

MINUTES OF THE HOUSE FINANCIAL INSTITUTIONS COMMITTEE

The meeting was called to order by Chairman Ray Cox at 3:30 P.M. on February 7, 2005 in Room 527-S of the Capitol.

All members were present except:

Oletha Faust-Goudeau- excused

Mario Goico- excused

Committee staff present:

Melissa Calderwood, Kansas Legislative Research Department

Michele Alishahi, Kansas Legislative Research Department

Bruce Kinzie, Revisor of Statutes Office

Patti Magathan, Committee Secretary

Conferees appearing before the committee:

Kevin Glendening, State Banking Commission

Tim Hagan, Consumer Credit Counseling

Ron Gaches, Kansas Association of Financial Services

Doug Wareham, Kansas Bankers Association

Brad Smoot, Representing Loan Max

Rod Aycox, Loan Max

Ms. Amy Parker, Loan Max Customer

Ms. Lisa Ross, Loan Max Customer

Ms. Jo Tiffany, Loan Max Customer

Bill Sneed, Midwest Title Loans

Others attending:

See attached list.

Representative Cox announced that there would be a presentation on Uniform Consumer Credit Code (U.C.C.C.). He also advised conferees that testimony would be limited to seven minutes due to the number of people who would be testifying today.

Melissa Calderwood, Legislative Research Staff, testified that the U.C.C.C. was enacted in 1973 and applies to all aspects of consumer credit transactions related to personal, family and household purposes. Generally these transactions are less than \$25,000. The U.C.C.C. is administered by the Deputy Commissioner of Consumer Mortgage and Lending who is part of the Office of the State Bank Commissioner. U.C.C.C. was amended by the legislature in 1980, 1988, 1994, and again in 1999.

The U.C.C.C. establishes three categories of interest rates: closed end or installment rates, open end or revolving credit rates, and lender rates. Under current law a seller may set a finance charge at "any rate agreed to by the parties" subject to the statutory limits of prepaid finance charges, which vary by loan category.

Two proposed house bills, **HB -2143 Consumer credit code, finance charges, and HB - 2145 Consumer credit code, regulations, penalties**, attempt to amend the current code. **(Attachment 1)**

Chairman Cox opened Hearings on: **HB -2143 Consumer credit code, finance charges.**

Proponent **Kevin Glendening**, of the State Banking Commissioner's Office, stated that **HB 2143** would reinstate an interest rate ceiling on certain consumer credit transactions which was removed in the late nineteen nineties. Mr. Glendening explained that core to the purpose of U.C.C.C. is the premise that a consumer is at a disadvantage in terms of knowledge and understanding of financial matters and credit practices in contrast to the more sophisticated knowledge of the lender. The U.C.C.C. seeks to ensure certain protections for the consumer using a variety of forms including consumer rights, lender responsibilities, and maximum interest rate ceilings.

Lack of an interest rate ceiling is inconsistent with existing ceilings now in place for closed-end credit and real estate secured consumer loans. In addition, lack of an interest rate ceiling on open-end credit or credit

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sales has created a gaping hole in the safety net for Kansas consumers and has potentially adverse implications for both individuals and the Kansas economy. Mr. Glendening told the Committee that a Georgia-based company has established a number of locations in Kansas making “title loans” at interest rates of 360 percent or more, secured by a lien on an individual’s vehicle. The debt is structured as a revolving loan to take advantage of the present lack of an interest rate cap. Mr. Glendening stated that his position is that these loans cannot be justified just because some consumers accept them, nor does he ascribe to the theory that high risk and high loss to the lender justify the higher interest rates. His goal is to strike a balance between the needs of credit providers, while ensuring reasonable protection for Kansas consumers. **(Attachment 2)**

Proponent **Tim Hagan**, Director of Education for the Wichita office of the Consumer Credit Counseling Service told the Committee that his nonprofit agency provides personal financial-management education and counseling services from offices in Wichita, Salina, Hutchinson, Garden City, and Hays. Their programs attempt to increase financial literacy and help Kansas consumers avoid bankruptcy. They counseled more than 10,000 Kansans last year who shared a common denominator which is “lack of financial literacy.” **HB 2143** affords an opportunity to protect Kansas consumers.

Mr. Hagan provided a copy of one customer statement which illustrates Annual Percentage Rate (A.P.R.) of 360 percent and outlined a 12-month payback on a loan of \$1000 in which interest alone totaled more than \$2750. That same \$1000 loan could be paid back over 12 months at 264 APR with interest only totaling \$1900.

