Testimony of
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U.S. Senate Committee on Banking, Housing, and Urban Affairs
Full Committee Hearing: "New Consumer Financial Products and the Impacts to Workers"

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The Consumer Federation of America (CFA) greatly appreciates the opportunity to testify before the Senate Committee on Banking, Housing, and Urban Affairs on "New Consumer Financial Products and the Impacts to Workers." CFA is a nonprofit association of more than 250 national, state, and local consumer groups that was founded in 1968 to advance the consumer interest through research, advocacy, and education. For over 50 years, CFA has been at the forefront of ensuring that our marketplace is fair and safe through advancing the consumer interest. CFA has a broad portfolio of issues including financial services, banking, credit, investor protections, privacy, food safety, product safety, telecommunications, energy efficiency, housing, insurance, and saving. CFA's non-profit members range from large organizations, such as Consumer Reports and AARP, to small state and local advocacy groups, as well as unions, co-ops, and public power companies.

New consumer credit products are exploding across market areas, including but not limited to Buy Now, Pay Later (BNPL) and Earned Wage Advance (EWA) products. Fintech providers are using the guise of innovation to offer "free" cash advance and overdraft protection products in exchange for purportedly voluntary tips. Predatory lenders are finding rogue banks to launder their loans through in order to evade state usury and consumer protection laws. Plus, Training Repayment Agreement Provisions (TRAPs) trap consumers in low paying jobs with the threat of unmanageable debt and high interest rates.

Although these products, provisions, and fee models seem incredibly different at first glance, and are unique in reality, they share one thing in common: they disguise credit and its true cost to consumers and regulators alike.

Some of the fee models, schemes, and provisions discussed today are inherently deceitful and downright predatory. Other products may help certain consumers manage their finances, but even those are not risk free. Either way, at their core, each of the products and provisions discussed today are still credit products that should be covered by basic consumer protections at the state and federal level, including interest rate limits, underwriting for ability-to-repay, cost transparency, dispute rights, and fair lending laws.

The consumer credit products discussed during this hearing are each distinct, however they share similarities in how they operate and how they use "innovation," whether in how the product is offered (via smartphone application/online), labeled, or structured, to claim that they do not fit within the existing regulatory framework. Regardless of their structure, each of these products is credit– they provide funding or the promise of funding today and are repaid at a later date. Given that, these products should be subject to the host of state and federal consumer protection laws that regulate credit products and prevent discrimination. It is also important that they be examined for unfair, deceptive, or abusive practices independently of compliance with credit laws.

Although innovation has an important role in the financial marketplace, it should be pursued in a way that is consistent with and enhances consumer protections. It should not shield innovators from enforcement and supervision nor limit state and federal regulatory authority.

This testimony will address various emerging forms of credit: Buy Now, Pay Later; Earned Wage Advance; cash advance, overdraft protection, and other credit products that collect "tips; Training Repayment Agreement Provisions; and Rent-a-Bank loans.

Buy Now, Pay Later products, if used as designed, can provide consumers with an affordable way to finance larger purchases, as these products allow consumers to purchase an item by only paying a portion of the price up front. Then, the consumer typically pays the rest of the credit in three equal, often interest-free installments over a set period (often 6 weeks). However, depending on structure, BNPL products can lack underwriting for a consumer's ability to repay, can rely on the expectation of fees, can lead consumers into taking on unmanageable amounts of debt, can lack dispute or refund rights should a consumer be unsatisfied with their purchase, and can lead to negative credit reporting and debt collection.

Earned Wage Advance (EWA) products are funds advanced by a third-party to a consumer before the consumer's regular payday. These funds are repaid out of the next paycheck. EWA products that charge fees are ostensibly a lower-cost form of a payday loan—requiring workers to pay to get paid—and should be regulated as credit. Many employers are starting to offer EWA programs for free, making those fee-based programs even more concerning. These programs are not risk free, as they can lead to the same cycle of repeat borrowing as other balloon payment loans. Even free EWA products may still create a hole in next week's paycheck and should be studied further.

Faux Earned Wage Advance, overdraft protection, and other cash advance products that collect "tips" are simply disguising finance charges under a new name. Tips are not truly voluntary, as they can be structured so that it is difficult for the consumer to avoid paying the default tip. By labeling finance charges otherwise, consumers feel obligated to tip, like in a restaurant or service setting, but unlike those settings, tips for credit products do not go towards a worker but rather the company's bottom line. The true cost is not clear to consumers, and tips can add up quickly, costing nearly as much as traditional payday loans in some instances. These should be viewed and regulated as finance charges subject to state and federal credit laws, including state usury laws and the Military Lending Act (MLA). Lenders that claim to provide consumers with EWAs but are not integrated with employers are simply payday loans and should be regulated as such.

Training Repayment Agreement Provisions (TRAPs) are a form of shadow student debt—employment contract provisions that require a consumer to pay large fees for on-the-job training or orientations if the consumer decides to leave before an arbitrarily determined date, essentially indebting the consumer to the employer. TRAPs are often found buried deep within employee contracts for low-paying jobs with poor working conditions and are essentially used to trap the employee in the job with threats of high interest rates, attorney and collection fees to collect the money owed, or withholding of other benefits, like pay and retirement balances, should they leave before the predetermined date.

The “rent-a-bank" scheme is used by predatory, often payday lenders in order to charge triple digit interest rates in states where those rates are illegal. Banks are largely exempt from state interest rate caps, so the predatory lender finds a rogue bank to name on the loan agreement or launder the loan in order to evade state laws. Rent-a-bank loans can be payday, auto-title, or installment loans, as well as credit offered through businesses that sell auto repairs, furniture, and even pets at rates as high as 200% APR.

Each of these products should not use the guise of innovation, the cover of a lengthy employment contract, a borrowed label, or a sham bank partnership to shield themselves from federal and state oversight and regulation of credit, consumer protection, and fair lending laws. Oversight is especially urgent as these offerings continue to increase and infiltrate new market areas. Failure to do so would lead to an undermining of consumer protection laws, making the financial marketplace less fair and competitive.

CFA recommends the following:

- Innovative financing products should be viewed and regulated as credit. State and federal financial regulators should supervise fintech providers to ensure that they are compliant with federal and state credit, fair lending, and consumer protection laws, as well as not engaging in unlawful discrimination or unfair, deceptive, or abusive acts or practices.
- Fintech providers should only offer products after determining a consumer’s ability to repay. Ability to repay should consider both income and financial obligations, as failure to do so can lead to a cycle of debt.
- Price transparency and unified terms and conditions are critical. The cost of credit should only be portrayed to consumers as an Annual Percentage Rate (APR) so that they are able to compare products and make informed, knowledgeable decisions based on their financial situation.
- Loans should be structured in an affordable way with proportional penalty fees, so that a consumer can repay without needing to reborrow or borrow elsewhere. Regulators should closely examine evasive pricing models including tips, inflated fees, participation fees, and payment rescheduling fees, to ensure that these are not evasive attempts to disguise finance charges.
- Consumer data should only be used in a responsible manner and in a way that consumers expect it to be used.
- State and federal regulators should consider collecting, analyzing, and publishing data to better understand and illuminate the risks associated with these products.
- State and federal regulators should work together, across agencies and levels of government, in order to ensure consumers are protected and predatory actors are held accountable.
- For BNPL, consumers should have the same chargeback rights as they do with credit cards, so that consumers have recourse should they run into a problem with their purchase.

- Congress should adopt a national interest rate cap, the simplest and most straightforward way to protect consumers from predatory interest rates.

1. Buy Now, Pay Later:

    A. Introduction

Although Buy Now, Pay Later (BNPL) options only began to appear in 2019, these products and consumer use have increased dramatically in recent years. The market grew by more than 70% in 2021[1] and is expected to increase 10 to 15 times its current size by 2025.[2] Although BNPL use is still far less common than debit and credit card use, roughly one-third of adults have used BNPL in the last 12 months.[3] BNPL is a checkout option available from many online retailers, credit cards, banks, and third-party providers that allows consumers to purchase an item by only paying a portion of the price up front. Then, the consumer typically pays the rest of the debt in three equal installments over a set period (often 6 weeks) and often without interest. BNPL credit accounts for a growing proportion of the non-bank credit market. For example, California found that the top six BNPL providers originated more than 10 million loans to consumers in 2020, which accounted for 91% of total non-bank consumer loans originated in 2020.[4] Both the number of offerings and users of BNPL have continued to grow considerably in recent years.

