BACKGROUND

A payday loan, known more formally in California as a deferred deposit transaction, is a short-term loan in which a borrower writes a post-dated, personal check to a lender for a specified amount, which is capped by law. The date on the check is the date on which the parties agree that the borrower will repay the loan. The lender advances the borrower the amount on the check, less a fee, which is also capped by law. The lender does not cash the check at the time the loan is made. Both parties are aware that the borrower lacks sufficient funds to cover the check when the check is written. The assumption underlying the loan is that the borrower will repay the loan by the agreed-upon date, either by depositing sufficient funds in his or her checking account to cover the check, or by paying the lender in cash on the loan's due date, and having the lender return the original check to the borrower, without cashing it.

California enacted its earliest version of a payday lending law in 1996, and gave jurisdiction over payday lenders to the Department of Justice (DOJ; SB 1959, Calderon, Chapter 682, Statutes of 1996). SB 898 (Perata, Chapter 777, Statutes of 2002), enacted the Deferred Deposit Transaction Law (CDDTL; payday loan law) and shifted the responsibility for administering payday lending from DOJ to the Department of Corporations (DOC; the Department).

Under the CDDTL, any lender who makes a payday loan must be licensed. Each licensee may defer the deposit of a customer's personal check for up to 31 days. The face amount of the check presented by a borrower may not exceed $300, and the fee charged by the licensee may not exceed 15% of the face amount of the check ($45 on a $300 check). Licensees may charge one non-sufficient funds fee, capped at $15, for checks that are returned by a customer's bank. Licensees may not directly or indirectly charge any additional fees in conjunction with a payday loan. Licensees may not enter into a payday loan with a customer who already has a payday loan outstanding and may not allow a customer to use one loan to pay off another. Licensees are also forbidden from accepting any collateral for a payday loan or making any payday loan contingent on the purchase of any goods of services. Each payday loan must be made pursuant to a written agreement. Licensees must post their fees and charges prominently at their business locations.

Costs for DOC to administer the payday loan law are borne by licensees. For fiscal year 2005-2006, licensees were each assessed $500 per location. DOC increased the assessment during the 2006-07 fiscal year to $941 per location.

Financial Code Section 23057 requires the Commissioner of Corporations (the Commissioner) to submit a report on December 1, 2007 regarding implementation of the payday loan law. The report must include, at a minimum, information regarding the demand for deferred deposit transactions, the growth and trends in the industry, common practices for conducting the business of deferred deposit transactions, the advertising practices of the industry, and any other information the Commissioner deems necessary to inform the Governor and the Legislature regarding potential legislation that may be necessary to protect Californians. Under the provisions of Section 23057, the Commissioner's recommendations for future action may include, but are not limited to, changes in the fees charged to consumers, specifications regarding the length of time for deferred deposit transactions, maximum amount provided to consumers, additional regulation of advertising practices, and the implementation of an installment loan product in lieu of a deferred deposit transaction.

INTRODUCTION

On March 10, 2008, the DOC released two reports to fulfill its requirements under Section 23057. The two reports are titled, "California Deferred Deposit Transaction Law, California Department of Corporations, December 2007" (referred to in the remainder of this paper as the DOC report) and "2007 Department of Corporations Payday Loan Study, December 2007, submitted to the California Department of Corporations by Applied Management Planning Group, in conjunction with Analytic Focus" (referred to in the remainder of this paper as the AMPG report).

On March 26, 2008, the California State Senate Committee on Banking, Finance & Insurance and Committee on Judiciary will hear from DOC and AMPG about both reports, and will solicit input on the reports' findings and recommendations from a variety of interested parties with wide-ranging views on the appropriate role and future of the payday lending industry in California.

SUMMARY OF REPORT FINDINGS

Generally speaking, the DOC report summarizes each of the elements required by Section 23057, and includes several recommendations for potential legislative action. The AMPG report, for which DOC contracted out, also covers each of the elements required by Section 23057, but focuses extensively on consumer demand for payday loans.