Mr. Hagan concluded that a better alternative could be to sell the vehicle and retain excess cash, instead of using it for loan collateral and risking loss of the entire vehicle value if repossession occurs. He also indicated that at times, for some people, bankruptcy is also a better alternative. **(Attachment 3)**

Chairman Cox announced that there was written testimony proved by **Melissa Lewis** of El Centro Inc., a proponent **(Attachment 4)**, then opened the floor to questions for proponents.

Representative George stated that Mr. Glendening had mentioned that LoanMax is applying for 44 repossessions each month. He asked Mr. Glendening if he could provide the total number of loan requests in order to compute the percentage. Mr. Glendening estimates that 44 applications for repossession is approximately 10 percent of total title applications.

Representative Brown asked Mr. Glendening how the repossession rate compares to other lenders. Mr. Glendening believes that they are higher than a typical lender.

Representative Vickery quoted the written testimony of El Centro and questioned whether some lenders are actually charging higher rates than LoanMax. Mr. Glendening stated that he has seen reference to rates as high as seven hundred percent.

Representative O’Malley asked Mr. Hagan what his response is to people who say that LoanMax and similar credit companies offer an opportunity to people who cannot obtain credit from traditional lenders. Mr. Hagan stated that indeed these people were in “dire straits” and offered that, since these loans are secured by the vehicle title, if the borrower needs one-half of the vehicle value, a better alternative would be to sell the car. One-half of the proceeds would be used to satisfy debt and the borrower could retain one-half the value of the car to provide for transportation costs, thereby avoiding the high interest rates.

Representative O’Malley asked if data is available to reflect percentage of loans that linger. Mr. Glendening replied that roll-over financing has become a common element.

Representative Brunk asked Mr. Hagan if his statement that no one would choose this type of loan was an interest rate issue or a disclosure issue? Mr Hagan replied that it was an impact issue. Loan terms have been disclosed but it’s an understanding issue since the consumer doesn’t understand what the terms will mean to them. Loans are secured by fifty percent of vehicle wholesale value.

Representative O’Malley questioned why the U.C.C.C. open-end credit wording was changed in 1999. Mr.

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Glendening stated that the changes were made to allow Kansas loan providers to compete with out-of-state providers who did not have interest-rate caps.

Chairman Cox announced that we would now hear testimony from the opponents.

Opponent **Ron Gaches** spoke as a representative of Kansas Association of Financial Services (K.A.F.S.). Deregulation of interest rates has allowed consumer finance and mortgage companies the ability to provide more accurate risk pricing, allowing consumers with outstanding credit histories to benefit from lower interest rates and allowing consumers who previously were denied credit viable options in the marketplace.

The K.A.F.S. lenders provide financing for a wide range of credit transactions in a regulated environment run by the Kansas Banking Commissioner's Office. Violations of the Kansas U.C.C.C. and regulations can result in civil penalties of up to \$5,000 per violation, cease and desist orders, negotiated settlements, and revocation of the lender's license. The division of Consumer and Mortgage Lending has the authority to ensure that companies are good operators and it regularly exercises that authority.

The Kansas legislature made the decision in 1999 to remove the cap on interest rates as part of a comprehensive updating of the U.C.C.C. Since that time the Kansas consumer market has grown significantly and consumers who previously did not have credit available now do. Reinstating the interest rate cap would fall most heavily on those who are least able to secure credit in the traditional bank and credit union markets. Just because individuals have a credit record that traditional banks view as undesirable or don't have a bank account doesn't mean the State of Kansas should prevent them from obtaining financial credit if they need it. **(Attachment 5)**

Opponent **Doug Wareham** spoke on behalf of the Kansas Bankers Association (K.B.A.). It is the position of the K.B.A. that in its current form, this bill goes beyond the scope of what is necessary to pinpoint the creditors the Commissioner's office is seeking to address. The K.B.A offers a balloon amendment to this bill which provides a floating rate cap in lieu of the flat 21% cap currently proposed in this bill.

Recognizing the need to periodically update the U.C.C.C., it is the K.B.A.'s position that enactment of this bill in current form will undo legislation adopted in 1999 by the Kansas Legislature and go beyond what is necessary to address the Commissioner's true concerns. In addition, the K.B.A. believes that, if adopted in its present form, the bill has the potential to drive business from Kansas. **(Attachment 6)**

Brad Smoot opened testimony on behalf of LoanMax. LoanMax operates in a highly regulated environment in nineteen other states. There are four licensed stores in Kansas. LoanMax is eager to cooperate with the Kansas Banking Department and to operate in accordance with all laws and regulations of the state. The President, General Counsel, LoanMax managers, and some customers are also here today to visit with you.

