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Middle Class Prosperity Project

Forum on

"Access and Opportunity: Predatory Financial Practices and Economic Injustice"

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Good afternoon Congressman Cummings and Senator Warren. On behalf of the Center for Responsible Lending, thank you for launching the Middle Class Prosperity Project as a platform to engage the public in a much-needed conversation about the challenges facing middle-class Americans and those who aspire to become part of their ranks.

The issues raised in today's forum are especially timely. With 8 out of 10 net-new households in the United States being created by people of color,[1] the lack of economic opportunity and mainstream financial services in urban areas and communities of color—when combined with the costly and sometimes predatory impact of allowing alternative financial service providers to fill that void—represent serious threats to the future of America's middle class and our nation's long-term prosperity. I applaud you for highlighting these issues today. Thank you for allowing me to share CRL's insights.

I am the Vice President of Government Affairs and Senior Counsel at the Center for Responsible Lending (CRL). CRL is a nonprofit, non-partisan research and policy organization dedicated to eliminating abusive financial practices, while protecting family and community wealth. CRL is also an affiliate of Self-Help, a nonprofit community development financial institution that operates two credit unions with 30 bank branches in North Carolina, Illinois, and California. In thirty years, Self-Help has provided more than $6 billion in financing to 70,000 homebuyers, small businesses, and nonprofits, while creating financial access and wealth-building opportunities for more than 80,000 low- and moderate-income, minority, rural, and women-headed families. Self-Help's success only reinforces CRL's confidence in the fact that a financial institution that chooses to meet the needs of traditionally underserved communities, without employing predatory practices, creates significant profits for the communities that it serves and the institution itself.

Multiple reports show that large disparities exist in the availability of mainstream financial services in traditionally underserved neighborhoods. In the years leading up to the financial crisis, traditional institutions added more than 10,000 full-service banking branches. [2] Yet, only 1 in 10 of those branches were opened in inner-city, minority neighborhoods.[3] Matters have only become worse in the aftermath of the crisis. An analysis by Bloomberg showed that—of the more than 1,800 bank branches that closed their doors in the U.S. between 2008 and 2013—93 percent were located in these already underserved communities.[4] During that same time, the total number of bank branches in more affluent neighborhoods continued to grow, producing a net increase in financial accessibility for wealthier and whiter communities.[5]

There is an urgent need to address the absence of mainstream financial institutions in underserved communities. And the tragic events in Baltimore over the past few weeks only highlight the consequences of our failure to do so. West Baltimore residents made it clear to anyone who chose to listen that their rallies and protests went beyond the issue of police brutality and the death of Freddie Gray. Twenty-five-year-old resident Brendon Joyner-El, one of the many peaceful protesters, perhaps explained it best when he said:

"this is happening because of years and years of socio-economic disparity."[6]

Research supports Mr. Joyner-El's conclusion. A recently released study by economists at Harvard University found that low-income children growing up in Baltimore faced slimmer chances for economic mobility than any other group of children living in the 100 largest counties in the United States.[7] A report by John Hopkins University found that West Baltimore teenagers had a bleaker economic outlook than 15 – 19 year olds living in economically distressed cities in Nigeria, India, China, and South Africa.[8] The city of Baltimore has one of the largest wealth gaps in the United States, with Baltimore residents in the bottom fifth income profile typically earning $13,588, while those in top 5 percent made an average of $166,924 the same year.[9] And in the heyday of predatory mortgage lending, the Justice Department found that the nation's largest mortgage lender targeted 4,500 homeowners in the Baltimore and Washington, D.C., region for discriminatory lending practices that involved intentionally giving people of color subprime mortgages, even though many of those borrowers qualified for a prime loan.[10] Research by the Center for Responsible Lending showed that mortgage racial disparities existed even when controlling for credit scores of 660 and above.[11]

There are no bank branches in the zip code where the CVS convenience store and ACE Cash Express check-cashing shop were recently looted in Baltimore.[12] And mapping analysis by the National Community Reinvestment Coalition shows that a mere handful of locations exist in neighboring communities.

This absence and continuing decline in numbers for traditional financial institutions located in underserved communities limits access to basic financial services for American citizens and forces them to pay steep fees for routine activities like cashing checks and paying bills. The results are quite costly.