As might be expected, findings of the two studies are generally in agreement with one another, where both studies overlap in their coverage. Areas in which notable discrepancies were identified are discussed in the sections below. The discussion below combines the findings of the two reports into one summary document for ease of review by interested parties.

Details Regarding California's Payday Loan Industry

According to the most recently available information, California is home to 447 licensed payday lenders, which operate 2,403 licensed payday lending stores. A total of 338 licensees indicated to AMPG that they were actively making loans during the study period of April 15, 2006 through September 11, 2007.

Over two-thirds of all payday loans are made by only twelve licensees (AMPG). The largest 30 licensees made 82% of payday loans by dollar volume during 2006 (DOC).

Over 61% of all licensees operate only one payday loan location (AMPG).

Forty-nine of the state's 58 counties have at least one payday loan location. With 166 payday loan locations, the City of Los Angeles has the highest concentration of payday loan locations of any city in the state. The City of Sacramento is second, with 81 locations (AMPG).

Sixteen licensees (3.5%) reported making over 115,000 payday loans over the Internet during 2006 (DOC).

More than half (58%) of all licensees have been in business for less than five years. Fourteen percent of licensees have been in business for 11 years or more (AMPG).

The average length of a payday loan is 16 days (DOC).

Most payday lenders advertise using large, conspicuous signage on the outsides of their licensed locations (DOC). Many (70%) also advertise in local telephone directories; a smaller percentage advertise in local newspapers (29%) and Internet directories (27%; AMPG).

Before agreeing to lend to a borrower, most licensees require the borrower to provide identification, proof of some form of income, a home address, employer’s address, and checking account information. Licensees rarely conduct a credit check or verify whether the borrower has the ability to repay the loan, when their other debts and expenses are considered. Most payday loans can be obtained in under 15 minutes (DOC).

Most lenders accept any kind of verifiable income as proof of income, other than unemployment checks or reports of self-employment (AMPG). Payroll checks, government assistance checks, retirement checks, disability checks, annuity and/or structured settlement checks are the most common forms of income verification accepted. Although all payday loan customers are required to have and show proof of an active checking account, only 5% of licensees require that borrowers have the qualifying income deposited directly into their checking accounts (AMPG).

Most licensees require borrowers to complete an application for their first loan with that licensee. Future loans can be obtained without the need to complete another application, unless the applicant needs to update his or her information (DOC).

Cash is the most common method of distributing loan proceeds to borrowers, although the option of electronically depositing the funds into customers’ bank accounts is increasing in popularity among licensees (DOC).

Eighty four percent of licensees’ business is attributable to repeat customers (only sixteen percent comes from customers who take out only one loan). Nineteen percent of licensees’ business is attributable to customers who took out more than 15 loans during the 18-month period studied by AMPG.

Forty one percent of licensees offer some type of bonus (either cash or gifts) to customers who refer new business to the licensees. Cash is much more common than other types of gifts. Of those who offer cash bonuses, nearly one half offer $10 or less, and just under one third offer between $20 and $25 (AMPG).

Very few licensees accept personal checks for repayment (this despite the fact that a post-dated check is required in order to obtain a payday loan). Customers commonly pay off their loans in cash. Nearly all lenders who do accept personal checks for repayment charge non-sufficient funds (NSF) fees for returned checks (DOC and AMPG).

Fifty seven percent of licensees require customers to borrow at least $50. The majority of loans (63%) are between $200 and $255. Twenty lenders responded that the minimum amount they would lend was $255 (AMPG).

Although lenders may charge up to $45 in loan fees to lend the maximum amount of $300, 14% of lenders charge less than $45 on $300 loans. The smallest amount charged on a $300 loan was $25, corresponding to a maximum loan amount of $275 (AMPG).

Licensees reported making over $110 million in loans that were not repaid. Once loans have been in default for over 91 days, most lenders (72%) write the defaulted amount off as bad debt (AMPG).

