Y).

[5] Opinion and Order, *CFPB v. All American Check Cashing*, No. 3-16-cv-356-WHB-JCG (S.D. Miss. Mar. 21, 2018) (docket no. 237) (denying defendants' *Daubert* motion).

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small-dollar lending industry, but I am also acquainted with some of the non-public information that has been developed by the Bureau in its supervisory process, as well as non-public information developed by state regulators. As such, I believe I am uniquely qualified to evaluate the Bureau's arguments in the NPRM.

II. COMMENTS ON THE NPRM

The NPRM puts forward two separate grounds for its proposed repeal of the ability-to-repay requirement: (1) that the evidentiary support for the 2017 Final Rule is not sufficient strong and (2) that the Bureau applied the wrong legal standard when interpreting the terms "unfair" and "abusive" in the Consumer Financial Protection Act. Both claims in the NPRM are wrong.

A. Evidentiary Support for the 2017 Final Rule

The Bureau's new political leadership alleges that the evidentiary support for the 2017 Final Rule is not sufficiently strong. Notably, however, the Bureau does not suggest that the 2017 Final Rule would fail to withstand scrutiny under the Administrative Procedures Act. Instead, the Bureau's new political leadership has arrogated to itself a higher (but unspecified) standard of evidentiary support. If the Bureau had not undertaken the 2017 Final Rule, the Bureau would generally be free to insist on whatever evidentiary standard it wanted above that required by the Administrative Procedures Act for affirmative promulgation of a rule. But once a final rule has been promulgated, the Bureau cannot simply decide to apply a new and higher (but unarticulated) evidentiary standard. The Bureau cannot now invoke a Caesar's Wife standard as the basis for repealing the 2017 Final Rule. Doing so is the ultimate in politically self-serving analysis, and is, as such an arbitrary and capricious basis for the proposed repeal of the ability-to-repay requirement.

1. The NPRM Does Not Contest Most of the Evidence Supporting the 2017 Final Rule.

Beyond this basic legal flaw in the Bureau's approach in the NPRM, the criticisms in the NPRM of the evidentiary support for the 2017 Final Rule are specious and disingenuous, as shown by the Bureau's inconsistent standards for studies that support the new leadership's political position versus those that do not.

Before turning to an examination of the Bureau's criticisms of the evidentiary support for the 2017 Final Rule, however, it is important to underscore what is *not* at issue here. The 2017 Final Rule was a 450-page Federal Register publication with 1,315 footnotes. It was supported by an incredible mass of research and evidence. As the 2017 Final Rule noted:

> the Bureau has been studying these markets for liquidity loans for over five years, gaining insights from a variety of sources. During this time the Bureau has conducted supervisory examinations of a number of payday lenders and enforcement investigations of a number of different types of liquidity lenders, which have given the Bureau insights into the business models and practices of such lenders. Through these processes, and through market monitoring activities, the Bureau also has obtained extensive loan-level data that the

> Bureau has studied to better understand risks to consumers. The Bureau has published five reports based upon these data. The Bureau has also carefully reviewed the published literature with respect to small-dollar liquidity loans and a number of outside researchers have presented their research at seminars for Bureau staff. In addition, over the course of the past five years the Bureau has engaged in extensive outreach with a variety of stakeholders in both formal and informal settings, including several Bureau field hearings across the country specifically focused on the subject of small-dollar lending, meetings with the Bureau's standing advisory groups, meetings with State and Federal regulators, meetings with consumer advocates, religious groups, and industry trade associations, Tribal consultations, and through a Small Business Review Panel process as described further below. As described in Summary of the Rulemaking Process, the Bureau received and reviewed over one million comments on its proposal, mostly from lenders and borrowers within the respective markets.[6]

Additionally, the 2017 Final Rule explained that:

> The Bureau has analyzed its own data on consumer complaints about the issues raised by small-dollar loans and the collections efforts made by lenders and debt collectors on such loans. And the Bureau has consistently engaged in market monitoring activities to gain insights into developing trends in the market for small-dollar loans.[7]

In other words, the 2017 Final Rule stood upon a mountain of evidence, not all of it public. Almost all of it is unaddressed and unchallenged by the NPRM, and this uncontested evidence (detailed in part below) is more than sufficient to support the 2017 Final Rule.[8]

Rather than addressing the bulk of the evidence supporting the 2017 Final Rule, the NPRM takes issue with the Bureau's reliance on only two specific pieces of evidence:

(1) a study by Professor Ronald Mann about whether payday loan borrowers accurately anticipate when they will pay off their loans; and

(2) a survey by the Pew Charitable Trusts that indicates that many payday borrowers are in acute financial distresses, such that they will take a payday loan on almost any terms.

This means, among other things, that the Bureau is not taking issue in the NPRM with the fact that the payday borrower population includes a group of borrowers who

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[6] 82 Fed. Reg. 54475, Nov. 17, 2017.

[7] 82 Fed. Reg. 54503, Nov. 17, 2017.

[8] Notably, the mass of evidence supporting the 2017 Final Rule is unknown to Director Kraninger, who just days after Senate confirmation signed off on the NPRM that was prepared at Acting Director Mulvaney's behest. Without acquainting herself with the evidence supporting the 2017 Final Rule, Director Kraninger's approval of the NPRM seeking to amend the 2017 Final Rule was inherently arbitrary and capricious. While a Director is, of course, entitled to rely upon staff (not all of whom supported the NPRM), the basis for the NPRM is so thin—a mere reinterpretation of two pieces of evidence—that failure to consider the remaining basis for the 2017 Final Rule is inherently arbitrary and capricious.

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repeatedly roll over or reborrow, resulting in extended periods of indebtedness. Nor does the Bureau take issue with the high rates of default on payday loans. Nor does the Bureau take issue with the fact that many payday loan borrowers simply lack the ability to repay their loans at the end of the initial term and must reborrow or default. Instead, the Bureau is simply contesting two of the pieces of evidence that support the 2017 Final Rule's conclusions that many consumers lack an understand of the material risks, costs, or conditions of payday loans and that many consumers cannot reasonably avoid the harm caused by loans made without consideration of ability to repay.

As it happens, the Bureau's new interpretation in the NPRM of these pieces of evidence is incorrect, but even if the new, politically-motivated interpretation were correct, the Bureau's conclusions in the 2017 Final Rule would still have robust support from other sources. I address the Bureau's interpretation of the Mann Study and then the Pew Study before turning to the evidence supporting the 2017 Final Rule on these points from other sources.

2. *The NPRM's Criticisms of the 2017 Final Rule's Reliance on the Mann Study Are Specious.*

One of the sources on which the 2017 Final Rule relied was a study by Professor Ronald Mann.[9] The Mann Study was a survey of storefront payday loan borrowers that asked borrowers about their expectations for repaying their loans and compared their predictions with their actual borrowing behavior. The Bureau relied on the Mann Study in the 2017 Final Rule to support its determination that many borrowers could not reasonably avoid the substantial injuries that can occur to payday borrowers because they substantially underestimated their likelihood of ending up in an extended loan rollover sequence.

a. *Professor Mann's Interpretation of His Study Is Irrelevant Because the 2017 Final Rule Relied Solely on an Uncontested Data Point in the Mann Study, Not the Study's Interpretation of That Data*

The NPRM takes issue with the 2017 Final Rule's reliance on the Mann Study for two reasons. First, the NPRM criticizes the 2017 Final Rule for relying on the factual findings in the Mann Study while ignoring Professor Mann's interpretive gloss on the data as a whole.[10] There is clearly a disagreement between the 2017 Final Rule and Professor Mann regarding the interpretation of the empirical findings in his study, as the 2017 Final Rule itself acknowledged.[11] But it is important to start with where there is agreement.