A handful of companies are viewed as key players within the BNPL industry and have the largest market share of BNPL transactions in the United States— Affirm, Afterpay, Klarna, PayPal's pay-in-4, Sezzle, and Zip, formerly known as Quadpay.[5] Although BNPL products can help certain consumers manage their finances as discussed below, these products are not risk free.[6] In

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[1] Ron Shelvin, *Forbes*, "Buy Now, Pay Later: The "New" Payments Trend Generating $100 Billion In Sales" (Sept. 7, 2021), https://www.forbes.com/sites/ronshevlin/2021/09/07/buy-now-pay-later-the-new-payments-trend-generating-100-billion-in-sales/?sh=71a2b7b62ffe [hereinafter Shelvin, The "New" Payments Trend (Sept. 2021)].

[2] CB Insights, *Disrupting The $8T Payment Card Business: The Outlook On 'Buy Now, Pay Later'* (Mar. 2, 2021), https://www.cbinsights.com/research/report/buy-now-pay-later-outlook/ [hereinafter CB Insights, Disrupting (Mar. 2021)].

[3] Tom Akana, Federal Reserve Bank of Philadelphia, *Buy Now, Pay Later: Survey Evidence of Consumer Adoption and Attitudes* (June 2022), https://www.philadelphiafed.org/-/media/frbp/assets/consumer-finance/discussion-papers/dp22-02.pdf [hereinafter Akana, Federal Reserve Bank of Philadelphia, BNPL Survey Evidence (June 2022)].

[4] California Department of Financial Protection and Innovation, *Annual Report of Finance Lenders, Brokers, and PACE Administrators Licensed Under the California Financing Law* (Oct. 2021), https://dfpi.ca.gov/wp-content/uploads/sites/337/2021/10/2020-CFL-Aggregated-Annual-Report.pdf.

[5] BusinessWire, *United States Buy Now Pay Later Market Report 2022: BNPL Payments are Expected to Grow by 66.5% to Reach $82086.8 Million in 2022 - Forecast to 2028 - ResearchAndMarkets.com* (Feb. 2022), https://www.businesswire.com/news/home/20220214005569/en/United-States-Buy-Now-Pay-Later-Market-Report-2022-BNPL-Payments-are-Expected-to-Grow-by-66.5-to-Reach-82086.8-Million-in-2022---Forecast-to-2028---ResearchAndMarkets.com.
See also, CB Insights, Disrupting (Mar. 2021).

[6] For a sample of consumer complaints *see* Rachel Gittleman, *Statement for the Record Submitted to U.S. Committee on Financial Services' Task Force on Financial Technology on "Buy Now, Pay More Later? Investigating Risks and Benefits of BNPL and Other Emerging Fintech Cash Flow Products"* (November 2, 2021), https://consumerfed.org/wp-content/uploads/2021/11/CFA-Submits-Statement-for-the-Record-to-U.S.-House-Task-Force-11.2.21.pdf [hereinafter Gittleman, Statement re BNPL (March 2022)];
See also, Ed Mierzwinski and Mike Litt, U.S. PIRG Education Fund, *The hidden costs of "Buy Now, Pay Later" Complaints to CFPB show need for action* (March 2022), https://pirg.org/wp-content/uploads/2022/03/BNPL-REPORT-USPIRG_0.pdf [hereinafter Mierzwinski and Litt, U.S. PIRG, BNPL (Mar. 2022)].

addition, as BNPL expands into new markets, including auto repairs, medical care, groceries,[7] and student loans,[8] the risks posed by BNPL can be even more severe.

Further as compared to credit card users, BNPL users are more likely to earn less than $75,000 annually, to be younger, and to be people of color.[9] These consumers are more likely to have limited or no credit history, existing debt burdens, and less wealth and lower wages to pay off that debt. The consequences of unaffordable BNPL credit can be disproportionately severe for these consumers. And yet, BNPL products have largely evaded oversight by federal and state regulators.

While we greatly appreciate the Consumer Financial Protection Bureau's (CFPB) investigation into five of the largest companies offering BNPL in late December[10] and the subsequent public inquiry, we are eager to see any resultant research and actions. In addition, we appreciate Senator Jack Reed, Chairman Sherrod Brown and other members of this committee urging the CFPB to take action regarding governance and oversight of BNPL providers.[11]

However, to date, California is the only state that has taken enforcement actions against BNPL providers. California fined three BNPL providers in 2020[12] and an additional provider earlier this year[13] for making unregulated loans to consumers and required them to apply for the applicable license.

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[7] Priya Krishna, *The New York Times, "*Would You Take Out a Loan to Buy This Week's Groceries?" (August 29, 2022), https://www.nytimes.com/2022/08/29/dining/buy-now-pay-later-loans-groceries.html.

[8] Student Borrower Protection Center (SBPC), *"Point of fail: How a Flood of "Buy Now, Pay Later" Student Debt is Putting Millions at Risk* (March 2022), https://protectborrowers.org/wp-content/uploads/2022/03/SBPC_BNPL.pdf [hereinafter SBPC, Point of Fail (March 2022)].

[9] Akana, Federal Reserve Bank of Philadelphia, BNPL Survey Evidence (June 2022).

[10]Consumer Financial Protection Buruea (CFPB), "Consumer Financial Protection Bureau Opens Inquiry into "Buy Now, Pay Later" Credit" (December 16, 2021), https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-opens-inquiry-into-buy-now-pay-later-credit/?_gl=1*197krbo*_ga*MjI4Mjg2NTIwLjE2MzY0MTA1NzY.*_ga_DBYJL30CHS*MTY2MjA2NjA2My44Ni4xLjE2NjIwNjYxMDIuMC4wLjA.

[11] U.S. Senate Committee on Banking, Housing, and Urban Affairs, "U.S. Senators Urge CFPB to Take Action to Ensure Transparency & Oversight of Buy Now Pay Later Products & Providers" (December 15, 2021), https://www.banking.senate.gov/newsroom/majority/us-senators-urge-cfpb-to-take-action-to-ensure-transparency-and-oversight-of-buy-now-pay-later-products_providers.

[12] California Department of Financial Services, "Point-of-Sale Lender Sezzle Agrees to Cease Illegal Loans, Pay Refunds in Settlement with the California Department of Business Oversight" (Jan. 16, 2020), https://dfpi.ca.gov/2020/01/16/point-of-sale-lender-sezzle-agrees-to-cease-illegal-loans-pay-refunds-in-settlement-with-the-california-department-of-business-oversight/;
California Department of Financial Services, "Point-of-Sale Lender Afterpay Agrees to Cease Illegal Loans, Pay Refunds in Settlement with the California Department of Business Oversight" (Mar. 16, 2020), https://dfpi.ca.gov/2020/03/16/point-of-sale-lender-afterpay-agrees-to-cease-illegal-loans-pay-refunds-in-settlement-with-the-department-of-business-oversight/;
California Department of Financial Services, Point-of-Sale Lender QuadPay Agrees to Cease Illegal Loans, Pay Refunds in Settlement with the California Department of Business Oversight" (Apr. 22, 2020), https://dfpi.ca.gov/2020/04/22/point-of-sale-lender-quadpay-agrees-to-cease-illegal-loans-pay-refunds-in-settlement-with-the-california-department-of-business-oversight/.

[13]CA.gov, "Buy Now, Pay Later Company Agrees to Cease Illegal Loans, Pay Refunds in Settlement" (August 9, 2022), https://dfpi.ca.gov/2022/08/09/buy-now-pay-later-company-agrees-to-cease-illegal-loans-pay-refunds-in-settlement/.

Other countries have seen similar growth in third-party BNPL products, and federal regulators have stepped in to protect consumers. For example, federal regulators in both Australia and the United Kingdom have recently taken steps to regulate BNPL apps.