Licensees charge off approximately 3% of their checks as bad debt (DOC). This finding contrasts with AMPG's finding that 12% of all loans outstanding in an average month are over 91 days delinquent and in default.

To prevent the loss of revenue due to defaulted loans, most lenders (87%) offer arrangements in which borrowers are allowed to pay back loans at a reduced rate or based on an agreed-upon schedule. Lenders reported that about 20% of loans issued during the eighteen-month study period required some type of workout arrangement (AMPG). However, less than 1% of all payday loan customers entered into formal, written payment plan arrangements during 2006 (DOC). In discussions with DOC to resolve this apparent discrepancy, staff learned that most loan workouts agreed to by licensees and borrowers are informal in nature, rather than formal, written payment plan agreements with scheduled payments due at specified times. Thus, the DOC and AMPG data are not in conflict. While nearly one-fifth of loans require some form of workout arrangement, only a very small number of these workouts are formalized repayment plans.

Details Regarding California's Payday Loan Consumers (Based on Data Provided by Lenders)

The aggregate dollar volume of payday loans has remained relatively constant during 2005 and 2006, at $2.5 billion (DOC). This dollar volume was spread across 9.8 million payday loan transactions in 2005 and 10 million payday loan transactions in 2006 (DOC).

There are approximately 1.1 million individual payday loan customers in California (AMPG). In sorting through data from 388 licensees for an eighteen month period from April 2006 through September 2007, AMPG found 1.0 million unique payday loan customers with identical first and last names and addresses. It identified 1.1 million individuals with identical last names and addresses. This slightly larger group reflects instances in which the same individual gave a slight variation of his or her name at different times. It also reflects instances in which two or more people with the same last name, living at the same address, obtained payday loans during the study period. It does not count instances in which the same individual payday loan borrower moved during the course of the eighteen month study period.

DOC reported the existence of 1.5 million individual payday loan customers during 2005 and 1.4 million individual payday loan customers during 2006. Reasons for the discrepancies between AMPG's and DOC's data appear to be due to the way in which the two organizations analyzed their data. When DOC surveyed each of its licensees, the Department compiled data from each of its licensees separately. Therefore, if the same individual had obtained a loan from two lenders during that year, DOC's survey would have counted that individual twice. AMPG would have counted that individual once, provided they reported the same first and last name and the same address.

AMPG identifies borrowers with identical first and last names and addresses as "individuals" and borrowers with identical last names and addresses but different first names as "families." According to AMPG, 73% of individual borrowers and 66% of families who borrowed during the last eighteen months had loans with only one payday lender. The remaining borrowers (27% of individuals and 33% of families) had accounts with two or more payday lenders. Among borrowers with accounts at multiple lenders, borrowers borrowed from 2.8 payday loan companies, on average.

Seventeen percent of payday loan customers received only one payday loan during 2006 (DOC). DOC also found that 57% of all payday loan customers received between two and five loans during 2006, 19% received between six and twelve loans, and 4% received between thirteen and eighteen loans during 2006. Customers who take out multiple loans in a year tend to do so in a consecutive fashion (with less than five days elapsing between paying the first one off and obtaining a second one).

Of those with more than one loan, the average borrower had 2.8 loans. The most loans taken out by an individual in the last eighteen months is 26. The most loans taken out by a family during the last eighteen months is 47 (AMPG).

Of those borrowers who obtained more than one payday loan in the last eighteen months, 28% used multiple locations of the same payday lender; 72% used multiple lenders (AMPG).

Slightly over 2% of payday loan customers during 2006 had more than one loan from different licensees at the same time. The majority of these customers (over 23,000 people) obtained two simultaneous payday loans, but over 1,500 customers obtained three simultaneous payday loans, and over 150 customers obtained four simultaneous payday loans (DOC).

Details Regarding California's Payday Loan Consumers (Based on Data Provided by Consumers)

As part of its scope of work, AMPG conducted a telephone survey of payday loan customers who had obtained at least one payday loan between April 15, 2006 and September 11, 2007. A total of 1,494 surveys were completed with payday loan customers throughout the state. Telephone interviews were conducted between November 17, 2007 and December 17, 2007.

