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PAYDAY LOANS – 2009 WISCONSIN ACT 405

On May 18, 2010, Governor Jim Doyle signed 2009 Senate Bill 530 into law, enacted as Wisconsin Act 405, which regulates the payday lending business.

The act, which takes effect on January 1, 2011, makes the following changes:

- Requires payday lenders to obtain special payday lending licenses;
- Regulates where payday lending businesses may be located;
- Creates new regulations for payday lenders and payday loans;
- Directs the Division of Banking to oversee payday lending practices; and
- Eliminates automobile title loans in Wisconsin.

PAYDAY LENDING

Payday lending refers generally to the practice of issuing small, short-term loans that often carry high interest and finance charges to people who would not otherwise be able or willing to borrow money under a conventional loan. These payday loans, also referred to as deferred deposit loans, are most often made against a borrower's personal check or automatic fund transfer agreement, which will be cashed or completed at the end of the loan period, ensuring that the lender has some security on the loan. Typically, a payday lender will issue a loan upon acceptance of a borrower's check or fund transfer agreement made out for the balance of the principal plus an additional amount of money that will represent the interest on the loan. For example, a lender may issue a \$100 loan upon receiving a check or fund transfer agreement in the amount of \$115 from the borrower, then at the end of a brief loan period the lender will cash the check or complete the fund transfer and be repaid with interest. Because these are such short-term loans the interest, when converted to an annual percentage rate (APR), can be exorbitant. In the case of

the example above, \$15 on a two-week \$100 loan would work out to an APR of 390%. Additionally, if a borrower does not have enough money in his or her bank account to cover the check or fund transfer agreement when it comes due, he or she will also likely face high penalty fees from the payday lender. The interest and fees charged by payday lenders can cause small, short-term loans to snowball into large amounts of debt very quickly. Because payday loan borrowers are often low-income, this debt, and the availability of more short-term credit to pay it off, can become a vicious cycle of borrowing and defaulting. Act 405 was adopted to alleviate concerns over this situation by increasing regulation and oversight of such loans.

LEGISLATIVE HISTORY

2009 Senate Bill 530 was introduced by Senators Sullivan, Hansen, Miller, Lehman, and Robson, and cosponsored by Representative Fields. The bill, as originally introduced, would have prohibited payday lenders from issuing loans to individuals who had already incurred a total of \$900 or more in outstanding payday loan liability from any licensed lender. This proved to be a contentious issue, and the cap was eventually increased to \$1,500 or 35% of a borrower's gross monthly income in Senate Substitute Amendment 1.

The bill, as passed by the legislature, permitted lenders to assess interest at a rate of up to 2.75% on loans that were not paid at maturity. The governor used his partial veto power to prohibit any interest on loans that are not paid at maturity.

The original senate bill did not seek to regulate title loans in any way. Assembly Amendment 2 added a significant number of title loan regulations to the proposal and was adopted to become part of the final bill passed by the legislature. The governor used his partial veto power to delete almost all of the title loan regu-

lation language, leaving a single sentence that effectively prohibits title loans entirely.

MAJOR PROVISIONS OF WISCONSIN ACT 405

Payday Loan Licensing

Prior to Act 405, payday lenders were only required to be licensed lenders to operate in Wisconsin. A licensed lender is any lending institution (with the exception of banks and similar institutions described below) that charges a finance charge of more than 18% per year. Under the act, institutions offering payday loans must now be specifically licensed as payday lenders by the Wisconsin Department of Financial Institution's Division of Banking ("the Division"). This license must be obtained before originating or servicing any payday loan involving a Wisconsin resident, whether the loan is transacted face-to-face, or through the telephone, Internet, mail, or other means. Banks, savings banks, savings and loan associations, trust companies, and credit unions are all specifically exempted from both the licensed lender requirements and the new payday lender licensing requirement.