The 2017 Final Rule and Professor Mann agree about the factual findings in the Mann Study. The NPRM does not gainsay any of Mann's factual findings. Professor Mann's study found that a around 60% percentage of the payday borrower subpopulation he studies (those who had not taken out a loan in the previous 90 days) were accurate in predicting the

[9] Ronald Mann, *Assessing the Optimism of Payday Loan Borrowers,* 21 SUPREME COURT ECON. REV. 105 (2013).

[10] 84 Fed. Reg. 4265, Feb. 14, 2019.

[11] 82 Fed. Reg. 54569, n.546, Nov. 17, 2017.

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duration of their indebtedness and thus may have had a substantial understanding of the risks involved.

Mann also found, however, that the borrowers who were the heaviest users of payday loans had much lower understanding of the product. As the 2017 Final Rule noted, Mann's finding "was largely driven by the fact that many borrowers predicted that they would not remain in debt for longer than one or two loans, and in fact this prediction was accurate for many such borrowers. But it did not address the much larger forecasting problems experienced by other borrowers, particularly those who ended up in extended loan sequences.[12] In Mann's study, the borrowers who ended up in long-term loan sequences were prone to substantially underestimate their time in debt by around 8.5 rollovers on average.[13]

Professor Mann chooses to emphasize the understanding of the large percent of the overall population, while the 2017 Final Rule concentrated on the lack of understanding among heavy users of payday loans—those most likely to incur substantial harms from their borrowing.

Such a disagreement about which findings to emphasize in interpreting the data—whether to call a bottle half full or half empty—is not an issue about the strength of the factual support for the 2017 Final Rule. The 2017 Final Rule makes this distinction clear.[14] Neither Professor Mann nor the current leadership of the Bureau disputes that Mann found there to be only limited understanding of the risks involved with payday loans from heavy users. That particular data point is what the 2017 Final Rule relied upon, not Mann's interpretive gloss on his data as a whole. The 2017 Final Rule relied on the Mann Study for a single uncontested data point. The fact that Professor Mann has a different interpretive view of the data is irrelevant to the evidentiary strength of the 2017 Final Rule.

Indeed, the undisputed data point in the Mann Study is alone sufficient to support the ability-to-repay requirement under either the "unfair" or "abusive" standard. Neither standard requires that an act or practice harm all consumers. For "unfair," it is enough for the Bureau to find that a practice is a substantial harmful that is not reasonably avoidable by some consumers and that it is not outweighed by benefits to consumers or competition. The Bureau has adduced no new evidence to challenge the original balancing analysis in the 2017 Final Rule,[15] and it is certainly reasonable to conclude that a concentrated harm on a smaller group of borrowers outweighs any benefit from access to credit to a larger group of borrowers.[16] In any event, nothing in the NPRM suggests that the balancing in the 2017 Final Rule was improper.

[12] *Id.*

[13] 82 Fed. Reg. 54569, Nov. 17, 2017.

[14] *Id.*

[15] *See supra* note 3.

[16] Moreover, it is not clear that access to credit is itself inherently a benefit if the consumer cannot realistically repay the credit.

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b. The NPRM's Claim that the Mann Study's Data Is Not Adequately Representative of Payday Borrowers Is Specious and Inconsistent with the Its Interpretation of Studies that Support Its New Political Position

Second, the Bureau claims that Mann's study is not adequately representative given its sample nature. The Bureau notes that the Mann study involved a single payday lender that operates in five states, and that the survey was administered in a limited number of locations.[17] The NPRM claims that a single lender or these five states may not be representative of payday lending nationally.[18]

This is utter speculation that is unsupported by any evidence and is in fact contrary to information the Bureau knows from its supervisory activity. The Bureau knows full well from its supervisory and enforcement activity that there are not substantial enough differences among payday lenders that would affect the representativeness of the Mann study in a material way, and indeed, the Mann Study accords with a range of other sources available to the Bureau that suggest limited borrower understanding of the risks involved with payday borrowing. The Bureau's objections to the 2017 Final Rule's reliance on the Mann study on the basis of non-representativeness strain credulity.

While there are as the Bureau notes, differences in the details of state regulation, such as whether rollovers are permitted, or the maximum finance charge allowed,[19] these differences have no material effect on the point for which the Payday Rule relied upon the Mann study—borrower understanding of the likelihood of when the borrower would succeed in repaying the loan. Most payday loans have materially similar contractual structures, and the differences that exist would not affect borrower understand of the likelihood of when the borrower would succeed in repaying the loan. This is well known to the Bureau. The Bureau has supervisory authority over payday lenders and does in fact conduct examinations of payday lenders. From this activity, the Bureau is well-aware from its supervision activity that there are not material differences in payday loans among states or lenders, and nothing in the NPRM points to any difference in state regulation that would actually have a material impact on borrower understanding of the likelihood of repayment. For the Bureau to feign concern about the representativeness of the Mann study in these regards is disingenuous and underscores the arbitrary and capricious nature of the proposed repeal of the core element of the Payday Rule under the beard of insincere concern about adequacy of evidence.[20]

Indeed, on the question of representativeness, the Bureau applies an inconsistent standard when evaluating sources that support the 2017 Final Rule and those that it believes do not. For example, the Bureau criticizes the Mann Study as possibly non-representative, even though there is no reason to believe so, but then assumes that a Federal Reserve Board survey of consumers generally—not just of the subset of consumers who are payday loan

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[17] 84 Fed. Reg. 4265, Feb. 14, 2019.

[18] *Id.*

[19] *Id.*

[20] It is notable the Bureau's current political leadership believes that in the presence of substantial consumer harm any uncertainty must always be resolved in favor of non-regulation rather than regulation.

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borrowers—is likely to be representative *of payday borrowers*, who are by definition financially different from other consumers.[21] The Bureau cannot have it both ways. The inconsistency in the Bureau's assumptions show that it approached its analysis with a pre-determined outcome based solely on political considerations.

c. *There Is No Evidence That Contradicts the 2017 Final Rule's Interpretation of the Mann Study*

Finally, the Bureau suggests that the 2017 Final Rule's read of the Mann Study's evidence must be wrong because it is inconsistent with two studies by Gregory Elliehausen about payday borrower "satisfaction."[22] In particular, the Bureau notes that only a small proportion of Elliehausen's respondents reported being dissatisfied with their most recent payday loan experience, which is suggests is inconsistent with the idea that it took consumers longer to pay off their loans than they thought they would: "if it took consumers longer to pay off payday loans than they thought it would, one might expect consumers to be dissatisfied with their payday loans. They were not."[23]

Yet a closer look at the Elliehausen studies shows that "satisfaction" is defined in a way that has no bearing on consumers' understandings of the risks of payday loans. Specifically, Elliehausen provides breakdown for the reason consumers are satisfied (or not) with their experience.[24] His most recent study (from 2009), for example, indicates that almost none of the customers were satisfied with the loans cost (less than 4%), or with the ease of getting out of debt (only 1.8%).[25] Instead, the main drivers of borrower "satisfaction' were the "easy convenient process/little paperwork" (41.3%), speed of obtaining funds (36.5%), and "Courteous/professional/friendly staff" (23.9%).[26] The Elliehausen studies are basically *customer service satisfaction surveys* that provide no indication whatsoever about consumer understandings of the risks involved with payday loans.

Similarly, the Bureau ignores other evidence in the Elliehausen survey, such as that 64.6% of customers (interviewed ex post) agree that "Payday loan companies make it hard for consumers to get out of debt."[27] In other words, Elliehausen found that nearly two-thirds of payday borrowers, when interviewed after-the-fact, believe that payday loans can be debt traps. Where the Elliehausen studies are in fact relevant, they are actually supportive of the 2017 Final Rule.