AMPG believes that the following represents the best information available on the characteristics of payday loan borrowers: Approximately 60% of the payday lending population is female, and 40% is male. The ethnicity of borrowers is evenly distributed between Caucasians and Hispanics (both 36%), with significant numbers of Blacks (18%) and smaller numbers of Asians (3%). Half of all payday borrowers are between 25 and 44 years of age; 19% are between 45 and 54, 13% between 55 and 64, and 9% between 18 and 24.

Only 45% of the individuals who participated in the study admitted to having obtained at least one payday loan during the eighteen-month period studied, despite the fact that *all* of the individuals who participated in the study had obtained at least one payday loan during the study period. If a respondent indicated that they had not taken a payday loan during their telephone interview, they were not asked any further questions regarding their payday loan experiences. For this reason, the responses of a large number of surveyed individuals are missing from the payday loan experience questions.

In reviewing the demographics associated with the loan usage question, AMPG found that the higher a survey participant's income, the less likely he or she was to admit to having taken a payday loan. Younger respondents were less likely to admit having taken a payday loan than older participants. Hispanics were less likely to admit to having taken a payday loan, relative to Caucasians and Blacks. Because those who denied having obtained a payday loan were not asked any questions regarding their payday loan experiences, and because untruthful responses to the loan verification question were not evenly distributed by ethnicity and age, responses to the remaining payday lending questions are not proportionally distributed by ethnicity or age (i.e., they are skewed based on nonresponsiveness).

Among those who admitted to having obtained a payday loan:

51% used a single location for obtaining a loan.

The largest percentage of borrowers chose their payday lender simply by driving by and going in (24%). The next most common way of choosing a payday lender was "word of mouth/referral by a friend or relative" (22%). Although most payday lenders use the local telephone directory to advertise, only 5% of respondents reported finding their payday lender using a phone book.

Over 87% receive a regular paycheck (74% received a payroll check from a job, 11% received a government assistance check, 3% received a retirement check). An additional 5% are on disability, which AMPG did not count as government assistance.

Most (48%) are paid every other week or twice a month; 23% are paid once a month, and 13% are paid weekly.

Fifty percent said they usually took payday loans to pay other bills, 22% said they used the funds to cover household needs such as groceries, and 10% said they used the funds only in emergency situations. (These responses were "first mention" responses. When all mentions of the reasons behind obtaining payday loans were tabulated, the responses were very similar).

When asked what other options were considered as sources of financial assistance before the payday loan was taken, 37% said "no other option was considered." Twenty-eight percent considered borrowing money from family or friends, and 10% thought about waiting until their next payday. Despite the fact that all payday loan customers have checking accounts, only 4% of all respondents considered borrowing money from a bank as an alternative to obtaining a payday loan.

Borrowers were also asked whether the amounts they borrowed were what they needed. This question was phrased in two different ways. First, borrowers were asked whether the amount borrowed was the amount needed or the minimum/maximum required by the lender. When asked in this way, most borrowers (79%) said they borrowed the amount needed, and 19% said the lender required that they borrow at least that much (implying that they would have borrowed less if the lender had offered that option).

Second, borrowers were asked whether the amount borrowed was the amount needed or the most the lender would loan. When asked in this way, 63% of borrowers said they borrowed the amount needed; 32% said they would have borrowed more, but the lender wouldn't loan it; and only 3% said that the lender offered more than the borrower needed.

When asked where they obtained the rest of the money they needed if they could not obtain all they needed from the payday lender, 8% said they borrowed the money from family or friends, 8% said they did not get the rest of the money they needed, 5% waited until their next payday, 3% went to another payday lender, and less than 1% borrowed money from a bank.

Thirty-six percent of borrowers indicated they had used more than one payday lender. When asked why, 73% said they needed more money than one location would loan them at one time, 12% said they needed more money before the loan with the first company could be paid off, and 11% said they used one loan to pay off another.