A payday lender must apply for a payday lending license by submitting an application to the Division along with a \$300 fee for the investigation of the application, and a \$500 annual licensing fee. The application also contains an acknowledgement that the lender is subject to the requirements of Wisconsin Statutes Chapter 427, which regulates debt collection. Finally, license applicants must file and maintain a bond of at least \$5,000 for each license they receive as a further acknowledgement that they will adhere to Wisconsin's payday lending laws.

Under Act 405, payday lending licenses are not transferable, and an individual or institution must obtain a license for each place of business where payday lending or payday loan servicing will be conducted. Lenders must also notify the Division if the address of such a place of business changes, and a new, amended license will be issued to reflect the new address.

If the change of address results in the place of business moving from one city, village, or town to another, then the license cannot be amended, and a new license must be obtained for the new location. The Division also has authority to suspend or revoke payday lending licenses under certain circumstances, including application misrepresentations, violations of various laws, or failure to pay the annual license fee.

Payday Loan Places of Business

Act 405 also regulates the places of business from which payday lenders operate. As mentioned above, payday lenders must obtain payday lending licenses for each of their places of business. The law then requires that these licenses be conspicuously posted in each place of business, or in a conspicuous location on a Web site in the case of lenders who operate over the Internet, so that they can be viewed by consumers. Payday lenders are also required to maintain all books and records related to payday lending, either in each of their licensed places of business, or in one central location as long as that location is also a licensed payday lending place of business. This allows the Division to efficiently review payday lenders' records to ensure compliance with the statutes at either the place of business where a loan was originated or serviced, or at a single location that houses all of the records for a number of places of business.

The regulation of payday lending places of business is not limited to on-site licenses and records. Act 405 also regulates the physical location of payday lending businesses, and what services may be offered at such locations. Under the new law, a payday lender may not operate in a Wisconsin city unless it receives a permit to do so from the city council. A city council cannot issue such a permit if the payday lending place of business would be located within 1,500 feet of another payday lender, or within 150 feet of an area zoned for single-family or two-family residential use. A city council may adopt a zoning ordinance that zones payday lenders more strictly, but it is not authorized to allow less strict zoning of payday lend-

ing places of business. The act contains a similar provision for zoning in unincorporated areas of counties, and applies the city requirements to any village or town that exercises village powers.

Payday lenders are only authorized to conduct payday loan business at their places of business unless they request and receive written authorization from the Division to conduct other business. With proper prior authorization, a payday lending place of business can also offer one or more of the following services, whether offered by the licensee or a third party: 1) a currency exchange service; 2) a check selling business; 3) a loan business; or 4) a sales finance company.

Regulation of Payday Loans

Act 405 establishes additional regulations on the actual practice of payday lending, from the issuance of loans, to the terms of those loans, to the process of repayment. At the time a payday loan is issued the lender must make various disclosures regarding the total cost of the loan, the annual percentage rate of interest on the loan, and the borrower's rights and obligations. Lenders must also ensure, using a database prepared by the Division, that no borrower has outstanding aggregate debt of more than \$1,500 or 35% of the borrower's gross monthly income, whichever is less, before issuing a new payday loan. Following the issuance of a payday loan, as mentioned in the disclosures above, borrowers have until the close of the following business day to rescind their acceptance of the loan agreement. In the case of a lender that operates on a 24-hour basis, such as an Internet-based lender, the close of the following business day will be 5:00 p.m. If a borrower rescinds acceptance of a loan agreement, then the principal must be returned immediately and the lender may not charge the borrower any fee or penalty.

The act also regulates the terms and conditions that a payday lending agreement may contain. The requirements of the Wisconsin Consumer Act ("the WCA," Chapters 421 through 427 of the Wisconsin Statutes) continue

to apply to payday loans, except in those cases where the WCA and the payday lending statute conflict, in which case the latter controls. In addition to the standard WCA requirements applicable to all loans, payday lenders may not charge any interest after the maturity date of a payday loan, although they are free to charge as much interest as they like for the repayment period of the loan. A payday lender may not charge any penalty or fee for prepayment, late payment, or default on a payday loan, though lenders are permitted to implement a service charge of not more than \$15 for a personal check or funds transfer that is denied due to insufficient funds.