In one year, the average underserved household spent approximately $2,412 just on interest and fees for alternative financial services.[13] In contrast, monthly checking account fees at the nation's 10 largest banks averaged out at $8.76 during the same timeframe—meaning individuals with access to mainstream institutions paid just $105.12 that year for many of the same financial services.[14] 39 percent of banked individuals paid no monthly fees at all.[15]

I recently testified before the House Financial Services Committee on the need to regulate alternative financial service providers at the federal level—especially payday lenders, indirect automotive lenders, and non-depository mortgage operations.[16] Members of Congress who opposed or questioned these ideas suggested that our position would strip single mothers, people of color, and working class communities of the "right to choose". One member of Congress even suggested that regulating payday lenders was the equivalent of telling people that they should not have the right to eat sugar.[17]

But the truth is this. Financial exploitation is rarely the byproduct of choice. Instead, financial exploitation is often driven by a state of necessity that only occurs when legitimate alternatives seem to be out of reach. Ask yourself this. What would honestly happen if we asked any American if they would choose to pay 390% interest on a $500 loan if they knew that they could also legitimately choose to pay less than 36% interest for the same loan? What would happen if we asked the residents of West Baltimore if they would choose to pay 23 times the cost that other people pay for conducting the same basic financial activities? I'm fairly confident that, in each case, most—if not all—of them would say "no."

Thankfully, the state of Maryland has recognized the nature of predatory payday lending and has chosen to ban its availability. Maryland law utilizes the most effective payday loan regulations, a small dollar loan cap of 2.7% per month and 33% per year. This keeps the payday borrowing rate in Maryland at 3%, a number that includes all payday lending – from storefront to online borrowers. It's important to note that, in Maryland, payday lending and check cashing are not the same thing. This terminology has confused advocates in the state before and created problems in gauging the true dangers of alternative financial service providers.

Maryland, like other non-authorization states, is very interested in the Consumer Financial Protection Bureau's rulemaking process on payday lending. The rules that are currently being considered include a glaring loophole to the proposed ability to repay standard. That loophole would allow up to six loans to be extended without consideration of the consumer's ability to repay. If enacted, this particular exemption could signal to state legislatures that the federal government endorses the unaffordable extension of credit and undermine the strong protections that the state of Maryland already has in place. A strong CFPB rule, one without exceptions or loopholes, is as essential in Maryland as it is in Mississippi—where high-cost payday lending is permitted—and the rest of the United States of America.

Likewise, it is important to note that the impact of declining mainstream financial access in inner cities doesn't just affect residents. It also affects the businesses that operate in these communities, a number of which are also minority owned. Without locally based banks, small businesses are not likely to receive the necessary capital to grow because commercial lending is, without question, a local matter. When deciding to make loans, financial institutions without a community presence struggle to understand the realities and opportunities of the neighborhoods in which these businesses are based. That lack of familiarity diminishes business expansion, jobs, and—ultimately—the city's tax base.

In addition to the challenges wrought by the absence of mainstream financial institutions in urban America and communities of color, it is important to note that other aspects of the mainstream financial services industry present troubling concerns in their treatment of communities of color and low- and moderate income individuals.

For example, this year, the Maryland legislature passed a “yo-yo sales” bill. Yo-yo sales are a “bait and switch” financial scam in which consumers unwittingly sign a conditional sales contract to purchase a car. The contract says the deal is complete, except for financing. The car dealer conveys that the car is the consumer’s by insisting that she or he put insurance on the car before driving it off the lot and by issuing temporary tags and registration. Days or even weeks later, the car dealer will call the consumer back and state that the financing fell through and demand the consumer sign a longer contract, make a bigger down payment, or pay a higher interest rate to keep the car. Often the consumer’s trade-in has already been sold off, so they are stuck paying more than they intended.

When the state of Maryland passed this bill, they rolled back 30 years of consumer protections on car sales. And while they included some consumer protections, the protections aren’t enough to help families who lose their cars to these scams. From 2008 – 2012 alone, Maryland families lost $240,000 to illegal yo-yo sales. Now, the legislature has endorsed this practice.