Among those borrowers who indicated they had taken out more than one loan at a time, 47% said they had taken out two loans at one time, 35% said they had taken three or four loans at the same time, and one borrower said he/she had taken out 12 loans at once.

Borrowers generally understood the fees associated with payday loans, but did not understand how these fees translated into annual percentage rates.

Twenty-seven percent of respondents said they had decided, at least once, not to take a payday loan, because of fees or interest. Of that group, just under half (48%) sought out family and friends for the money, and a significant number waited until their next payday (38%).

About 15% of the respondents made arrangements to pay back payday loans on which they had become delinquent (Staff notes that this number is consistent with the survey of lenders, who indicated that approximately 20% of all loans required some sort of workout arrangement). Most of the survey respondents who made arrangements to pay off their delinquencies arranged to pay back what they owed over time. A smaller number of respondents paid back less than what was due.

RECOMMENDATIONS

AMPG

AMPG made two recommendations. First, there is an immediate need to establish a real-time information network that allows lenders to identify borrowers who have more than one account and/or more than one open loan at any given period.

Second, while noting that all lenders report they provide responsible borrowing information to their clients when loans are made, AMPG believes that additional efforts to inform borrowers of long-term borrowing costs may be needed to assist in preventing payday loan abuse and industry losses associated with unpaid loans.

DOC

DOC divided its recommendations into those intended to improve its oversight of the industry (twelve recommendations) and those intended to strengthen its enforcement of the payday loan law (ten recommendations). The Department also offered seven options for consideration by the Legislature. Each of the recommendations and options is summarized briefly below, along with its rationale. A comprehensive analysis of the recommendations and options is deferred to a subsequent policy committee analysis. Staff understands that DOC will be sponsoring legislation, SB 1551 (Correa), to enact some of its recommendations.

<u>Regulatory Oversight Recommendation Number 1: Clarify and confirm that licensees cannot refer delinquent payday loans to a local prosecutor for collection of returned checks.</u> Financial Code Section 23035 provides that a customer is not subject to criminal penalty for failure to comply with the terms of a payday loan agreement and requires licensees to disclose to customers that they cannot be prosecuted or threatened with prosecution to collect a payday loan. DOC's recommendation would help clarify that a licensee may not use the criminal process to collect a returned check in conjunction with a payday loan, even if the customer is not criminally prosecuted.

<u>Regulatory Oversight Recommendation Number 2: Enhance the Regulation of Electronic Transactions.</u> Clarify that the definition of a personal check includes the electronic equivalent of a personal check. This change would update the payday loan law to reflect the increasing use of automated clearing house transactions in lieu of paper checks.

Require a licensee to give a borrower the option of having the licensee deposit the customer's personal check or electronically debit the borrower's account for payment of the loan on the due date, if the licensee offers this service. This is intended to provide advance notice of this service to customers, to help them make an informed choice.

Allow a licensee to electronically debit the borrower's account one additional time for the full amount of the loan any time after the due date, without any further authorization from the borrower, if there were insufficient funds in the borrower's account when the account was first electronically debited for payment of the loan on the due date. Require any additional electronic debits from the borrower's account to be authorized in writing by the borrower. Require the borrower to acknowledge the dates and amounts of the additional electronic debts. These recommendations are intended to help protect customers from unanticipated debits by a payday lender, which could overdraw their accounts.

<u>Regulatory Oversight Recommendation Number 3: Improve Consumer Disclosures.</u> Require that the notice provided to borrowers prior to entering into a payday loan agreement be a separate, distinct document from the written agreement; require the licensee to have the borrower initial a copy of the notice to acknowledge receipt; and require the licensee to retain a copy of the notice with the borrower's initials acknowledging receipt in the file. These recommendations are intended to ensure that customers have an opportunity to review and understand the mandated notices and disclosures.