The Elliehausen studies are hardly inconsistent with the 2017 Final Rule's interpretation of the Mann Study's data. The Bureau's suggestion in the NPRM that there

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[21] 84 Fed. Reg. 4267, Feb. 14, 2019.

[22] 84 Fed. Reg. 4266, Feb. 14, 2019.

[23] *Id.*

[24] Gregory Elliehausen, *An Analysis of Consumers' Use of Payday Loans*, at 41 (2009), https://www.researchgate.net/publication/237554300_AN_ANALYSIS_OF_CONSUMERS'_USE_OF_PAYDAY_LOANS at 41.

[25] *Id.*

[26] *Id.*

[27] *Id.* at 50.

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is an inconsistency suggests that the Bureau's current political leadership is grasping at straws for a way to reverse the 2017 Final rule.

3. The NPRM's Criticisms of the Pew Study Are Specious

The Bureau also now questions the reliability of a study by the Pew Charitable Trusts[28] on which the 2017 Final Rule relied.[29] The Pew Study that finds survey evidence of many payday borrowers being in financial distress such that they do not have a meaningful choice of whether to borrow or not. The "Pew study found that 37 percent of borrowers say they have been in such a difficult financial situation that they would take a payday loan on almost any terms offered."[30] The Bureau claims that "the Pew Study is an inadequate basis for the Bureau in the 2017 Final Rule to have drawn broad conclusions about consumers' ability to take actions to protect their own interests."[31] Specifically, the Bureau criticizes the Pew Study because the Pew "survey asked respondents about their feelings, not about their actions."[32]

The Bureau's criticism of the Pew Study for being about "feelings" is inconsistent with its embrace of the Elliehausen customer satisfaction surveys discussed above. The Elliehausen studies asked respondents about their "satisfaction"—a "feeling," not about their actions. The only relevant difference is that the Pew Study supports the 2017 Final Rule, while the Elliehausen studies (in the Bureau's view) do not. Once again, this disparate application of standards to scholarship belies the Bureau's political motivation and shows that the NPRM is arbitrary and capricious.

The Bureau also concocts a set of sham criticisms of the Pew Study to question its robustness and reliability regarding the lack of other options for borrowers. For example, in the NPRM the Bureau points to "recent research" that emphasizes "the extent to which borrowing among friends and families is common among the most financially vulnerable." Yet the sole study cited by the NPRM, Jonathan Morduch & Julie Siwicki, *In and Out of Poverty: Episodic poverty and income volatility in the U.S. Financial Diaries*, at 17 (2017), https://www.usfinancialdiaries.org/paper2, is a study about the *poor*.[33] The payday borrower population is generally not poor, but lower middle class. Most notably, payday borrowers are, by definition, in the banking system. Many of the poor are not. Not surprisingly, the Morduch & Siwicki study cited by the NPRM contains no discussion whatsoever about payday borrowing for a simple reason—it is not an option for the mainly unbanked population it studied. The Bureau has pointed to no evidence in the NPRM that the same population that uses payday loans relies on information borrowing from family and friends. Accordingly, research that focuses on how the poor obtain funds, such as what the

[28] Pew Charitable Trusts, How Borrowers Choose and Repay Payday Loans, at 20 (2013), http://www.pewtrusts.org/~/media/assets/2013/02/20/pew_choosing_borrowing_payday_feb2013-(1).pdf.

[29] 84 Fed. Reg. 4267, Feb. 14, 2019.

[30] 82 Fed. Reg. 54618, Nov. 17, 2017.

[31] 84 Fed. Reg. 4267, Feb. 14, 2019.

[32] *Id.*

[33] *Id.* at 4268, n. 210.

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Bureau cites in the NPRM, is not relevant to evaluating the strength of Pew's survey research on payday borrowers.

Moreover, even if payday borrowers did sometimes borrow from family and friends, that fact has no bearing on whether they are out of options when they turn to a payday loan. Indeed, all deposition testimony I have read from payday loan borrowers in multiple litigations is that they did not feel as if borrowing from family and friends was an option, either because of the concomitant embarrassment or because their family and friends also lacked resources.

The Bureau also notes that payday loans are prohibited in a number of states, so financially distressed consumers in those states must rely on options other than payday loans. This is pure speculation by the Bureau. The fact that payday loans are prohibited in some states does not mean that they are not available. Storefront lenders can operate just beyond state lines, and many on-line payday and other short-term lenders lend in violation of the state laws (or claim to be exempt from such laws on the basis of sovereign immunity). Indeed, the Bureau has brought enforcement actions against some such on-line lenders.[34]

My point here is not to debate the ultimate correctness of the Pew Study, but to highlight the disingenuousness of the NPRM's criticisms and claims.

4. The Bureau Is Aware of Substantial Additional Evidence Supporting the 2017 Final Rule Beyond the Mann and Pew Studies and Has Not Questioned Any of This Additional Evidence

The NPRM treats the 2017 Final Rule as being grounded "primarily" on the Mann Study and Pew Study. While those studies were *part* of the basis of the 2017 Final Rule, they were hardly the entire basis for the 2017 Final Rule's conclusions that many borrowers did not adequately understand the risks of payday and other short-term, small-dollar loans or that these borrowers are frequently in acute financial distress and unable to take actions to protect their interests. As the 2017 Final Rule noted, it did not limit itself to the Mann study as its basis for concluding that the substantial consumer injury was not reasonable avoidable. Instead, as the 2017 Final Rule explained, "[a]s the Bureau perceives the matter, *based on its experience and expertise in addressing consumer financial behavior*, the observed evidence described more fully in the Section 1022(b)(2) Analysis and Market Concerns—Underwriting indicates that a large number of consumers do not understand even generally the likelihood and severity of these risks."[35]

Other sources, both public and proprietary to the Bureau's supervisory and enforcement processes, also supported the 2017 Final Rule. Indeed, there is more than an adequate basis for the 2017 Final Rule from these other sources even if the Mann Study and Pew Study were disregarded in their entirety. Thus, even if the Bureau's criticisms of the Mann Study and the Pew Study were correct, it does not follow that the 2017 Final Rule

[34] Complaint, *CFPB v. CashCall, Inc.*, No. 1:13-cv-13167 (D. Mass Dec. 16, 2013); Complaint, *CFPB v. NDG Financial Corp.*, No. 1:15-cv-05211 (S.D.N.Y. July 31, 2015); Complaint, *CFPB v. Think Finance, LLC*, No. 4:17-cv-00127 (D. Mont. Nov. 15, 2017).

[35] 82 Fed. Reg. 54597-98, Nov. 17, 2017.

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lacked evidentiary support for its conclusions regarding borrowers' understanding of risk or ability to protect their interests.

I outline below five types of sources that supported the 2017 Final Rule that are not discussed at all in the NPRM.

a. Propriety Information from the Supervisory and Enforcement Processes Supports the 2017 Final Rule.

First, the 2017 Final Rule was supported by the Bureau's proprietary information gathered from enforcement actions and the supervisory process.[36] As the 2017 Final Rule explained:

> The Bureau's understanding of these loans, and how they affect consumers, has also been furthered by its ongoing supervisory activity, which involves exercising its legally mandated authority to conduct formal examinations of companies who make such loans and of debt collectors who collect on such loans. These examinations have canvassed the operations, marketing, underwriting, collections, and compliance management systems at such lenders and continue to do so on an ongoing basis. In addition, the Bureau has investigated and taken enforcement actions against a number of small-dollar lenders, which has provided further insight into various aspects of their operations and the practical effects of their business models on consumers.[37]

I have been privy to some of this proprietary supervisory information in my capacity as an expert witness for the Bureau. While I cannot divulge this information in a public comment letter such as this, I want to strongly emphasize that the discovery produced in litigation and information obtained in the supervisory process supports the 2017 Final Rule.