- Yo-yo sale disproportionately affect low-income people and people with low credit scores. Marceline White, of the Moving Maryland Forward Network, testified to this in February in front of the Judicial Proceedings Committee when she said, “the likelihood of being a victim of a yo-yo scam is strongly correlated to a consumer’s level of income;

- A Center for Responsible Lending study found that 12% of car-buyers with incomes below $40,000 experienced a yo-yo scam ,while 25% of consumers with incomes below $25,000 had been victims of a yo-yo scam.

- The Maryland Consumer Rights Coalition’s research found that 62% of complaints to the Attorney General’s office were from women, and 26% of all complaints were from car buyers in Baltimore City.

For low-income consumers, a car is often their one link to job opportunity, a way to ensure children get to school on time, and essential for work attendance. After all, Baltimore's public transportation system is notoriously unreliable. Since the protests began, a number of pieces have been written about the state of Baltimore's public transportation – including how late or overcrowded buses lead to missed school, missed job interviews, and lost wages. It isn't hard to see the link between access to transportation and access to wealth, and how the yo-yo sales bill threatens that nexus.[18]

For-profit colleges have also exploded onto the national consciousness in the last several years, due to widespread allegations of fraud and abuse within open-admission schools. These private post-secondary programs, which often offer career or technical degrees and certificates, are on average 2-6 times more expensive than traditional schools, depending on the program.

There are about 29,677 students enrolled in 314 for-profit post-secondary for-profit programs in Maryland. These students are disproportionately female and African American. According to research by MCRC, 63% of African American students in the state are enrolled in for-profit programs. Many students at for-profits do not receive the education they need and in many cases, do not complete the program, leaving them with significant debt and limited job prospects. For example, while just about 10% of federal student loan borrowers attend for-profit schools, they account for 44% of loan defaults.

The Maryland legislature made the situation worse this year by passing a bill authorizing the state to join SARA, a scheme that allows out-of-state, online only, for profit schools to operate without any approval from state regulators. SARAs also remove the authority of the state's education regulatory to review and sanction for-profit programs that take advantage of Maryland students.

Conclusion

68 million people living in America are underserved by mainstream financial institutions.[19] Many of them are either young (under the age of 25), come from African-American, Latino and lower-income households, or live in inner cities.[20] The reality is that these Americans represent the fastest growing demographics in our nation.

We ignore the consequences of their exclusion from the mainstream financial market to our own detriment. Our nation's economy needs and depends upon a strong middle class. In the future, the U.S. will fall short of that goal if it continues to overlook the economic reality of so many of our citizens by failing to take the necessary steps to encourage mainstream financial access and limit the costly and often predatory nature of alternative financial services.

I look forward to working with each of you to accomplish these objectives and, in the process, ensure that all Americans truly have access to economic opportunity. Thank you for allowing me to share CRL's insights today. I look forward to answering your questions.

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[2] CBS News, Bank Branches Boom, But Not for Minorities, August 17, 2009, available at http://www.cbsnews.com/news/bank-branches-boom-but-not-for-minorities/

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[5] Id.

[6] Howard Koplowitz, Baltimore Riots 2015: City Residents' Struggle Under Poverty, Income Inequality and Mass Incarceration Predates Freddie Gray Unrest, International Business Times, April 28 2015, available at http://www.ibtimes.com/baltimore-riots-2015-city-residents-struggle-under-poverty-income-inequality-mass-1899732.

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[14] The $2,412 figure is drawn from 2012 data. To determine a comparison cost for financial services for banked individuals, CRL relied upon 2012 monthly checking account fee data from the 10 largest institutions provided by ABC News. ENJOLI FRANCIS, Basic Checking Account Fees At 10 Largest Banks, ABC News, September 24, 2012 available at http://abcnews.go.com/blogs/business/2012/09/basic-checking-account-fees-at-10-largest-banks/.
[15] Id.
[16] House Financial Services Committee, "Hearing entitled 'Examining Regulatory Burdens on Non-Depository Financial Institutions'", available at http://financialservices.house.gov/calendar/eventsingle.aspx?EventID=398862.
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[18] http://wypr.org/post/no-yellow-buses-here-one-students-mta-commute?nopop=1
[19] Federal Deposit Insurance Corp. (FDIC), 2011 FDIC National Survey of Unbanked and Underbanked Households, September 2012, http://www.fdic.gov/householdsurvey/2012_unbankedreport.pdf, pp. 4-10.
[20] FDIC, 2011 FDIC National Survey of Unbanked and Underbanked Households, p.15.