<u>Regulatory Oversight Recommendation Number 4: Require license applicants and existing licensees to notify DOC of other business that would be or is being conducted at the licensed location.</u> This will help coordinate oversight of businesses with other agencies and regulatory programs that may have jurisdiction over the other businesses (e.g., check cashing, which is overseen by the Department of Justice). This recommendation could also help detect whether consumers are receiving other products or services in a manner that violates the law.

<u>Regulatory Oversight Recommendation Number 5: Expand Consumer Protections for Deferred Deposit Transaction Business Conducted Over the Internet.</u> Ensure that all required notices and disclosures are provided to Internet borrowers, and that borrowers can download the agreement, notices, and disclosures. Alternately, if the borrower cannot download those documents, require the licensee to mail copies to the borrower within 24 hours. Require that the borrower agree to conduct the transaction over the Internet. Require the transaction to comply with the Uniform Electronic Transactions Act (Civil Code Section 1633.1 et seq.). These changes are intended to ensure that consumers obtaining payday loans over the Internet from California licensees are adequately protected.

<u>Regulatory Oversight Recommendation Number 6: Require that payment plans entered into between licensees and borrowers specify the payment dates and amounts of each payment, be in writing, and be signed by the borrower.</u> Further provide that this requirement shall not prohibit a licensee from accepting payments from a borrower after the due date of the loan, without a written payment plan signed by the borrower. This recommendation would help ensure that borrowers and lenders understand their rights and obligations in connection with payment plans. It would also help to alleviate misunderstandings that sometimes occur when payment plans are entered into verbally, whether in person or over the phone.

<u>Regulatory Oversight Recommendation Number 7: Require a written agreement signed by the borrower in order to extend the due date of a loan.</u> Provide the licensee with an option to notify the borrower by mail of the approval to extend the due date of the loan, if the borrower elects not

to sign the extension agreement. Like the recommendation above, this recommendation would help avoid misunderstandings between lenders and borrowers over repayment plan terms.

<u>Regulatory Oversight Recommendation Number 8: Require licensees to prominently disclose that borrowers have the right to request a written extension agreement and payment plan</u>. This is intended to help borrowers understand that both options are available to them.

<u>Regulatory Oversight Recommendation Number 9: Apply existing Financial Code Section 23027, governing advertising of payday loans, to advertising on the Internet, and require licensees to keep copies of their advertising for at least two years</u>. These changes would help protect consumers from false advertising on the Internet and ensure the availability of advertising records for audit purposes.

<u>Regulatory Oversight Recommendation Number 10: Require that specific language be used in payday loan advertising to disclose one's licensure by the Department of Corporations, and require that all advertising disclosures be in the same language as the advertising itself.</u> These changes are intended to help consumers more quickly identify DOC as the appropriate regulatory agency for payday lenders. They are also intended to stop the practice of advertising payday loans in a foreign language but including required consumer disclosures in those advertisements in English.

<u>Regulatory Oversight Recommendation Number 11: Require (rather than authorize) the use of a specific chart to compare payday loan fees and related cost information.</u> Existing law requires licensees to post a schedule of all charges and fees, as specified, and provides an example of one way in which the information may be presented. This recommendation would require licensees to use the sample chart provided in law, to help ensure that consumers have the information needed to make an informed choice.

<u>Regulatory Oversight Recommendation Number 12: Increase DOC's ability to scrutinize license applicants and those in charge of payday loan locations.</u> Require license applicants to list each person in charge of a payday lending location, and require that person to submit fingerprint information and a historical profile through a Statement of Identify and Questionnaire (SIQ). Require the licensee to notify DOC within ten days of a change in the person responsible for the location, and to submit new fingerprint information and an SIQ for that person. Require each licensee to notify DOC at least 60 days prior to a change of its officers, directors, or any other persons named in the application. This notification must include the effective date of the change, the names of all persons involved in the change, and must include fingerprint information and an SIQ for each successor person involved in the change. Require license applicants and all persons named in license application to disclose whether they have conducted or are conducting deferred deposit transaction business in any other state, and whether they have violated similar regulatory schemes in that other state/those other states, both in the past and on an ongoing basis. These recommendations are intended to help DOC detect unscrupulous operators and bar them on an ongoing basis.