For example, the Bureau is aware of internal marketing materials from payday lenders that illustrate that lenders are aware that borrowers are likely to get stuck in a "debt trap," and that lenders actively attempt to ensnare consumers into such debt traps.[38] Referencing only two publicly available pieces of information, in the Bureau's enforcement action against ACE Cash Express, one of the largest payday lending chains in the nation, the Bureau discovered an internal training document that illustrates a "cycle of debt" desired by the

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[36] *See* 82 Fed. Reg. 54503, Nov. 17, 2017. *See also* 82 Fed. Reg. 54505, Nov. 17, 2017 ("the Bureau has developed a broader understanding of small-dollar lending through its supervisory and enforcement work.").

[37] 82 Fed. Reg. 54503, Nov. 17, 2017. *See also* 82 Fed. Reg. 54505, Nov. 17, 2017 ("the Bureau has developed a broader understanding of small-dollar lending through its supervisory and enforcement work."), and 82 Fed. Reg. 54475, n.14 (noting that "Information underlying this proposed rule is derived from a variety of sources, including from market monitoring and outreach, third-party studies and data, consumer complaints, the Bureau's enforcement and supervisory work, and the Bureau's expertise generally. In publicly discussing information, the Bureau has taken steps not to disclose confidential information inappropriately and to otherwise comply with applicable law and its own rules regarding disclosure of records and information.").

[38] *See, e.g.*, 82 Fed. Reg. 54563 ("Supervisory evidence also supported the Bureau's conclusion that payday lenders were encouraging long loan sequences.").

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lender, in which the consumer is constantly borrowing to pay off previous loans.[39] Likewise, in the Bureau's enforcement action against All-American Check Cashing,[40] the Bureau discovered a cartoon shared by All-American employees in which a payday lender is pointing a gun at a consumer and insisting that the consumer take the money, the idea being that the way to rob the consumer is to have the consumer take out the loan.

While these are illustrations from materials that are publicly available, the non-public record contains substantially more examples suggesting that the payday lending industry itself believes that consumers are likely to fall into debt traps, and encourages them to do so. In other words, the industry's internal documents are consistent with consumers being unable to reasonably avoid harms from a cycle of debt and/or not understanding the material risks and costs associated with payday loans.

b. Payday Lender Advertising Supports the 2017 Final Rule.

The Bureau is also aware from its supervisory activity and general market research of payday lender advertising.[41] Payday loan advertising provides a strong indication—the informed belief of payday lenders themselves, backed up by advertising dollars—of what their customer base looks like. Payday consumers often have acute liquidity needs—for repairing a car so they can get to work, for fixing a broken fridge full of groceries, for paying for a family member's funeral—such that time is at a premium for them and they do not have the luxury of being able to shop around for the lowest cost or safest source of credit. Moreover, many payday borrowers have impaired credit and therefore assume (correctly) that their borrowing options are limited. As a result, the payday borrower population includes many consumers desperate for credit and with few options. This is reflected in payday lender advertising.[42]

First, many payday lenders have names that indicate the premium borrowers put on getting funding fast. Lenders often have names that emphasize the speed at which funds are available to borrowers: "Cash Now," "ACE Cash Express," "FastBucks," "Cash-in-a-Snap," "Loan-N-Go," and "Speedy Cash Loans."

Second, payday lenders and payday loan lead generators advertise with slogans like "Need cash fast?"[43] "Need cash now?"[44] "Fast, same day credit" and "Bad Credit? Not a Problem!" These advertisements also indicate that borrowers place a premium on getting funds fast. Many lenders' and lead generators' websites also emphasize the idea that borrowers might be facing an emergency—a duress situation. For example, one lender's

[39] CFPB, *CFPB Takes Action Against ACE Cash Express for Pushing Payday Borrowers into Cycle of Debt*, July 10, 2014, *at* https://www.consumerfinance.gov/about-us/newsroom/cfpb-takes-action-against-ace-cash-express-for-pushing-payday-borrowers-into-cycle-of-debt/.

[40] Complaint, *CFPB v. All American Check Cashing*, No. 3:16-cv-356 (S.D. Miss. May 11, 2016) at 15, at https://files.consumerfinance.gov/f/documents/201605_cfpb_complaint-for-permanent-injunction-and-other-relief-all-american-check-cashing-inc.pdf.

[41] 82 Fed. Reg. 54503, 54561-62, Nov. 17, 2017.

[42] Expert Report of Professor Adam J. Levitin, *Illinois v. CMK Investments, Inc.*, No. 14-C-2783 (N.D.Ill.), ¶ 77-78.

[43] https://www.cashnetusa.com/no-credit-check-fast-cash.

[44] https://www.needcashnow.org/.

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website explains, its loans "are designed to help you meet your short-term emergency borrowing needs."[45] Others indicate that their loans are for "When you need a cash advance for a financial emergency, [and] you don't have time to wait on your funds."[46] Payday loan advertising indicates that lenders are targeting a population of consumers in immediate financial duress and is consistent with the finding of the Pew Study on which the 2017 Final Rule reasonably relied.

c. Payday Lender Price Competition Supports the 2017 Final Rule.

The 2017 Final Rule's findings that consumers are consumer are unable to protect their interests when using payday loans or to reasonably avoid harm from payday loans is also supported by the unusual nature of payday lender competition, a situation of which the Bureau was well-aware when it promulgated the 2017 Final Rule. To the extent that payday lenders compete, it is not generally price competition, but competition based on convenience and customer service.[47] The Bureau is aware of the unusual nature of the price competition because it repeatedly cited the leading article on it, Mark Flannery & Katherine Samolyk, "Payday Lending: Do the Costs Justify the Price?," (FDIC Ctr. for Fin. Res., Working Paper No. 2005–09, 2005), in the 2017 Final Rule.[48]

Additionally, the Bureau is aware of the unusual nature of price competition in payday lending based on an expert report I prepared for the Bureau in 2016 in the *All-American Check Cashing* litigation. The Bureau successfully defended the admissibility of my report in 2018 as part of on-going litigation. My report noted deposition testimony from the employee of the defendant payday lender that indicated that consumers were not focused on pricing terms:

> Q. Customers don't ever come into the store and say, 'I would like to take a loan. How much is the fee?'
>
> A. That's not a normal question, no. They want to know, can I get some money today.[49]

This testimony is consistent with deposition testimony in other payday lending litigation.[50]

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[45] https://www.plaingreenloans.com.

[46] https://www.cashnetusa.com/no-credit-check-fast-cash. *See also* https://guaranteedloansnow.org/we-approve-your-emergency-loan-application-immediately/ *and* https://www.cashinasnap.com/emergency-payday-loan.

[47] Mark Flannery & Katherine Samolyk, "Payday Lending: Do the Costs Justify the Price?," (FDIC Ctr. for Fin. Res., Working Paper No. 2005–09, 2005), *at* https://www.fdic.gov/bank/analytical/cfr/2005/wp2005/cfrwp_2005-09_flannery_samolyk.pdf.

[48] 82 Fed. Reg. 54481, n. 57, , Nov. 17, 2017; 82 Fed. Reg. 54481, n. 64, Nov. 17, 2017; 82 Fed. Reg. 54484, n. 98, Nov. 17, 2017; 82 Fed. Reg. 54842, n. 1223, Nov. 17, 2017.

[49] Levitin Report, *CFPB v. All American Check Cashing*, No. 3-16-cv-356 (S.D. Miss.), p. 26, n. 110.