The U.K. Treasury has said that BNPL providers are now under supervision of Britain's Finance Conduct Authority (FCA),[14] and that the FCA would run affordability checks on BNPL providers and ensure that all marketing is fair and clear, among other measures.[15]Additionally, Australian regulators created a new BNPL code of practice.[16] It's time for federal and state regulators to provide much needed oversight of the BNPL industry.

B. Potential Consumer Benefits

These products may offer consumers an affordable alternative to finance large purchases. If used as intended, a consumer can finance a larger purchase without interest, only paying one quarter of the purchase price up front and then paying off the rest in three equal installments, typically over six weeks. A recent survey by Consumer Reports found that nearly half of those consumers who had used BNPL chose to do so because they "didn't have enough money to purchase what [they] wanted, so this enabled [them] to afford it."[17] A Federal Reserve study also found that more than 46% of users opted for BNPL because of the size of the purchase.[18] Although this illustrates that consumers may view BNPL as an alternative to finance large purchases, it also points to the likelihood that consumers are using BNPL for purchases outside of their budget.

In comparison to credit cards, some consumers view BNPL as a more affordable payment form that can be quicker to pay off. Indeed, of those who have used BNPL, more than half of consumers chose it instead of credit cards because they could pay back the purchase in installments rather than a lump sum.[19] Similarly, another study found that nearly 44% of BNPL users chose it for the "ability to better manage their finances."[20] If paid back on time, BNPL credit can be interest free. For consumers carrying a revolving credit card balance, their purchases incur interest from the moment the purchase hits, which can cause credit card debt to be expensive and difficult to pay off. Further, credit card debt poses an increasing burden for many consumers, with credit card debt increasing to $46 billion in the second quarter of 2022, marking the largest quarterly increase in the last two decades.[21] If used as intended and with sufficient consumer protection, BNPL can certainly provide consumers with a more affordable

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[14] Ryan Browne, *CNBC*, "Britain is Cracking Down on the $3.7 Billion 'Buy Now, Pay Later' Industry" (Feb. 2, 2021), https://www.cnbc.com/2021/02/02/uk-to-regulate-buy-now-pay-later-bnpl-firms-like-klarna-and-clearpay.html.

[15] Elizabeth Piper and Huw Jones, *Reuters*, "Britain plans to regulate 'buy now, pay later' lenders" (June 20, 2022), https://www.reuters.com/markets/europe/britain-introduces-plans-better-regulate-buy-now-pay-later-firms-2022-06-19/.

[16] *Finextra*, "Australian Finance Industry Association Introduces Voluntary Code of Practice for BNPL Sector" (Mar. 2, 2021), https://www.finextra.com/pressarticle/86399/australian-finance-industry-association-introduces-voluntary-code-of-practice-for-bnpl-sector.

[17] Consumer Reports, *American Experiences Survey: A Nationally Representative Multi-Mode Survey* (Jan. 2022), https://article.images.consumerreports.org/prod/content/dam/surveys/Consumer_Reports_AES_January_2022 [hereinafter Consumer Reports, American Experiences Survey (Jan. 2022)].

[18] Akana, Federal Reserve Bank of Philadelphia, BNPL Survey Evidence (June 2022).

[19] Consumer Reports, American Experiences Survey (Jan. 2022).

[20] Akana, Federal Reserve Bank of Philadelphia, BNPL Survey Evidence (June 2022).

[21]Jacyln Peiser, *The Washington Post*, "Credit card debt surges as inflation pushes Americans to borrow more" (August 2, 2022), https://www.washingtonpost.com/business/2022/08/02/credit-card-debt-inflation/.

alternative to credit cards that can be paid off over a shorter period of time and in smaller installments than credit card debt.

Finally, some consumers may choose to use BNPL simply because it is convenient and easy, and increasingly offered at checkout for online purchases. Indeed, 20% of consumers who had used BNPL chose to do so because it was perceived as easier than paying with credit card.[22] Some BNPL providers now offer a browser extension, making online purchases with BNPL even easier.[23] Of the top ten online retailers in the U.S., six either currently have BNPL options at checkout or have announced partnerships with BNPL providers.[24] The other four are available through third party applications.

C. Consumer Risks

As explained in our joint comments to the CFPB in response to the public inquiry regarding BNPL,[25] multiple parts of the BNPL business model and product can pose serious risks to consumers, including lack of underwriting; dispute and chargeback process; effect on credit report and score; potential debt collection; payment difficulty caused by a lack of consolidated statement and payment; and insufficient financial data privacy.

Marketing of these products is enticing, with promises of instant approval and no impact on a consumer's credit, however underwriting does not meaningfully assess a borrower's ability to repay. Underwriting for BNPL products varies based on provider, and many market "instant approval" or "no credit check required" for these credit products. For many providers, consumers need only verify their identity, provide a payment form, and have a "soft" credit check pulled.[26] Some BNPL providers base purchase approvals and spending limits on the number of purchases and on time payments made on that BNPL application, rather than holistically reviewing a consumer's ability to repay along with the rest of their financial obligations. One provider even said that they approve 90% of applicants, even if they can't find critical information about the person's history and another has said it does "no external credit checking."[27] Further, as we will address later, credit reporting varies by provider and by credit reporting bureau, so if consumers have multiple BNPL loans with various providers, there's currently no way for companies to assess that since most payment history is not reported to credit bureaus.

In addition, a recent Federal Reserve survey found that heavy BNPL users are most likely to cite a lack or credit or an inability to get approved for credit elsewhere as a reason for choosing

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[22] Consumer Reports, American Experiences Survey (Jan. 2022).
[23] Klarna and Zip now offer browser extensions for Google Chrome users, *see* https://www.klarna.com/us/ and https://zip.co/us/chrome (last visited September 1, 2022).
[24] Jamie Grill-Goodman, *Retail Info Systems*, "Top 10 E-Commerce Retailers and Their Digital Experience" (Aug. 12, 2021), https://risnews.com/top-10-e-commerce-retailers-and-their-digital-experience.
[25] Center for Responsible Lending (CRL), Consumer Federation of America (CFA), & National Consumer Law Center (NCLC), Comment to CFPB re Notice and Request for Comment Regarding the CFPB's Inquiry into Buy-Now-Pay-Later (BNPL) Providers 87 FR 3511 Docket No.: CFPB-2022-0002 (March 25, 2022), https://consumerfed.org/wp-content/uploads/2022/03/Joint-BNPL-comments-3.25.22.pdf [Hereinafter CRL, CFA, NCLC, BNPL Comments (2022)].
[26] CFPB, "What is a Buy Now, Pay Later (BNPL) loan?" (December 2, 2021), https://www.consumerfinance.gov/ask-cfpb/what-is-a-buy-now-pay-later-bnpl-loan-en-2119/.
[27] Maxwell Strachan, *Vice*, "'I Know I Have an Issue': Does 'Buy Now, Pay Later' Convince People to Overspend?" (August 25, 2022), https://www.vice.com/en/article/pkgkbg/i-know-i-have-an-issue-does-buy-now-pay-later-convince-people-to-overspend.

BNPL.[28] Although we do not know whether heavy usage is caused or perpetuated by lack of sufficient underwriting, the correlation of high usage and citing lack of other credit sources as a reason for using BNPL is deeply concerning.