Stronger Enforcement Recommendation Number 1: Confirm DOC's jurisdictional nexus over payday lending activities by stating that a payday lender is subject to the CDDTL when it conducts deferred deposit transaction business "in this state." This recommendation is intended to allow DOC to enforce the law against those who originate payday lending business in California and who direct it to California, under specified circumstances.

Stronger Enforcement Recommendation Number 2: Expand the grounds for barring, suspending, or censuring persons managing or controlling payday lenders, and for denying, suspending, or revoking licenses. Authorize DOC to bar, suspend, or censure persons and to deny, suspend, or revoke licenses on the following grounds: 1) committing specified administrative, civil, and criminal acts involving theft, embezzlement, fraud, conversion or misappropriation of property, forgery, bookmaking, receiving stolen property, counterfeiting, extortion, improprieties involving checks or credit cards, or computer violations; 2) violating rules or orders of the Department or other regulatory schemes; 3) providing false statements in records provided to the Department; 4) failing to supervise others in preventing violations of the law; or 5) being the subject of court or regulatory orders enjoining further payday business. Further clarify that surrendering a license does not affect the licensee's administrative liability or its civil or criminal liability. These recommendations are intended to help DOC protect consumers from unscrupulous persons with a track record of unlawful activity.

Stronger Enforcement Recommendation Number 3: Protect consumers through administrative orders. Allow DOC to issue administrative orders to prevent unsafe and injurious practices, and make these orders effective within 30 days, if no hearing is requested by the person(s) accused. Allow DOC to suspend or revoke a license for failing to maintain a surety bond, as required by law, through more expedient administrative orders. Allow the Department to assess a penalty of $500 (rather than pursue civil action, as is currently required) when a licensee fails to provide notice of any change in business location. These changes will help prevent and deter certain violations of law in a more efficient manner than is allowed by current law.

Stronger Enforcement Recommendation Number 4: Increase and add enforcement penalties. Increase the civil penalty for violating the payday loan law from $2,500 to $10,000 per violation. Allow administrative penalties of up to $2,500 per violation to be levied and collected through specified administrative hearing procedures. Allow the Commissioner to collect costs, including reasonable attorney's fees and related expenses, in connection with administrative or civil actions. Increase the penalty for failure of a licensee to pay the annual licensing assessment from 1% of the assessment for each month payment is withheld to at least 10%.

Stronger Enforcement Recommendation Number 5: Require the preparation and retention of accurate records and reports by licensees. Require deferred deposit transaction records to be kept for six years (rather than two years, which makes it difficult to pursue civil or criminal cases). Require licensees to keep and use complete sets of books, records, and accounts of transaction, in accordance with good accounting practice. Provide that failure to keep these records of account is prima facie evidence of unlawful activity. Require each payday lender's annual report to be verified or certified by the licensee or an authorized representative, under penalty of perjury.

Stronger Enforcement Recommendation Number 6: Compel the production of books and records by licensees. Authorize the Commissioner to subpoena all books and records of payday lenders. Under existing law, the Commissioner may only require the production of books, records, and supporting data used by a licensee to prepare reports to the Commissioner. Clarify that the requirement of licensees to produce records within ten days after written demand is not in conflict with the section of law that requires free access to the Department pursuant to an exam, nor in conflict with the section of law that allows the Department to examine records at any reasonable time. These recommendations will clarify DOC's authority to compel production of books and records from licensees at any time.

Stronger Enforcement Recommendation Number 7: In specified civil actions, allow DOC to appoint a receiver or conservator to manage a payday lender's assets, require a licensee to take remedial action, and/or require a licensee to provide an accounting or audit of specified financial reports. These recommendations are intended to help prevent any further harm to consumers in certain civil cases.