[50] Expert Report of Professor Adam J. Levitin, *Illinois v. CMK Investments, Inc.*, No. 14-C-2783 (N.D.Ill.),¶¶ 59-76.

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Additionally, my report noted that almost all storefront payday lenders price up to the legal maximum despite substantial pricing differences across state lines.[51] If borrowers were price elastic (beneath some reserve point), such pricing disparities should not exist. This price inelastic demand is consistent with the finding in the Pew Study that borrowers will take the loans on almost any terms offered because of their financial distress. The concern of many payday borrowers is getting cash *now*, not the cost of borrowing. As a result, many payday borrowers are unable to adequately protect their interests through the market because of their financial distress.

d. An Empirical Study by Professor Nathalie Martin Also Supports the 2017 Final Rule.

Fourth, the Bureau was aware of an academic study that both supported its original interpretation of the Mann Study and buttresses the Pew Study. Specifically, the Bureau was aware of an article by Professor Nathalie Martin of the University of New Mexico School of Law entitled *1,000% Interest—Good While Supplies Last*, 52 ARIZ. L. REV. 563 (2010). The Bureau was aware of this article as part of its original rulemaking because the article was attached to two of the public comments submitted to the Bureau[52] and also referenced in several other comment letters.

Professor Martin's article includes an empirical study of payday loan borrowers. Specifically, Professor Martin interviewed some 109 payday loan borrowers at numerous New Mexico storefront locations. The Martin Study reports the results of the interviews. It finds that payday borrowers have little sense of the annual percentage rate (APR) on their loans and little sense of what their loans are actually going to cost in dollar terms. Nearly 60% of borrowers—who had just exited the store after completing their transactions—had no idea what their APR was, while another 16% hazarded guesses that were a magnitude off. Nearly a fifth of respondents couldn't describe the dollar cost of their borrowing, while nearly 40% of borrowers inaccurately described the dollar cost of their borrowing. Additionally, nearly 80% of borrowers did not shop around for loan terms, and choice of lender was driven more by the convenience of a storefront location than by any other factor; almost no respondents cited the economic terms of the loans as being factors in their choice of lender.

Professor Martin's findings are consistent with the 2017 Final Rule's interpretation of the Mann Study—a majority of payday borrowers simply do not understand the basic terms of the product and thus the material risks they assume. Accordingly, these risks are not reasonably avoidable and the consumer cannot protect his or her interests when selecting or using the product. It is also consistent with the Bureau's original interpretation of the Pew

[51] *See, e.g.*, Pew Charitable Trusts, How State Rate Limits Affect Payday Loan Prices, Fig. 2, April 2014, https://www.pewtrusts.org/~/media/legacy/uploadedfiles/pcs/content-level_pages/fact_sheets/stateratelimitsfactsheetpdf.pdf.

[52] Attachment to Comment of Mary Stokes, Nov. 22, 2016, ID CFPB-2016-0025-161909, https://www.regulations.gov/document?D=CFPB-2016-0025-161909; Attachment to Comment of Ola Vought, Nov. 10, 2016, ID CFPB-2016-0025-155183, *at* https://www.regulations.gov/document?D=CFPB-2016-0025-155183.

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Study, namely that payday borrowers are in financial distress and do not engage in meaningful comparison shopping such that they cannot reasonably protect their interests.[53]

e. Consumer Narratives in Comment Letters Support the 2017 Final Rule.

The Bureau was aware of consumer narratives in over 1 million comment letters filed as part of the rulemaking[54] and with complaints in its complaint database.[55] These letters, both in favor and against the 2017 Final Rule, as well as complaints in the complaint database, amply illustrate that many payday borrowers borrow when they are in acute financial distress and without other options and thus without ability to protect their interests.

f. Comment Letters from State Attorneys General and Legal Aid Organizations Support the 2017 Final Rule.

The Bureau was aware of the findings of state attorneys general and legal aid organizations that were submitted as comments on the 2017 Final Rule. Included in these submissions as an attachment to a comment letter by the Illinois Attorney General was an expert report I produced for the Illinois Attorney General in a case called *Illinois v. CMK Investments, Inc.*, No. 14-C-2783 (N.D.Ill.). In that report, I made the same point as the Pew Study, albeit based on different sources, particularly, deposition testimony from payday borrowers and advertising materials from payday lenders all of which indicate that payday borrowers are a group in acute financial distress such that they will generally not shop for better terms, but merely take whatever product they are offered. As such, payday borrowers are not reasonably able to protect their interests or avoid loans that are empirically likely to be debt traps for many borrowers because they are not made with any consideration of the borrower's ability to repay.

g. The Bureau Needs to Explain Why All of the Other Myriad Sources that Are Consistent with the 2017 Final Rule's Interpretation of the Mann Study and Pew Study Are Invalid.

The Bureau's original rulemaking did not stand solely on the Mann Study or the Pew Study. While these happened to be among the studies the Bureau chose to cite in the background materials explaining its rationale for the rule, they were not the full measure of the sources the Bureau considered. Nothing requires the Bureau to cite specifically, much less exhaustively, the sources on which it relies in a rulemaking; any citations provided are merely illustrative. The Bureau has always been aware of additional sources that supported its original rulemaking. These sources are consistent with the Bureau's original interpretation of the Mann Study and the Pew Study. While the Bureau now disavows its original interpretation of the Mann Study and casts shade on the Pew Study, it has nothing whatsoever to say about its other sources. These sources still stand and continue to support the Bureau's rulemaking. Unless the Bureau can also explain why these other sources—

[53] Methodologically, the Martin Study is superior to the Mann Study. Unlike Mann, Martin did not allow a payday industry consultant to select her interviewees. Moreover, unlike Mann, Martin did not exclude from her sample all borrowers who had had a payday loan in the previous 90-days (thereby excluding rollovers). This means that Martin's study is more likely to be representative than Mann's.

[54] 82 Fed. Reg. 54475, Nov. 17, 2017.

[55] 82 Fed. Reg. 54475, n. 14, Nov. 17, 2017.

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including sources it has defended in federal court—are somehow now not reliable, it should not proceed with the proposed Rule.

B. The NPRM Applies the Incorrect Legal Standard for Unfair and Abusive

In the NPRM, the Bureau argues that it previously applied an incorrect legal standard in the 2017 Final Rule regarding both "unfair" and "abusive". This attempt to redefine the appropriate legal standard is part and parcel with the Bureau's spurious evidentiary claims in the NPRM. Only by moving the goal posts does the NPRM manage to justify itself. Before turning to the substance of the problems with the Bureau's redefinition of the applicable legal standard, it is necessary to address the process itself.

1. The NPRM's Backdoor Definition of "Unfair" and "Abusive" Without APA Notice-and-Comment Is Illegal.

The Bureau is attempting to institute a backdoor definition of both "unfair" and "abusive" without going through the APA notice-and-comment rulemaking process. This is illegal. Once again, it would appear that nothing changed except the Bureau's political leadership, that would explain the new view of the legal requirements. The Bureau criticizes the 2017 Final Rule for having applied the wrong legal standard to "unfair" and "abusive," yet the Bureau has not ever formally articulated a standard.

The Consumer Financial Protection Act restricts the Bureau from declaring an act or practice to be "unfair" or "abusive" unless the act meets certain statutorily defined characteristics.[56] The Bureau has not undertaken any rulemakings to date to define "unfair" or "abusive." The Bureau is, of course, free to undertake such rulemakings through the required notice-and-comment process, but until and unless it does, the Bureau cannot claim that there is a proper legal standard that it did not previously follow.[57] Doing so would operate as a *de facto* definitional rulemaking, but without the required notice-and-comment process. The fact that the NPRM is itself a notice-and-comment rulemaking does not cure this procedural defect because the Bureau does not purport to actually define "unfair" or "abusive," but merely to claim that the interpretation in the 2017 Final Rule was incorrect.