There are several trends that suggest that BNPL credit products are not meaningfully underwritten. For example, there is a high incidence of late fees and missed payments among BNPL users. Most providers charge late fees, and some charge other types of fees like missed payment fees, account reactivation fees, returned payment fees, and rescheduling fees. A 2021 survey of U.S. consumers who had used BNPL found that 38% had missed payments—and that percentage went up for younger consumers, with more than half of Generation Z or Millennials saying they had missed a payment.[29] For those who have fallen behind on payments, 72% reported a decline in their credit score.[30] A 2020 study found similar amounts of BPNL users falling behind on payments—43% of users had fallen behind on payments, and of those consumers, two-thirds said that the reason for falling behind was because they had lost track of payments.[31]A U.K. study found that for some providers that charge fees, these fees can make up a significant portion of the company's revenue.[32] Fees range depending on the provider, but can reach as high as $25, and many providers lack limits on how many fees can be charged, causing fees to add up quickly.[33]

Further, BNPL fees can trigger punitive overdraft and nonsufficient funds fees on the bank side. If a BNPL payment bounces or the consumer is late on a payment, late or returned payment fees can trigger overdraft and nonsufficient fund fees in a consumer's bank account. Thus, the consumer can be charged by both the BNPL provider and their bank. A Morning Consult survey found that one-third of BNPL users had overdrafted.[34] The survey also found that those consumers that had overdrawn their account were more than twice as likely as non-overdrafters to use BNPL.[35] [36] It's unclear whether this overlap is because BNPL causes overdraft fees or because BNPL users are more likely to be struggling with their finances. Regardless, it illustrates that BNPL credit is being provided to those that cannot afford it. Overdraft and nonsufficient

[28] Akana, Federal Reserve Bank of Philadelphia, BNPL Survey Evidence (June 2022).
[29] Anna Irrera, *Reuters, "*As 'Buy Now, Pay Later' Surges, a Third of U.S. Users Fall Behind on Payments" (Sept. 9, 2021), https://www.reuters.com/technology/buy-now-pay-later-surges-third-us-users-fall-behind-payments-2021-09-09/.
[30] *Id.* Although this study was released prior to the announcement that the credit reporting bureaus would begin incorporating BNPL credit into credit reports, it illustrates the fact that BNPL credit is an awkward fit, at best, within existing credit reporting system.
[31] Penelope Wang, Consumer Reports, "The Hidden Risks of Buy-Now, Pay-Later Plans" (Feb. 14, 2021), https://www.consumerreports.org/shopping-retail/hidden-risks-of-buy-now-pay-later-plans-a7495893275/ [hereinafter Wang, Consumer Reports, Hidden Risks (Feb. 2021)].
[32] Personal Finances and Funds Team, U.K. HM Treasury, *Regulation of Buy-Now Pay-Later Consultation* (Oct. 2021), https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1027366/210923_-_BNPL_condoc_-_Cleared.pdf.
[33] Leticia Miranda, *NBC News*, "The Hidden Costs of 'Buy Now, Pay Later' Loans" (Nov. 4, 2021), https://www.nbcnews.com/business/consumer/hidden-costs-buy-now-pay-later-loans-rcna4367.
[34] Claire Williams, *Morning Consult*, "'Buy Now, Pay Later' Users Significantly More Likely to Overdraft Than Nonusers" (Mar. 2, 2022), https://morningconsult.com/2022/03/02/buy-now-pay-later-bnpl-overdraft-data/.
[35] *Id.*
[36] U.K. Financial Conduct Authority, *The Woolard Review - A Review of Change and Innovation in the Unsecured Credit Market* (Feb. 2, 2021), https://www.fca.org.uk/publication/corporate/woolard-review-report.pdf [hereinafter U.K. Financial Conduct Authority, Woolard Review (Feb. 2021)].

funds fees can be incredibly damaging to consumers as overdraft and NSF fees are highly associated with closed bank accounts, leading to financial exclusion.[37]

In addition to the risk of bank fees, most providers require consumers to link the BNPL credit to a credit or debit card at check out and authorize payments to be automatically deducted. Auto-pay reduces the provider's incentive to underwrite and may violate the consumer's right to revoke this authorization, which is protected by the ban on compulsory repayment by the Electronic Fund Transfer Act (EFTA).[38] This preauthorization also makes it difficult for consumers to exercise dispute rights for returns, cancelled, or non-delivered items.

Further, allowing or requiring repayment by credit card is even more alarming.[39] Using a credit card to pay off other forms of debt is a practice that credit card issuers often do not permit with traditional debt, like mortgages and student loans. Despite that, a recent Credit Karma survey found that 22% of respondents used a credit card to pay off a BNPL account.[40] For those with revolving credit, the BNPL charge will trigger interest from the day it is posted.

Although we know consumers do use a single BNPL provider multiple times in the same month,[41] there is no way for BNPL providers to assess how many outstanding BNPL products a consumer has on other platforms, meaning the provider cannot see the scope of BNPL debt and thus meaningfully assess a consumer's ability to repay. In addition, there are concerns about consumers buying more with BNPL than without, making this lack of knowledge even more concerning. One survey found that more than [42] [43] Although the terms may be attractive, there are concerns about these products being marketed to people who cannot afford them, which can mean that buying more equates to unmanageable debt loads.

Additional concerns exist beyond insufficient underwriting. Consumers do not have the same dispute and chargeback rights as they do with credit cards, and because both a merchant and BNPL provider are involved in a return process, it can be complicated and difficult for the consumer. If a consumer has a problem with the product purchased, refund and return rights vary between providers, and information about these rights is difficult to find. A report by U.S. PIRG found that many consumers were required to keep paying the BNPL provider as the merchant and lender went back and forth about the return process.[44] Even for canceled or non-delivered

[37] CRL, Statement for the Record: *Overdraft Fees Cause Financial Exclusion; Policymakers Must Act Hearing on "Banking the Unbanked: Exploring Private and Public Efforts to Expand Access to the Financial System" Before the U.S. House Committee on Financial Services, Subcommittee on Consumer Protection and Financial Institutions* (July 21, 2021), https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-testimony-overdraft-financial-exclusion-21jul2021.pdf.
[38] *See* CRL, CFA, NCLC, BNPL Comments (2022), pg. 41.
[39] *See* for example, Splitit charges all payment to a credit card rather than a bank account, see terms and conditions, (last accessed September 11, 2022) https://www.splitit.com/shopper/.
[40] Claire Ballentine, *Bloomberg News for American Banker*, "How buy now/pay later services are boosting American credit card debt" (March 18, 2022), https://news.bloomberglaw.com/banking-law/buy-now-pay-later-services-are-boosting-u-s-credit-card-debt.
[41] Cardify, *Convenience, Debt, and Novelty: Analyzing BNPL Consumer Data* (Sept. 8, 2021), https://www.cardify.ai/reports/bnpltrend-report.
[42] Wang, Consumer Reports, Hidden Risks (Feb. 2021).
[43] Erika Giovanetti, Lending Tree, "Shoppers Use 'Buy Now, Pay Later' Financing to Purchase Things They Can't Afford" (April 20, 2021), https://www.lendingtree.com/personal/buy-now-pay-later-survey/ [hereinafter Lending Tree, BNPL (2021)].
[44] Mierzwinski and Litt, U.S. PIRG, BNPL (Mar. 2022).

items, consumers can be charged, or even charged more than once.[45] Other consumers may never receive their refund.[46] Plus, a U.K study found that consumers still viewed BNPL as a financial service that was regulated and came with associated protections. Consumers may believe that they have the same chargeback rights protected under law as with credit cards.[47]

Although BNPL has been touted as a credit building product, there are more potential risks than benefits to a consumer's credit score unless these products are reported correctly. The way in which BNPL credit is reported matters. Even for consumers that make on-time payments, reporting within the current system may lower their credit score as the current system is an inappropriate fit for BNPL. For consumers beleaguered by an unmanageable BNPL debt burden, the negative impact to their credit scores can be severe.

Based on the current plans, the nationwide Credit Reporting Agencies (CRAs) do not treat BNPL accounts in the same manner, which has the possibility to hamper any benefits.[48] Equifax has introduced a new industry code but will still allow BNPL providers to furnish data in the format of their choice.[49] In contrast, Experian[50] and TransUnion[51] have announced that BNPL products would be reported to specialty bureaus. These inconsistencies will mean that any possible benefit to consumers will depend on the user's decision of how the data is reported and used, rather than the consumer's decision. The CFPB has already expressed concerns about these dissimilar approaches.[52] Given the underwriting concerns and the potential damage to consumer credit reports, inconsistent reporting, the inclusion of delinquent data, and promotion of BNPL as a credit building product can be incredibly harmful to consumers.[53]

Regardless of how the CRAs have begun to incorporate BNPL data, FICO scores of credit reports that have incorporated said data have lowered slightly.[54] FICO warns that this is because of the increase in the number of accounts and indebtedness on consumer credit reports with BNPL.[55] This trend, however slight, still illustrates that BNPL is not an easy fit within the current system and if mishandled, can lead to severe credit reporting issues and declines in credit scores.