Current law guarantees the continuing availability of credit to consumers up and down the economic scale. **HB 2143** removes that guarantee for low and middle income people or those with impaired credit histories.

Since opening for business in Kansas seven months ago, LoanMax has made nearly 7,000 loans, suggesting that there is a pent-up need for small consumer loans. Low interest rate loans seem consumer friendly, but a loan that you can not get is not consumer friendly.

Proponents of **HB 2143** focus on the high A.P.R., which is misleading. These are short-term loans not intended to continue for a year. They are not comparable to 30 year home mortgages or 60 month new car loans. Proponents of interest rate caps also maintain that LoanMax takes advantage of people "ignorant" of interest rates. Our customers are adults with ordinary cash flow needs like many of us have had from time to time. LoanMax tells them how much the loan will cost, that it is high interest, encourages them to consider less expensive lending opportunities, and encourages them to repay the loan quickly. We want and have happy customers.

We think the Legislature made the right decision directing the U.C.C.C. Administrator to "assure an adequate supply of credit to consumers" and that the 1999 Kansas Legislature was correct in letting the marketplace

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determine what that credit should cost. We urge the Committee to think long and hard about the “unintended consequences” of this legislation. **(Attachment 7)**

Mr. **Rod Aycox**, representing LoanMax testified as an opponent. He informed the committee that LoanMax has made 6900 cash advances from the four Kansas offices, and has also made 2800 cash advances from their Missouri offices to customers residing in Kansas. He emphasized that their product fills a niche market. LoanMax offers a product for short-term cash flow problems. Their current interest rate is 22% per month. Mr. Aycox stated that their loans are made based on vehicle collateral and they do not run credit reports or report to credit bureaus. They do not garnish wages. Their loans are vehicle only exposure. Vehicles are sold at auction with excess proceeds promptly returned to the borrower. They have repossessed 210 vehicles since beginning of business in Kansas. This amounts to under five percent of loans.

These are small balance transactions, averaging three to four hundred dollars and are very costly to process. Loss ratios are higher. Compared to home equity loans the LoanMax product is actually cheaper for a short-term commitment. **(Attachment 8)**

Mr. Aycox presented Mrs. **Amy Parker**, Miss **Lisa Ross**, and Miss **Jo Tiffany**, who testified as satisfied customers of LoanMax.

Bill Sneed, representing MidWest Title Loans Company, testified as an opponent. MidWest Title Loans is based in Tennessee. They do not operate in the state of Kansas, but have hundreds of customers who reside in Kansas and do business thru their Missouri offices. Mr. Sneed stated that his client felt it important to go on record that they would not be interested in establishing offices within the state of Kansas were this legislation passed. This legislation would put overly stringent limits on the type of financial transactions in which they engage. **(Attachment 9)**

Written testimony only was provided by **Intrust Bank**, an opponent, **(Attachment 10)**.

Chairman Cox opened the floor to questions.

Representative Brunk asked Mr. Sneed how his company differs from other companies and how his product would differ. Mr Sneed replied that his product is similar to LoanMax and wherever his customer has opened for business where competition exists the interest rates have gone down.

Representative Grant asked Mr. Wareham if the K.B.A would support this bill if his amendment were adopted. Mr. Wareham said that if both components of his amendment were adopted the K.B.A. opposition to this bill would disappear.

Representative Vickery asked Mr. Aycox why LoanMax had reduced their interest rates from 360 percent to 224 percent. Mr. Aycox responded that the drop was due to market conditions. He also asked Mr. Aycox that if five percent of their loans ended with repossession, were there other loans that were simply written off. Mr. Aycox replied that, yes, they have written off approximately four percent of their loans which is in addition to the five percent that were repossessed.

Representative O'Malley asked Mr. Aycox about other operations and whether those states have loan caps. Mr Aycox replied that they operate in 21 states of which five have rate caps in the twenty two to twenty five percent per month range. Three states limit the length of the loan.

Chairman Cox closed the hearings on **HB 2143** and announced that the committee would not hear **HB 2145** today. The committee will work **HB 2143** on February 16.

The meeting was adjourned at 5:07 P.M. The next meeting will be Wednesday, February 9.