2. The NPRM Applies the Incorrect Legal Standard for Unfairness

a. Reasonable Avoidability Requires an Understanding of Specific Risks, Not Merely a General Awareness that Risks Might Exist.

The NPRM claims that the 2017 Final Rule applied the incorrect legal standard for unfairness because it supposedly required consumers to "have a specific understanding of their individualized likelihood and magnitude of harm such that they could accurately predict how long they would be in debt after taking out a covered short-term or longer-term

[56] I note that read literally, the restriction applies solely to the Bureau and not to other entities that have authority to enforce the prohibition against unfair, deceptive, and abusive acts and practices.

[57] While the Bureau cites to the Federal Trade Commission's Policy Statement on Unfairness, it is important to note that the Policy Statement is not law that binds no one. The FTC cannot cite the Policy Statement in enforcement actions because it is merely an informal statement of policy, not a regulation that was promulgated through a notice-and-comment rulemaking process.

balloon- payment loan for the injury to be reasonably avoidable."[58] In particular, the NPRM claims that the 2017 Final Rule would require consumers to know "their *individualized* likelihood and magnitude of harm" in order to reasonably avoid injury.[59] This is a mischaracterization of the 2017 Final Rule.

b. The 2017 Final Rule Does Not Require an Individualized Understanding of Risks and Harms

The 2017 Final Rule did not apply an "individualized" standard for consumer understanding of likelihood and magnitude of harm as part of its "reasonably avoidable" analysis, and even if it did, that would not invalidate the "reasonably avoidable" analysis because a consumer can have a perfect understanding of the likelihood and magnitude of harm and still not be able to reasonably avoid the harm, as is the case with some of the harms from payday loans.

The 2017 Final Rule does not require an understanding of individualized risk. Instead, it applies a "reasonably aware" standard:

> [U]nless consumers are reasonably aware of the likelihood and severity of these injuries, it would not be reasonable for them to make special efforts to avoid such injuries where they are not in position to accurately evaluate the risks. This may be especially the case where the lender qualifies them for a loan without making a reasonable assessment of their ability to repay, as many consumers would be unlikely to expect that lenders would intentionally offer them an unaffordable loan that they would likely be unable to repay.
>
> That is not to say that every consumer must understand everything about the potential risks or must be able to anticipate these risks with mathematical precision. Instead, it is only to say that consumers must have a sense of the order of magnitude of the risk, both in terms of its likely frequency and its likely severity.[60]

The 2017 Final Rule only discusses individualized understanding in the context of a discussion explaining why a disclosure remedy would be inadequate. The 2017 Final Rule does not actually endorse individualized disclosure. Instead, its position is that no disclosure is likely to work, except perhaps individualized disclosures:

> In light of these circumstances, the Bureau finds that generalized disclosures to consumers will not prevent the unfair and abusive practice identified above or equip consumers to avoid the harms it causes as effectively as prohibiting lenders from engaging in the unfair and abusive practice in the first instance.
>
> The only disclosure that the Bureau could envision that could come close to positioning consumers to mitigate the unfair and abusive practice effectively would be an individualized forecast of whether the consumer could afford to

[58] 84 Fed. Reg. 4269, Feb. 14, 2019.
[59] *Id.* (emphasis added).
[60] 82 Fed. Reg. 54594, Nov. 17, 2017.

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> repay the loan according to its term, and if not, a forecast of how long such repayment would be reasonably expected to take.[61]

The NPRM is criticizing the 2017 Final Rule for applying a standard that it did not in fact use.

c. Consumers Lack An Awareness of the Specific Types of Harms that Can Stem from Payday Borrowing

The NPRM contends that the proper standard for consumer awareness of risk of harms is that consumers:

> have an understanding of the likelihood and magnitude of risks of harm associated with payday loans sufficient for them to anticipate those harms and understand the necessity of taking reasonable steps to prevent resulting injury. Specifically, this means consumers need only to understand that a significant portion of payday borrowers experience difficulty repaying and that if such borrowers do not make other arrangements they either end up in extended loan sequences, default, or struggle to pay other bills after repaying their payday loan.[62]

This standard appears to be materially the same as that applied in the 2017 Final Rule: reasonable awareness of the likelihood and severity of injuries, meaning a sense of the order of magnitude of the risk in terms of both likelihood and severity. It is unclear what meaningful difference exists in these standards.

Irrespective, of the precise standard, however, 2017 Final Rule's evidentiary findings would still support a conclusion that consumers cannot readily avoid injury. As the 2017 Final Rule stated, the typical consumer is not likely to be familiar with all of the harms that can flow from a default on a payday loan:

> Some additional harms beyond the costs incurred on the loan can include, for example, the risk of accumulating penalty fees on their bank account, the potential loss of their account, or (for title loans), or the risk of aggressive collections.[63]

The NPRM gives no suggestion that consumers have an understanding of the particular type of risks that they face.

d. The NPRM Wrongly Suggests That Payday Borrowers Understand the Risks of Harm from Payday Loans

The NPRM claims that consumers who reborrow would inherently have an understand of the risks of the product from their own experience. While this may be true regarding their understanding of the risks, which is relevant for an analysis under 12 USC 5531(d)(2)(A)'s "abusive" standard, it is actually evidence in support of the 2017 Final Rule's determination on "unfairness" because it indicates that even if these consumers

[61] 82 Fed. Reg. 54637, Nov. 17, 2017.
[62] 84 Fed. Reg. 4270, Feb. 14, 2019.
[63] 82 Fed. Reg. 54594, Nov. 17, 2017.

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understood the product and its risks from their past experience, they are still back using them again and therefore cannot avoid the products.

Similarly, the NPRM suggests that a plausible interpretation of a study indicating that state-mandated payday loan term disclosures had little effect on borrowing habits because consumers were already aware of the terms and risks.[64] This suggestion strains credulity and goes against everything known in the scholarly community and to the Bureau through its supervisory function about payday loan borrowers. It is also contradicted by the Martin Study, which indicates borrowers frequently have no idea whatsoever about the terms of loans they just took out minutes before being surveyed.[65] That the Bureau would make such a far-fetched claim is again an indication of just how desperate its new political leadership is to avoid implementing the 2017 Final Rule.

e. Consumer Awareness of Risk of Harms Is Only Part of the Reasonable Avoidability of Injury Analysis

The NPRM assumes that if the 2017 Final Rule applied the incorrect standard for consumer awareness of the risk of harm that the 2017 Final Rule is irreparably flawed. This is incorrect. Even if the 2017 Final Rule's standard for consumer awareness of risk of harm were wrong, the 2017 Final Rule's application of the legal standard for whether injuries are "reasonably avoidable" would still remain the relevant touchstone, and the 2017 Final Rule makes clear that consumer awareness of risk of harm is not the totality of the "reasonable avoidable" analysis for unfairness.

It is possible for circumstances to exist in which a consumer has perfect awareness of the risk of harm from a financial product, but nonetheless uses that product because of limited choice given the consumer's situation. This is exactly the argument made by the 2017 Final Rule, and the NPRM does nothing to gainsay it. The 2017 Final Rule states that the problem with even individualized disclosures is that

> the only option for a consumer warned about the risks of an unaffordable loan is simply not to take out the loan at all, since once a consumer takes out a loan that in fact turns out to be unaffordable the consumer's only options are to choose between the harms associated with default, re-borrowing, or forgoing other major financial obligations or basic living expenses.[66]

The "just say no" option is does not constitute "reasonable avoidability," as the 2017 Final Rule rightly explains:

> [T]he Bureau does not accept, and the FTC and prudential regulators have never been satisfied with, the notion that injury is avoidable just because a consumer has the right not to enter the market in the first place. No precedent supports the idea that the existence of such a right is by itself an answer to the ''reasonably avoidable'' issue. Indeed, a consumer generally has a right to decline to initiate the purchase of any product or service, and if the mere

[64] 84 Fed. Reg. 4271, Feb. 14, 2019.

