Which Shall It Be, A Hamburger Or A Loan

by Steve Brown

We've seen the reports highlighting that there are more payday and auto title loan stores in the U.S. than all the McDonald's and Burger Kings combined. This is not a new revelation, as this ratio was achieved in 1996. Today, following the ugly recession and slow recovery, the number of people resorting to finding a loan outside the traditional banking system has increased. To regulators in particular, payday lending is an odd business model which appears to have the central objective of lending to people who need short term cash but then most likely won't be able keep up with the payments or pay it back on time. Every step of the way the borrower pays fees--late fees, renewal fees and interest rates can reach 300%.

It's not the same everywhere in the U.S. though, and in fact, 11 states have outlawed such practices or have strict usury laws limiting interest rates. This approach has mostly driven such operators out of those states. Further, according to research by California State University at Northridge, there are vast differences in per capita penetration by payday lenders among the states that still allow it. For example, NM tops the list at almost 42 per 100,000 in population; closely followed by MS, SD and AL.

We note the data was pre-2010, so we contacted the researcher hoping for an update. He said that a number of states had made efforts to regulate specific areas of this kind of lending but as a result, the payday lenders were calling themselves by other names, such as "Auto Title" or "Installment Lenders." This evolving language has made policing even the most egregious predatory lenders seem like playing whack-a-mole. Plus, it makes gathering accurate data difficult.

Today, the CFPB has federal authority to oversee all consumer lenders and set nationwide standards of behavior, so this is changing. As the cleanup begins, the CFPB has released a report that non-banks are exhibiting "systemic flaws in their compliance management systems," especially in dealing with collection and resolving consumer disputes. In addition, the CFPB reported that they have forced more than $70mm to be returned to consumers in recent months.

The findings of the CFPB around payday lenders found many had illegally threatened lawsuits, harassed borrowers by phone at work and hired third parties to carry out similar illegal collection tactics. Debt collectors were also using similar practices and calling people as frequently as 10x a day.

Finally, CFPB analysis found a number of firms to not have an adequate regulatory compliance program. One firm was even found to not have any company-wide compliance oversight at all. For those of us who drive by the brightly colored store-fronts with blinking neon signs advertising check cashing and "free" loans, it's a bit of a stretch to imagine a meeting of the compliance committee in the back room. But, somewhere between the Wild West and the highly regulated banking industry there must be some rules, so we are glad the CFPB is looking into enforcing what laws there are and hopefully increasing oversight.

As bankers, we understand the balance between regulation and just doing business. It is part of the fabric of our industry, so we welcome more oversight on the predatory practices of these so-called "lenders." They give everyone a bad name and undermine the positive things real banks provide customers.

BANK NEWS

M&A

American National Bank and Trust Co. ($1.3B, VA) will acquire Franklin Community Bank ($166mm, VA) for $24.2mm in cash and stock or about 0.97x book.

M&A

Stonegate Bank ($1.7B, FL) will acquire Community Bank of Broward ($493mm, FL) for $61.2mm in stock.

Duty of Care

Regulators expect bank directors and management under the duty of care standard to diligently and honestly administer the bank's affairs in a manger measured against what a reasonable and prudent person would do in similar circumstances.

Duty of Loyalty

Regulators expect bank directors and management under the duty of loyalty standard to place the corporate interests of the bank above personal interests, act in the best interests of the bank, ensure insiders don't abuse their positions by benefitting personally at the bank's expense, avoid conflicts of interest and the appearance of conflicts of interest.

Conflicts of Interest

Regulators indicate conflicts of interest can exist if a director or officer of a bank has a significant interest outside the bank that reasonably affects his or her judgment with respect to the bank's business.

Fiduciary Duty

Regulators expect bank directors and officers to act in the best interest of the bank, avoid any conflicts of interest between themselves and the bank or its clients.

Biz Owners

A Financial Planning Association survey finds the biggest issues small business owners say they have to deal with related to an exit strategy are finding a buyer (31%), valuing the business (23%), emotional toll (21%), determining what to do next (13%) and figuring out retirement (8%).

Risk Examination

Bank regulators indicate they are focusing more efforts now on banks with significant concentrations in longer term assets or liability structures that make them vulnerable to rising interest rates.

Flexible Biz

Aite Group finds 71% of small businesses say they primarily interact with their banks using online channels, smartphones or tablets.