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[45] *Id.*
[46] AnnaMaria Andriotis, *Wall Street Journal*, "Shopping With Buy Now, Pay Later Is Easy. Getting a Refund Is Harder" (June 24, 2022) https://www.wsj.com/articles/shopping-with-buy-now-pay-later-is-easy-getting-a-refund-is-harder-11656051506?st=vo6tfil1gxii0rq&reflink=article_email_share.
[47] *Id.*
[48] Martin Kleinbard and Laura Udis, CFPB, "Buy Now, Pay Later and Credit Reporting" (June 15, 2022), https://www.consumerfinance.gov/about-us/blog/by-now-pay-later-and-credit-reporting/ [hereinafter Kleinbard and Udis, BNPL and Credit Reporting (June 2022)].
[49] Equifax, "Equifax First to Formalize Inclusion of 'Buy Now, Pay Later' Payment Information in Consumer Credit Reports" (December 20, 2021), https://investor.equifax.com/news-events/press-releases/detail/1204/equifax-first-to-formalize-inclusion-of-buy-now-pay.
[50] Greg Wright, Experian, "Introducing The Buy Now Pay Later Bureau™ from Experian" (January 26, 2022), https://www.experian.com/blogs/news/2022/01/26/buy-now-pay-later-bureau/.
[51] TransUnion, "TransUnion to Maximize Financial Inclusion Opportunities for the Nearly 100 Million Consumers Using BNPL Loans" (February 24, 2022), https://newsroom.transunion.com/transunion-to-maximize-financial-inclusion-opportunities--for-the-nearly-100-million-consumers-using-bnpl-loans/.
[52] Kleinbard and Udis, BNPL and Credit Reporting (June 2022).
[53] CRL, CFA, NCLC, BNPL Comments (2022), at 17-21.
[54] Suna Hafizogullari, FICO, "How Might Buy Now, Pay Later Loans Impact FICO® Scores?" (June 20, 2022), https://www.fico.com/blogs/how-might-buy-now-pay-later-loans-impact-ficor-scores.
[55] *Id.*

Debt collection poses risks for any credit product but can be even more severe for those that do not underwrite properly or push consumers into unmanageable amounts of debt. Consumer understanding of the terms of BNPL loans varies widely, with many consumers, especially younger consumers, not viewing BNPL as credit, according to a U.K. study.[56] If these products are not perceived as credit, consumers may not fully understand the consequences of failing to repay. For example, many BNPL companies refer accounts to third-party debt collectors, and consumers consent to that in the initial terms and conditions.[57] Depending on provider, consumers may also consent to receiving debt collection emails and phone calls and authorizing the transfer, sale, or assignment of the debt to another entity like a debt buyer. Although default is not readily discussed as a consequence of BNPL credit, one study found that 1 in 10 consumers had defaulted on their BNPL credit product.[58] Further, consumer complaints to the CFPB illustrate that debt collection poses a great risk, with 25% of complaints about BNPL to the CFPB about debt collection.[59] These products are credit and carry the same consequences for defaulting as other types of loans.

Lack of clear and uniform consumer disclosures and statement requirements make it difficult for consumers to understand the exact cost of the credit, to compare costs amongst providers, and to keep track of multiple BNPL credit products at a given time. Under TILA, credit card providers are required to provide a billing statement that includes the amount and date of each credit extension, the payment due date, any finance charge or fees, the total charges calendar year-to-date, and the creditor's address for billing error purposes.[60] This critical information is provided in a clear, easily accessible manner. However, BNPL providers are not required to uniformly or clearly disclose how much these fees are, where to find information about fees, and whether these fees are capped. Some fees are listed in the terms and conditions, while others are listed in an installment agreement or in "frequently asked questions" sections on websites. Certain products contain disclosures about the possibility of a fee without an indication of the amount of that fee. Plus, one survey found that although seven in ten BNPL users were charged interest or fees for missed payments, fewer than one-third of users knew what those fees or interest would be before entering into the agreement.[61]

Further, each consumer purchase of a product or good is financed with its own payment plan and has its own payment due dates, as opposed to a single, monthly payment like other forms of credit. A single monthly payment is easier to track and manage than various payments throughout the month. Consumers with multiple BNPL credit products may find it difficult to track since due dates vary based on the date of purchase. Plus, some providers also charge

[56] U.K. Financial Conduct Authority, Woolard Review (Feb. 2021).
[57] CRL, CFA, NCLC, BNPL Comments (2022) at 24-28.
[58] Citizens Advice, "One in 10 Buy Now Pay Later shoppers have been chased by debt collectors" (Sept. 3, 2021), https://www.citizensadvice.org.uk/about-us/about-us1/media/press-releases/one-in-10-buy-now-pay-later-shoppers-have-been-chased-by-debt-collectors/.
[59] Mierzwinski and Litt, U.S. PIRG, BNPL (Mar. 2022).
[60] Reg. Z § 1026.7
[61] Lending Tree, BNPL (2021).

rescheduling fees for consumers who need to move their payments, making it burdensome for consumers to change the payment schedule should an unexpected financial obligation arise.[62]

Like with many of the products discussed today, BNPL providers harvest and store immense amounts of consumer data. Consumer payment, purchase history, and other personal information may be improperly used by BNPL providers. For example, earlier this year, the CFPB raised concerns about Apple's data misuse with its BNPL product.[63]

Although BNPL offerings typically provide financing for goods and clothing, these products are shifting into new market areas, including groceries, student loans, travel, and even medical debt. In fact, in a forthcoming survey of 1200 LMI Latino consumers, UnidosUS, the nation's largest Hispanic civil rights organization, found that although only 14% of respondents have used a Buy Now Pay Later (BNPL) product, 49% of those respondents used BNPL for necessities such as groceries, gas, utilities, and household supplies.[64] That number goes up to 62% for respondents who are unbanked and don't have a credit card.[65] Using BNPL for groceries and other necessities may push consumers, especially those who are already overextended and lack other forms of credit, into unmanageable debt loads.

In addition, the Student Borrower Protection Center found that fifty unaccredited and/or unregulated for-profit schools marketed BNPL as a student loan offering.[66] BNPL providers for student loans have shifted into for-profit credentialing bootcamps, which lack any regulatory oversight and appear to not provide graduates with any of the promised benefits and career prospects.[67]

With a similar structure to other BNPL plans, these financing options offer no interest and no hard credit check, often with similar terms and conditions, including unexpected fees, limited or no underwriting, no chargeback rights, and mandatory arbitration agreements. However, in certain market areas, BNPL can be even more problematic for consumers.

D. Recommendations

As explained in joint comments CFA and fellow consumer organizations filed with the CFPB, BNPL providers are within the scope of TILA and should be treated as "Card Issuers" subject to all credit card protections codified by TILA.[68] As clearly illustrated in those comments, BNPL providers offer consumers an open-end credit device that is designed for repeat use and has a

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[62] *See* Sezzle provides one free reschedule on every order, but charges fees for any payment moves beyond that, see https://shopper-help.sezzle.com/hc/en-us/articles/360045946992-How-do-I-reschedule-a-payment- (last visited September 11, 2022).

[63] Ron Shevlin, *Forbes*, "Apple Accused Of Potential Consumer Data Misuse With Its 'Buy Now, Pay Later'" Service (July 27, 2022) https://www.forbes.com/sites/ronshevlin/2022/07/27/cfpb-accuses-apple-of-misusing-consumer-data-with-its-buy-now-pay-later-service/?sh=6d3afa6f555d.

[64] UnidosUS, Survey of 1200 Low to Moderate Income Latino Consumers (forthcoming) (2022).

[65] *Id.*

[66] SBPC, Point of Fail (March 2022).