[65] Nathalie Martin, *1,000% Interest—Good While Supplies Last*, 52 ARIZ. L. REV. 563 (2010).

[66] 82 Fed. Reg. 54618, Nov. 17, 2017.

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> existence of that right were the end of the "reasonably avoidable" question, then no act or practice by a seller would ever be subject to regulation on unfairness grounds.[67]

The NPRM does not argue against this point. Instead, the NPRM claims the 2017 Final Rule wrongly requires an individualized consumer awareness analysis to determine reasonable avoidability of injury. The 2017 Final Rule does not in any way require such a patently absurd analysis, but even if it did, the 2017 Final Rule makes clear that reasonable avoidability of injury does not depend on such an analysis because of the acute financial distress faced by many payday borrowers. In many cases, the alternative to payday loan borrowing result in worse outcomes for consumers; as a result, consumers cannot reasonably avoid the harms that can follow from payday loan borrowing.

3. The Bureau Mistakes Competitors for Competition

Unfairness requires a consideration of the effect on consumers and "competition." Yet the Bureau wrongly interprets "competition" as meaning "competitors," and incorrectly assumes that the more competitors exist in the payday industry, the greater competition will be.

In the 2017 Final Rule, the Bureau estimated that the Rule's Mandatory Underwriting Provisions would result in "a large (55 to 62 percent) contraction of the storefront payday industry—an industry that includes over 2,400 small businesses—and the virtually complete elimination of the single-payment vehicle title industry—an industry that includes over 800 small businesses."[68] The NPRM assumes that the result would be deleterious to consumer welfare because of a reduction in consumer choice and access to credit. The evidence and a consideration of payday industry economics does not support such a conclusion, however.

First, the NPRM misrepresents the 2017 Final Rule. The 2017 Final Rule predicted a 55-62% reduction in the number of loans.[69] That does not necessarily translate into any reduction of the number of lenders. The NPRM adduces no evidence regarding the number of storefront payday lenders that will be affected by the 2017 Final Rule.

The whole reason the "unfairness" standard includes a consideration of "competition" is because competition is a proxy for consumer welfare. Generally, greater competition results in better terms of consumers. And greater competition generally involves more competitors. Payday lending, however, is an unusual market in which low barriers to entry have resulted in cannibalistic competition that drives *up* prices. Specifically, store front payday lenders have few unique customers per store. This means that fixed and semi-variable costs must be recovered from a relatively small borrower base. The result is to set a pricing floor for those consumers.[70] If there were fewer lenders operating, there would be more

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[67] 82 Fed. Reg. 54596, Nov. 17, 2017.

[68] 84 Fed. Reg. 4264, Feb. 14, 2019.

[69] 82 Fed. Reg. 54826, Nov. 17, 2017.

[70] Mark Flannery & Katherine Samolyk, "Payday Lending: Do the Costs Justify the Price?," (FDIC Ctr. for Fin. Res., Working Paper No. 2005–09, 2005), *at* https://www.fdic.gov/bank/analytical/cfr/2005/wp2005/cfrwp_2005-09_flannery_samolyk.pdf.

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borrowers per store, and, perhaps counterintuitively, lower prices per borrower as costs would be amortized over a larger borrower base, allowing for competition to push down pricing.

The experience of Colorado after its 2007 payday reforms supports this conclusion.[71] Following its reform, the number of payday lenders in Colorado substantially contracted, but the lending volume remained stable, and the cost of loans dropped, as did rollover risk[72] Thus, while the Mandatory Underwriting Provisions in the 2017 Final Rule will likely result in many storefront payday lenders ceasing to operate, a contraction in the number of lenders may in fact increase consumer welfare because it will drive prices down.

Moreover, in the case of single-payment vehicle title lenders, the 2017 Final Rule did not conclude, nor does the Bureau now adduce any evidence in the NPRM that these firms would go would of business. Indeed, the more likely effect of the Mandatory Underwriting Provisions is that these businesses will adopt their product offerings to the rule. Thus, firms that offer single-payment vehicle title loans will likely shift to installment payment structures that are less likely to result in consumers finding themselves in unsustainable debt traps. Such a shift in the product market would improve consumer welfare without reducing consumer choice in terms of service providers. (There is no evidence that consumers have a meaningful preference between single-payment versus installment vehicle title loans.)

C. The NPRM Applies the Incorrect Legal Standard for Abusive Acts and Practices

1. The NPRM Wrongly Criticizes the Legal Standard Applied by the 2017 Final Rule Regarding Consumers' Lack of Understanding of Material Risks, Costs, or Conditions

The NPRM also argues on the same basis as it does for reasonable avoidability of injury for "unfairness" analysis that the 2017 Final Rule applied the wrong legal standard for "abusiveness" under 12 U.S.C. § 5531(d)(2)(A), which involves a covered person or service provider taking unreasonable advantage of consumers' lack of understanding of material risks, costs, or conditions.[73] The NPRM argues that the 2017 Final Rule incorrectly applied an individualized standard of knowledge, when a generic one would suffice. As noted above, in section II.B.2.i, this is a blatant mischaracterization of the 2017 Final Rule. It did not apply an individualized standard, but more generalized standard (although perhaps not as generic as that suggested by the NPRM).

2. The NPRM Wrongly Criticizes the Legal Standard Applied by the 2017 Final Rule Regarding Taking Unreasonable Advantage

The term "abusive" is defined by statute, 12 U.SC. § 5531(d). The statutory definition contains four potential categories of abusive behavior. Three of those categories

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[71] The Pew Charitable Trusts, *Trial, Error, and Success in Colorado's Payday Lending Reforms*, Dec. 2014, *at* https://www.pewtrusts.org/~/media/assets/2014/12/pew_co_payday_law_comparison_dec2014.pdf.

[72] *Id.*

[73] 84 Fed. Reg. 4274-75, Feb. 14, 2019.

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involve a covered person or service provider "taking unreasonable advantage" of consumers in certain situations. The 2017 Final Rule was promulgated both on the basis of 12 U.S.C. § 5531(d)(2)(A), which prohibits taking unreasonable advantage of "a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service" and 12 U.S.C. § 5531(d)(2)(B), which prohibits taking unreasonable advantage of "the inability of the consumer to protect the interests of the consumer in selecting or using a consumer financial product or service."

Both of these prongs of "abusive" require a consideration of what constitutes "taking unreasonable advantage." The 2017 Final Rule explained that:

> [a]t a minimum lenders take unreasonable advantage of borrowers when they [1] develop lending practices that are atypical in the broader consumer financial marketplace, [2] take advantage of particular consumer vulnerabilities, [3] rely on a business model that is directly inconsistent with the manner in which the product is marketed to consumers, and [4] eliminate or sharply limit feasible conditions on the offering of the product (such as underwriting and amortization, for example) that would reduce or mitigate harm for a substantial population of consumers.[74]

The NPRM takes issue with each one of these four elements in the 2017 Final Rule's rubric for "taking unreasonable advantage." In each case the NPRM is wrong.

First, the NPRM argues that the mere fact that a consumer financial product is unusual does not constitute unreasonable advantage taking, lest any innovative product be considered abusive. This argument misconstrues the 2017 Final Rule. The 2017 Final Rule did not say that a product being unusual in and of itself constitutes unreasonable advantage taking. Instead, the unusual nature of a product is one of four factors that in combination result in unreasonable advantage taking. The 2017 Final Rule was correct to consider the unusual nature of a product as a factor in evaluating unreasonable advantage taking because unusualness goes to the likelihood of consumer understanding and therefore also the ability of a consumer to protect his interests because consumers are less likely to understand an unusual product and if consumers do not understand a product, they cannot be expected to take actions to protect their interests.