Finally, the act regulates the repayment of payday loans in some situations. Lenders may not prohibit prepayment of payday loans, and if a borrower does prepay before the date of maturity, a lender must return the unearned portion of the interest assessed on the loan. If a borrower is unable to repay a payday loan at the date of maturity, then the lender must allow the borrower the option of repayment of any outstanding balance in four equal installments with due dates coinciding with pay periods at the borrower's place of employment. A borrower is permitted to repay a payday loan with the proceeds of a second payday loan, but this "rollover" can only occur once, so the second loan may not be paid off with the proceeds of a third payday loan.

Criminal Penalties and Consumer Lawsuits

Act 405 makes a violation of the payday lending statute a misdemeanor punishable by a fine of not more than \$500, imprisonment for not more than six months, or both. Any person, partnership, corporation, or the officers or employees thereof may be liable for such violations.

The act also creates a private cause of action that allows a borrower to recover damages of \$250 or the amount of the loan, whichever is greater, from any lender who violates the payday lending statute.

If a lender is not licensed to originate or service payday loans but does so anyway, the

lender will be liable for the violation and any loans issued will be held void and unenforceable. In such cases, the borrower may recover all amounts paid under the voided loan in civil court, provided an action to recover is commenced within the one year statute of limitations.

Division of Banking Authority and Duties

Act 405 requires the Division of Banking, which is part of the Wisconsin Department of Financial Institutions, to regulate payday lenders. The Division is granted the authority to promulgate rules that, in keeping with the payday lending statute, regulate the industry. Proposed rules on payday lending have been drafted and are available through the Wisconsin Department of Financial Institutions' Web site. If the proposed rules are adopted, they will be codified in the Wisconsin Administrative Code. The act also grants the Division the power to hold hearings, take testimony, secure evidence, and investigate violations of the payday lending statutes by lenders.

The act also requires the Division to collect and compile the annual reports that each payday lender must submit under the payday lending statute. The Division must review these reports and prepare its own annual report to an appropriate standing committee of the legislature. The Division's annual report must contain data on the total number of payday loans issued in the state, the average principal amount and interest on those loans, and their rate of repayment, among other things.

The act further requires the Division to prepare written education materials about payday lending for borrowers, including the potential costs of the loans and other possible options for obtaining more traditional loans or financing. The written materials must contain a warning that payday loans are not intended to meet long-term financial needs and should be used only in emergencies, as well as statistical information on payday loans contained in the Division's annual report to the legislature.

Finally, the act requires the Division to create, or contract with an outside company to

create, a single, statewide database that will allow payday lenders to identify borrowers using a unique identification number, and to provide information that lenders need to avoid violating state or federal law when issuing payday loans. The Division is also required to set a database transaction fee for each use of the database, which will be used to recoup the money spent developing the database and ensure its continued maintenance.

Motor Vehicle Title Loans

Act 405, as originally passed by the legislature, contained various provisions that would have regulated motor vehicle title loans in Wisconsin as well. Title loans, which are defined in the statutes as personal loans of \$25,000 or less secured by an interest in the borrower's vehicle (except for the purchase money security interest that automobile loan lenders receive in financed vehicles), share many of the issues and concerns of payday loans. Governor Doyle used his partial veto power to eliminate all title loan regulations, leaving only the words "No licensed lender may make a title loan" to accompany the definition of licensed lender and title loan in the newly created statutory section. By doing this, the governor eliminated title loans in Wisconsin, and thereby eliminated any need to regulate them in Act 405.

FOR MORE INFORMATION

2009 Wisconsin Act 405:

<http://www.legis.state.wi.us/2009/data/acts/09Act405.pdf>

DFI Payday Loan Page:

http://www.wdfr.org/yymm/brochures/financing/payday_loans.htm

DFI Report – Review of Payday Lending in Wisconsin – 2001:

http://www.wdfr.org/_resources/indexed/site/newsroom/press/payday_loan_may_2001.pdf

Wisconsin State Law Library Banking Law Page:

<http://wilawlibrary.gov/topics/banking.php>