[67] *Id.*

[68] For legal analysis *see* CRL, CFA, NCLC, BNPL Comments (2022) at 29-35.

replenishing credit line.[69] Indeed, they have all the core functions to be designated a credit card under both the general TILA definition and the CARD Act definition.[70]

We urge the CFPB to clarify that BNPL products are credit cards, subject to the fee disclosures, ability-to-repay requirements, reasonable and proportional penalty fees, chargeback protections, dispute rights, standard statement requirements, and appropriate and helpful credit reporting practices that apply to credit cards. These protections would ensure that consumers have the same basic protections they do when using other forms of credit.

Beyond the CARD Act, federal and state regulators should provide necessary oversight and supervision of BNPL providers, ensuring that they are not engaging in unlawful discrimination or unfair, deceptive or abusive acts or practices. Although many of these closed-end credit products largely do not carry periodic interest, most have late fees, missed, or rescheduled payment fees, and other finance charges that should not be permitted to exceed the allowable interest and fees for active-duty military under the MLA. Further, many of these products include mandatory arbitration agreements, which covered military members should be exempt from as established by the MLA.

In addition, given that consumers of color use BNPL at higher rates than white consumers, it is incredibly important that state and federal regulators enforce anti-discrimination laws to ensure that there are not disparate impacts on certain consumers.

The CFPB should also ensure that BNPL providers are compliant with EFTA's ban on compulsory repayment by electronic transfer. In addition, since many terms and conditions include consent to receive communication from third-party debt collectors, they should also be compliant with the Fair Debt Collection Practices Act (FDCPA).

State regulators should require lenders to abide by applicable licensing and usury laws. State and federal regulators should make sure that lenders are not charging unfair fees or shifting into an abusive fee model.

Finally, state and federal regulators should consider collecting data on these programs to better understand the risks associated with them.

2. Earned Wage Advance (EWA) Products

A. Introduction

Earned Wage Advances (EWA) are an employer-based form of credit. Employees can use EWAs to take out an advance ahead of payday for wages they have earned but have not yet been paid. The third-party EWA provider uses the employer's time and attendance system to gauge how much an employee has earned. The EWA provider then advances those funds to the employee, which are repaid to the EWA provider through a variety of avenues: the EWA can deduct the employee's payroll; the provider can offset the employee's next direct deposit to an associated debit or payroll card; the provider can intercept wages through an intermediate pass-through

[69] *Id.*
[70] *Id.*

account; or the provider can debit the worker's bank account directly. The final option creates the risk for consumers of overdraft and nonsufficient fund fees. Use of these products has grown recently, with $9.5 billion moved by EWA providers in 2020 according to the Aite-Novarica Group.[71]

Regardless of structure, a fee-based EWA product is essentially a payday loan—a product where a third-party advances funds to a consumer ahead of the consumer's payday and is then repaid in some fashion out of the next paycheck —regardless of whether it's lower than a traditional payday loan.

Further, many of these providers charge both access fees and inflated expedite fees, for the consumer to access funds immediately (more on fees below). EWAs with fees require an employee, often lower-wage, hourly employees, to pay to be paid. Although there is a trend towards employers covering the cost of these fees as an employee benefit, these programs still may lead consumers into a cycle of reborrowing and turning to higher priced forms of credit.

Further study of free EWA products is needed, and employers should focus on paying a living wage; consistent, predictable work schedules; employee savings programs; and affordable small dollar installment loans instead of encouraging employees to spend their paycheck early. Regardless of their structure, these products are not risk-free, and fee-based EWA programs should be regulated as credit.

B. Consumer Risks

Although there is a trend towards offering EWA products to employees for free, many still charge fees. These fees are normally $1 to $2 per advance and sometimes have a weekly or biweekly cap. Many providers also limit advances to 50% of expected net wages. Although these fees are smaller than traditional payday loan fees, EWAs are still balloon payment loans that can lead to a cycle of reborrowing and cascading fees. These products are largely marketed and used by hourly, minimum wage workers, which means that even a $1 or $2 fee can make a substantial difference and leave a hole in next week's paycheck.

Consumers may be faced with both an access fee, to access the advance, as well as an inflated expedite fee, to access the advance immediately. These expedite fees can cost consumers $1-2 more than the initial access fee. Nearly 90% of users opt for instant access—not surprising given that these products are marketed towards lower wage workers who struggle to make ends meet between paydays.[72]

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[71]Ryan Deffenbaugh & Veronica Irwin, *Protocol* "Fintech wants to pay workers faster. The CFPB might have a word" (July 25, 2022), https://www.protocol.com/fintech/cfpb-earned-wage-access.

[72] Lauren Saunders, NCLC, *Testimony to Task Force on Financial Technology U.S. House Committee on Financial Services Hearing on "Buy Now, Pay More Later? Investigating Risks and Benefits of BNPL and Other Emerging Fintech Cash Flow Products"* (Nov. 2, 2021), https://financialservices.house.gov/uploadedfiles/hhrg-117-ba00-wstate-saundersl-20211102.pdf.

Further, these fees are inflated well beyond the cost the provider faces for sending the money instantly. For example, many EWA providers have access to the Clearing House's RTP network. The $1 to $2 charged to consumers for instant access severely exceeds the $0.45 cost to the provider for instant transfer.[73] The costs of Visa Direct and MasterCard Send are likely in a similar range.[74]

Repeat usage is common, multiplying the fees even further. Most users rely on these products around 24 times a year, but frequency can span between 12 times to 120 times per year.[75] For the average user, they utilize an EWA twice per month. Another 2021 survey found that 70% of EWA users took out consecutive advances.[76]

Although many workers see the access fee for standard delivery as the price of the product, the expedite fees and repeat usage rack up the price dramatically. At one provider, a worker could pay up to $36 a month at the high end, assuming a repeat user who takes 12 instant accesses in a month.[77] Some providers have even higher cost models.

In addition to the fees, overreliance, and potential cycle of reborrowing, we have additional concerns about the business model. For those providers that require authorization to debit a consumer's bank account, repayment requests can lead to abusive attempts to collect payment and cause consumers to rack up overdraft and NSF fees[78] Additionally, as with many fintech providers, EWA providers compile massive amounts of employment and wage data, which can lead to a host of concerns.[79] For example, data collection can lead to vulnerable concerns being targeted for credit products they cannot afford.

These products are marketed to hourly, minimum, or lower wage workers that are likely to face income volatility from week to week. Regardless of the size of the fee, it's still money that's lost from the consumer's paycheck. Further, accessing their pay early leaves a hole in the following week's budget. We worry that that hole leads to further borrowing, or worse, turning to higher-cost forms of debt. While some users of EWA products have reported lower usage of payday

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[73] The Clearing House, *Simple, Transparent, Uniform Pricing for All Financial Institutions* (last visited Apr. 25, 2022).
[74] *See f*or example, this article noted that Uber drivers paid $0.50 to get instant access to their pay through Visa Direct. Tom Groenfeldt, *Forbes*, "Visa Direct Is The Engine Behind Zelle and Venmo" (Mar. 15, 2019), https://www.forbes.com/sites/tomgroenfeldt/2019/03/15/visa-direct-is-the-engine-behind-zelle-and-venmo/?sh=1814efc58739.
[75] Letter from NCLC & CRL to California Department of Financial Protection & Innovation at 8–12 (Mar. 15, 2021), https://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/CRL_CA_DFPI_EWA_Comments.pdf [hereinafter NCLC & CRL, Letter to CA DFPI (Mar. 2021)].
[76] Financial Health Network, "Earned Wage Access and Direct-to-Consumer Advance Usage Trends" (June 25, 2021), https://finhealthnetwork.org/research/earned-wage-access-and-direct-to-consumer-advance-usage-trends/.
[77] NCLC & CRL, Letter to CFPB (Oct. 12, 2021), re "Concern about prior leadership's finding that certain earned wage access products are not "credit" under TILA" (October 12, 2021), https://www.nclc.org/images/pdf/banking_and_payment_systems/fintech/EWA-letter-to-CFPB_Oct-4-2021.pdf [hereinafter NCLC/CRL, EWA Letter to CFPB (October 2021)].
[78] NCLC/CRL EWA Letter to CFPB (October 2021).
[79] Caitlin Harrington, *WIRED*, "Workers Are Trading Staggering Amounts of Data for 'Payday Loans'" (March 23, 2022), https://www.wired.com/story/payday-loan-data/.