The NPRM also argues that payday loans are not unusual insofar as they lack consideration of the borrower's ability to repay. In support of this argument, the NPRM cites student loans, reverse mortgages, and secured credit cards. This is, again, disingenuous. The Bureau well knows that most student loans do effectively have a back-end ability-to-repay requirement in the form of income-driven repayment options. Moreover, federal student loans are among the most consumer-friendly financial product in existence, with a set of protections unparalleled by any other product—automatic forbearance and deferment, forgiveness, no late charges, and no compounding of interest. Likewise, reverse mortgages are subject to the most extensive disclosure regime of any consumer financial product—a regime administered by the Bureau and designed to ensure consumer understanding of

[74] 82 Fed. Reg. 54623, Nov. 17, 2017 (bracketed numbers added).

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risks.[75] And secured credit cards are not credit products in any meaningful sense. They are payment products—the consumer deposits, say, $300 as collateral with the card issuer and gets a payment card that can be used to spend up to $300. While there are other credit products that do not consider borrower ability to repay, such products are the exception, not the rule. Instead, lending in the major non-governmental consumer finance markets—regular mortgages, regular credit cards, and auto loans—are all based on consumer ability to repay.

Second, the NPRM argues that the 2017 Final Rule did not show actual The NPRM baldly asserts that "the 2017 Final Rule did not adequately explain how the practice of not reasonably assessing a consumer's ability to repay a loan according to its terms leveraged particular consumer vulnerabilities."[76] This is an astonishing claim. The entire 450-page 2017 Final Rule is an extended explanation of how failure of payday lenders to assess a consumers' ability to repay leverages financially distressed consumers' vulnerability to place them in loan products that are likely to result in unanticipatedly long periods of indebtedness and with it more finance charges and other adverse consequences. If borrowers' ability to repay were to be considered, the 2017 Final Rule explains, then such extended periods of indebtedness and knock-on consequences would cease to be as likely. While the NPRM tendentiously questions the strength of the evidence supporting the 2017 Final Rule's findings regarding consumer vulnerability (addressed above regarding the Mann Study and Pew Study), it takes willful blindness and a large dose of chutzpah for the Bureau to now claim that the 2017 Final Rule failed to adequately explain the way payday loans exploit borrower vulnerabilities by failing to consider borrower ability to repay.

Even more bizarrely, the NPRM misreads the 2017 Final Rule's reference to "particular consumer vulnerabilities" as referring to the vulnerabilities of particular consumers, rather than particular types of vulnerabilities common among the borrower population. Thus, the NPRM criticizes the 2017 Final Rule for failing to "conclude that lenders had the ability to identify consumers with particular vulnerabilities prior to lending and use that information to treat some consumers differently than others, for example, by charging them different prices or including different terms in contracts for them."[77] Obviously targeting particularly vulnerable consumers—those with cognitive impairments, natural disaster victims, or those with limited English proficiency for example—would qualify, but targeting a consumer population that is generally in financial distress should be sufficient insofar as borrowers in financial distress are vulnerable because of their constrained ability to shop around among potential credit offers given the exigency of time. Few if any borrowers who are not experiencing some level of financial distress frequent payday lenders. In that sense, there is no reason to expect lenders to differentiate within the borrower population. More importantly, lenders have no way of readily distinguishing borrowers' level of financial distress short of undertaking a costly underwriting.

[75] 12 C.F.R. § 1026.33.
[76] 84 Fed Reg. 4275, Feb. 14, 2019.
[77] 84 Fed. Reg. 4275-76, Feb. 14, 2019.

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Third, the NPRM questions the 2017 Final Rule's conclusion that an inconsistency between how a product is marketed to consumers and a lender's business model is relevant to unreasonable advantage taking. The NPRM argues that "whether or not consumers understand the lender's revenue structure does not in itself determine whether they lack understanding about the features of the loan that they choose to take out."[78] Yet again, the NPRM's criticism is wrong.

The traditional lender-borrower relationship is a type of partnership, in which the lender only makes money if the borrower repays according to the terms of the loan. Hence the term "credit," comes from the Latin *credere*—to believe, as in the lender believing the borrower will repay. Consumers reasonably expect that lenders will not make loans to them that they cannot handle. In this regard, the payday business model is fundamentally misleading. The economics of payday lending depend on rollovers. Yet payday loans are marketed to consumers as short-term loans, where the lender expects to be repaid on payday, rather than the expectation being a longer-term balloon loan with periodic interest payments. The effect of the disconnect is that consumers are lulled into thinking that they can repay the loan according to its original terms, rather than rolling it over.

It is inherently unreasonable advantage-taking to make a consumer a loan that is labelled and advertised as short-term credit, when the lender knows and hopes and bases its entire business model on the consumer failing to repay the loan according to its terms and rolling it over. Put another way, payday lenders want consumers to fail to repay the loan according to its terms. Providing consumers a product that is designed to fail is unreasonable advantage taking if anything is.

Finally, the NPRM argues that a lender's decision not to offer features that would mitigate a products harm are not unreasonable advantage taking. Again, by itself, the failure to offer such a feature is not unreasonable advantage taking. But in combination with the other three factors identified in the 2017 Final Rule it clearly is. In particular, when combined with the other three factors, the failure to offer a feasible feature that mitigates harms goes to both the unreasonableness and the advantage taking because it presses consumers with a harm that can be readily avoided *by the business*.

Ultimately, the NPRM's criticisms of the 2017 Final Rule's analysis have to be viewed holistically: the political stance of the Bureau under the NPRM is effectively that there is no practice that is "abusive." Indeed, the Bureau has not brought a single enforcement action alleging "abusiveness" under the Mulvaney-Kraninger directorships. One has to ask, if the factors outlined by the 2017 Final Rule are not relevant to "taking unreasonable advantage," then what possibly is? The NPRM simply "doubts" and "questions" the 2017 Final Rule's analysis of abusive to the point that there is no practice that would be taking unreasonable advantage and thus be abusive under 12 U.S.C. §§ 5531(d)(2)(A)-(B). This is not coincidental, of course, but merely reflects a political desire to neuter a potent consumer protection tool.

[78] 84 Fed. Reg. 4276, Feb. 14, 2019.

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III. CONCLUSION

The NPRM is a ham-handed critique of the 2017 Final Rule. The NPRM engages in specious and inconsistent critiques of the 2017 Final Rule, strangely misreads and mischaracterizes it repeatedly, and feigns ignorance of the massive body of unchallenged evidence supporting the 2017 Final Rule. All of this points to what is really going on. The Bureau's new political leadership does not like the 2017 Final Rule for political reasons. That is, of course, their right. But the Administrative Procedures Act demands more than an arbitrary political taste as a basis for reversing a rule, and the Bureau has adduced no such reasonable basis here. The Bureau should let the 2017 Final Rule stand unless it produces new evidence demands a reevaluation of the carefully considered positions of the 2017 Final Rule.

Sincerely,

Adam J. Levitin

Attachments:

(1) Expert Report of Professor Adam J. Levitin, *CFPB v. All American Check Cashing*, No. 16-cv-00356 (S.D. Miss.).

(2) Expert Report of Professor Adam J. Levitin, *Illinois v. CMK Investments, Inc.*, No. 14-C-2783 (N.D.Ill.).

(3) Nathalie Martin, *1,000% Interest—Good While Supplies Last*, 52 ARIZ. L. REV. 563 (2010).

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