Stronger Enforcement Recommendation Number 8: Allow DOC to seek a court order to enforce any administrative decision awarding restitution, administrative penalties other than citations, and cost recovery, without having to file a civil suit and motion for summary judgment. This recommendation is intended to help DOC expedite relief to consumers.

Stronger Enforcement Recommendation Number 9: Change the citation process. Provide that a citation is deemed final if the cited licensee fails to request a hearing within 30 days of receiving the citation. Allow DOC to issue a citation to assess an administrative penalty, not to exceed $2,500 per violation (rather than $2,500 per citation). These recommendations are intended to strengthen DOC's enforcement authority.

Stronger Enforcement Recommendation Number 10: Streamline DOC's ability to void loans and order fees forfeited. Clarify that DOC has the authority to order the voiding of loans and the forfeiture of fees by administrative order, rather than by pursuing a civil suit. Conform references to fees and charges in the law to provide uniformity and minimize confusion.

Other Options Offered by DOC Regarding Payday Loan Transactions

In its report, DOC asserts the importance of offering lower-cost alternatives to payday loan products. The Department offers seven options for consideration by the Legislature. All seven options are based on the premise that payday loans will continue to be available to help Californians meet short-term emergency cash needs, but that longer-term installment products will be available for those consumers unable to pay back the full amount of their payday loans on their due dates.

Option Number 1: Change the payday loan origination fee from a percentage of the face value of the check to a flat fee. Consider reducing costs if the loan remains outstanding for a full month rather than for two weeks.

Option Number 2: Increase the maximum amount of a payday loan from $300 to another amount, such as $500 or $750. California's maximum loan amount is less than that of most other states, most of which have loan limits of $500 or more. Amend the law to add the fee on top of the face amount of the check (rather than the current practice of subtracting the fee from the face amount of the check).

Option Number 3: Adjust fees based on the loan amount, with a sliding scale that reduces the fee as the amount borrowed goes up. For example, allow a maximum fee of $12 for each $100 up to $300, and a maximum fee of $10 for each $100 borrowed up to the maximum allowed. This approach will enable lenders to recover more fees for taking on higher risk, and will reduce costs (relative to existing law) for consumers who require a higher loan amount.

Option Number 4: Prohibit a licensee from entering into a deferred deposit transaction with a customer during the period of time that the customer has an outstanding deferred deposit transaction with another licensee. Financial Code Section 23036 states in part that, "A licensee shall not enter into an agreement for a deferred deposit transaction with a customer during the period of time that an earlier written agreement for a deferred deposit transaction for the same customer is in effect." DOC's option would extend this prohibition to multiple simultaneous loans, regardless of whether they are issued by the same licensee or multiple licensees.

Option Number 5: Restrict a customer from having a payday loan outstanding with any payday lender for more than three months during a twelve-month period. This option would prevent borrowers from using payday loans as a long-term source of credit and is consistent with guidance issued to depository institutions by the Federal Deposit Insurance Corporation (FDIC) in 2005. In its guidance, the FDIC noted that when payday loans are used for a long period of time, the fees charged can rapidly exceed the amount borrowed, which can create a serious financial hardship for the borrower.

Option Number 6: Require licensees to offer a payment plan with a minimum of six equal, monthly installment payments to all borrowers who have had continuous (consecutive) loans for three months, and prohibit licensees from charging customers any additional fees or interest in connection with the payment plan. This option is intended to help financially strapped borrowers avoid additional interest or charges. Staff notes, however, that charging additional fees or interest in connection with repayment plans is already illegal under the payday loan law.

Option Number 7: Require all licensees to use a uniform database to record all transactions in real time. Allow for the cost of the system to be paid directly by the licensee to a third party database manager. Using a single database to track payday loan transactions would allow DOC to clearly identify the number individual payday loan customers, enforce prohibitions against multiple loans and loan rollovers, and enforce rules regarding loan terms and charges. Seven other states reportedly have databases similar to the one envisioned by DOC. Staff notes that this option is consistent with one of AMPG's two recommendations.