loans and overdraft fees, these products are still a balloon payment loan that can lead to a cycle of reborrowing and cascading fees far higher than the initial ticket price and should still be subject to oversight and monitoring.[80]

C. Recommendations

Under Director Kraninger, the CFPB issued a deeply problematic advisory opinion about EWA products[81] and an approval order to PayActiv for its EWA product under the CFPB's then active, compliance assistance sandbox.[82] CFA joined nearly 100 consumer, labor, civil rights, legal services, faith, community, and financial organizations in advocating that the CFPB revoke this approval order, rescind the advisory opinion and treat these products as credit covered by TILA.[83] Fortunately, this approval order was rescinded earlier this year and in doing so, the CFPB said it planned to "provide greater clarity concerning the application of the definition of "credit" under the Truth in Lending Act and Regulation Z." [84]

We look forward to the CFPB's revisitation of this advisory opinion and urge that they clarify that EWAs provide credit to consumers. Although free EWA products may fall outside of the scope of TILA, those that charge fees are within the scope.[85] Access and expedite fees charged by EWA providers are finance charges that should be presented to consumers in terms of an annual percentage rate.[86] State regulators should also regulate these fee-based earned wage access products as credit covered by all state credit regulations and laws, including usury laws.

Regardless of structure, a product where a third-party advances funds to a consumer ahead of the consumer's payday and is then repaid in some fashion out of the paycheck is a loan. We are greatly concerned about the potential harms of viewing these fee-based earned wage access products as something other than credit, leading to evasion of consumer protection and fair lending laws. Treating EWA products as credit does not mean these products should not exist. It merely means that consumers have the same basic consumer protections and disclosures as they do when using other forms of credit—a concept that is likely already expected. Moreover, failing to regulate them as credit will invite payday lenders and other high-cost lenders to enter this market, which could lead to even more exploitive rates and practices.

In addition, the CFPB should address inflated expedite fees either through TILA or through its authority to protect consumers from Unfair, Deceptive and Abusive Acts and Practices

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[80]DailyPay, "Our Survey Says … DailyPay Saves Employees, On Average, $1,205 Per Year" (May 14, 2020), https://www.dailypay.com/blog/our-survey-says-dailypay-saves-employees/.
[81] CFPB, Advisory Opinion, 12 CFR Part 1026, Truth in Lending (Regulation Z); Earned Wage Access Programs (Nov 30, 2020), https://files.consumerfinance.gov/f/documents/cfpb_advisory-opinion_earned-wage-access_2020-11.pdf.
[82] CFPB, "Consumer Financial Protection Bureau Issues an Approval Order to Facilitate Employee Access to Earned but Unpaid Wages" (December 30, 2020), https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-issues-an-approval-order-to-facilitate-employee-access-to-earned-but-unpaid-wages/.
[83] Letter from NCLC, CRL, CFA, et. al, to Consumer Financial Protection Bureau re "Rescind earned wage access advisory opinion and sandbox approval and treat fee- based earned wage access products as credit" (Oct. 21, 2021), https://consumerfed.org/wp-content/uploads/2021/10/CFA-joins-Groups-in-Urging-CFPB-to-Reverse-Earned-Wage-Actions-that-Threaten-to-Create-Dangerous-Fintech-Payday-Loan-Loopholes-10.12.21.pdf.
[84] CFPB, "CFPB Rescinds Special Regulatory Treatment for Payactiv" (June 30, 2020), https://www.consumerfinance.gov/about-us/newsroom/cfpb-rescinds-special-regulatory-treatment-for-payactiv/.
[85] For further legal analysis *see* NCLC/CRL, EWA Letter to CFPB (2021).
[86] *Id.*

(UDAAP). We also recommend that the CFPB further supervise these fee-based EWA providers and conduct research on the impact of EWA programs, especially on low-income consumers and their ability to build wealth and achieve financial security.

Fintech providers that purport to lend earned wages and seek access to a consumer's bank account, but are not employer integrated, are essentially a payday loan and should be supervised and regulated as such.

3. The "Tip" Model, used to pay for earned wage access, overdraft protection, cash advances, and loans:

   A. Introduction

Increasingly, nonbank fintech providers are charging consumers "tips" for financial products, including faux early wage access, "peer-to-peer" cash advances, overdraft protection, and other forms of credit.[87] Although providers claim that these fees are purportedly voluntary, tips are simply disguised finance charges and should be treated as such.

Certain nonbanks offer consumers enticing promises of fee-free overdraft protection, claiming that overdraft fees have gotten out of hand. However, the overdraft protection offered still comes at a price—consumers are asked to "tip" to help other users make ends meet or pay for the cost of the service.[88] Another provider offers consumers cash advances for no interest, no monthly fee, and no credit check, "unlocking" higher cash advances each time they use the service. However, consumers are asked to leave a "small optional tip" to help cover costs of the product.[89] Some providers collect tips in addition to subscription and expedite fees.[90] Other providers charge consumers tips for payday advances that claim to be "earned wage access" products but in actuality have no connection to employer payroll or an employee's actual earnings.[91]

By labeling these finance charges as "tips," financial providers are attempting to mask finance charges, evade interest rate limits and other consumer protection laws, and disguise overdraft fees. These tips are not truly voluntary as companies use a number of means to ensure that the consumer tips. The label does not change the cost to consumers; instead, it allows providers to disguise the true cost of credit, deceiving consumers into larger finance charges than originally disclosed.[92]

   B. Consumer Risks

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[87] *See* NCLC, CFA, CRL, and Americans for Financial Reform (AFR), Comments to CFPB re "Request for Information Regarding Junk Fees Imposed by Providers of Consumer Financial Products and Services," at 46-47 (May 2, 2022), https://consumerfed.org/wp-content/uploads/2022/05/Groups-Submit-Comments-in-Response-to-CFPBs-Request-for-Information-Regarding-Fees-Imposed-by-Providers-of-Consumer-Financial-Products-or-Services-5.2.22.pdf [hereinafter NCLC, CFA, et. Al, Junk Fee Comments to CFPB (May 2022)].

[88] *See* SpotMe, https://www.chime.com/spotme/ (last visited September 6, 2022).

[89] *See* Instacash, https://www.moneylion.com/instacash/ (last visited September 6, 2022).

[90] *See* https://www.joinklover.com/ (last visited September 6, 2022).

[91] *See* https://www.earnin.com/ (last visited September 6, 2022).

[92] For sample of complaints regarding tips, *see* Gittleman, Statement re BNPL (March 2022).

These "tips" are not truly voluntary due to a variety of techniques companies use to make it difficult not to tip. Although there seems to be an assumption that so-called tips are voluntary and consumers must opt into them, companies are utilizing a variety of strategies to make it difficult not to tip or to make the consumer feel compelled to tip. Strategies include adding a default tip that must be removed each time; or denying or reducing future credit if a consumer fails to tip enough. Further, one colleague recounted that he found it impossible to undo the default tip option even after deleting and reinstalling the app. Even without manipulative strategies, consumers are more likely to feel compelled to tip for fear of being treated differently or denied access in the future.[93]

Tips are inherently deceptive and deceitful. Tips are not often included in product marketing and promotions or even in information about fees in the product terms and conditions. This leads consumers to believe that these products are free, especially when promoted with promises of no interest or monthly fees. By labeling a finance charge as a tip, providers are relying on the obligation that consumers often feel when tipping another human after completion of a service, like in restaurants or other service industries. Some providers further encourage that feeling by labeling tips as "lender appreciation" tips.[94] Other providers make disingenuous statements about how tips support a "community" or will help other "users make ends meet" or deceitfully labeling tips as "donations."

However, these tips do not go to another human being and are not in appreciation of a service—instead, they go to the company's bottom line. Further, tips are added to the repayment amount before the transaction is fully completed and tips are paid via the authorization to debit a user's account per user contracts. Consumers do not tip after the service has taken place in appreciation for good service which might make them more voluntary. The label does not change the inherent nature of these charges; it simply allows providers to claim otherwise.

Tips increase the cost of credit, can add up quickly, and consumers have no way to compare that cost with other forms of credit. The "tip" model takes advantage of consumers' lack of awareness of how tips add up, especially since small tips can add up to a high cost over time nearing payday loan pricing and thus, can make it easier for consumers to get sucked into the cycle of debt. For example, a voluntary tip can be near $15 per $100, similar pricing to that of payday loans — one provider encourages users to leave a tip of $0 to $14 on a $100 weekly loan, which would equate to 730% APR.[95] Another provider was recently issued a cease-and-desist order for charging tips equivalent to 43% to 4280% APR, far above the legal rate in most states.[96]

Not only is this rate illegal in states throughout the country, but the pricing may also look cheap to consumers on its surface because it's portrayed as a flat fee rather than APR. It is marketed in ways to hide the true cost or dismiss the APR as irrelevant due to the shorter loan cycle. Plus, tip

[93] For further analysis of whether tips are 'voluntary,' *see* NCLC & CRL Letter to CA DFPI (Mar. 2021) at 8-12.
[94] *See* https://solofunds.com/ (last visited September 6, 2022).
[95] Kevin Dugan, *NY Post*, "Cash-advance App Earnin Gets Subpoenaed by NY Regulator: source" (Mar. 29, 2019), https://nypost.com/2019/03/28/cash-advance-app-earnin-gets-subpoenaed-by-ny-regulator-source/.
[96] Penny Crossman, *American Banker*, "Connecticut slaps fintech Solo Funds with cease-and-desist order" (May 11, 2022), https://www.americanbanker.com/news/connecticut-slaps-fintech-solo-funds-with-cease-and-desist-order [hereinafter Crossman, *American Banker*, Solo Funds (May 2022)].

models rely on the consumers' assumption that they will not be able to access the product in the future if they don't tip.[97]

But these high charges for smaller loans result in exorbitantly high APRs, regardless of whether they are portrayed to consumers in that way. Regardless of the label, advances that charge tips are balloon payment loans, with repayment on the next deposit or other equally short schedule. Like other balloon payment loans, they can lead to dependency or a cycle of reborrowing, and high rates of overdraft and NSF fees.

Finally, consumers have no way to compare the cost of tips to other forms of credit because they are often added late in the application process and are not presented in terms of APR, like with other credit sources. These tactics help disguise the true cost of credit and the potential impact on borrowers.

C. Recommendations

Even if voluntary, tips could be considered finance charges under the Truth in Lending Act (TILA) and therefore, subject to state usury laws and fair lending laws. Regardless of how the charge is labeled to a consumer, the cost remains the same. Most borrowers likely do not understand how high an interest rate they are paying, and even if some borrowers are able to translate the fees or tips into APRs, these fees should still be subject to consumer protection laws. Labeling interest as a "tip" does not change its cost to the consumer and should not exclude it from usury law.

In addition, the CFPB should supervise tip-based cash advances as payday loans under its supervision authority. Providers promote themselves as alternatives to traditional payday loans, with some even marketing borrowing with "no debt traps."[98] The CFPB should use its supervision authority to ensure that the opposite is not the case.

Finally, the CFPB should enforce the MLA's 36% rate cap against tip-based credit products. Regardless of the label, tips are finance charges and should be subject to the MLA's interest rate cap that covers active-duty service members and their families.

State regulators should aggressively enforce their banking regulations and usury laws. For example, Connecticut and New York regulators have each accused fintech providers of claiming tips are voluntary, but then only providing loans to those consumers that pay tips. These regulators have argued that these providers failed to apply for the proper lending and collections licenses and failed to disclose the tips.[99] Other state regulators should follow suit.

Failing to regulate these so-called "tips" as finance charges will enable dangerous erosions of fair lending laws and usury laws across the country. The CFPB should provide much needed oversight of finance providers that utilize the dangerous tip model and ensure that these providers comply with consumer protection laws and are not engaging in unfair, deceptive or abusive acts and practices.

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[97] For consumer examples of tip models, *see* NCLC & CRL, Letter to CA DFPI at 8–12 (Mar. 2021).
[98] *See* https://solofunds.com/borrow/ (last visited September 6, 2022).
[99] Crossman, *American Banker*, Solo Funds (May 2022).

4. Training Repayment Agreement Provisions

A. Introduction

Training Repayment Agreement Provisions, or TRAPs, are a form of employer-driven debt that can trap consumers in tens of thousands of debt with high interest rates and the threat of third-party debt collection. TRAPs require employees who receive on-the-job training to pay back the alleged cost of training to their employer if they try to leave their job, either voluntarily or involuntarily, before an arbitrarily determined date ranging from months to years after employment.[100] The training is often of questionable necessity and quality, and if the agreement is enforced, traps consumers in tens of thousands of dollars of debt.[101] For some workers, the potential cost of the agreement is greater than their yearly salary.[102] If workers bound by a TRAP attempt to leave their job before the predetermined date, they can face exorbitant interest rates, attorney and collection fees, and withholding of pay or retirement savings.[103] Even if not enforced, the threat of this debt and ensuing consequences function as a deterrent for leaving a job. These provisions keep employees in often low-paying jobs with poor working conditions.

The use of TRAPs is widespread and growing more commonplace. These provisions are buried deep inside employment contracts of many major employers, including trucking companies, hospital operators, retailers, roofing contractors, financial services firms, airlines, and more. The Student Borrower Protection Center estimates that companies that collectively employ more than one in three private-sector workers use TRAPs in employee contracts.[104]

TRAPs hinder workplace mobility which can exacerbate disparities. TRAPs are used in jobs that are disproportionately held by women, immigrants, and Latino and Black employees. With the threat of debt hanging over their head, employees can feel forced to stay in substandard working conditions with poor pay. TRAPs can disempower workers from fighting disparities, undermine their bargaining power, and limit their ability to use mobility as a solution.

B. Recommendations

First off, we appreciate Chairman Sherrod Brown, Chairwoman Patty Murry of the Senate Health, Education, Labor, and Pensions Committee, and their colleagues writing to the CFPB to urge them to provide much needed oversight of TRAPs.

Recently, CFA joined a coalition of groups in response to the CFPB's request for information about employee driven debt. The coalition urged the CFPB to have an important role in

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100 SBPC, Trapped at Work: How Big Business Uses Student Debt to Restrict Worker Mobility (July 2022), https://protectborrowers.org/wp-content/uploads/2022/07/Trapped-at-Work_Final.pdf [hereinafter SBPC, Trapped at Work (July 2022)].

101 *Id.*

102 *Id.*

103 *Id.*

104 *Id.*

protecting consumers against industry abuses where these provisions exist.[105] First, the CFPB should vigorously enforce the prohibition against unfair, deceptive, or abusive acts and practices (UDAAPs), and other essential consumer protection laws such as TILA and the Equal Credit Opportunity Act (ECOA), to protect against industry abuses where these provisions currently exist. In addition, the CFPB should routinely supervise debt collectors that collect debts arising from TRAPs. Finally, the CFPB should exercise its market monitoring authority to identify consumer harm before it happens.

In addition, the Federal Trade Commission (FTC) should use its broad authority to protect consumers from unfair and deceptive labor practices. The FTC has broad authority to interpret "unfair methods of competition," and it should use that authority to prohibit practices like TRAPs that hold back labor competition.

Finally, the Department of Labor, state agencies, and state policymakers have a responsibility to protect consumers from these abusive provisions, as TRAPs are often used to evade existing state and federal worker protections, including state-level bans on noncompete clauses.

5. Rent-a-Bank Loans

A. Introduction

Since the American Revolution, states have had the power to set their own interest rate caps Today, more than 45 states and the District of Columbia have interest rate caps on installment loans.[106] However, due to consistent deregulation, banks are largely exempt from state interest rate caps. High-cost lenders are exploiting that exemption to evade state interest rate laws. Multiple predatory lenders launder their triple-digit loans through rogue FDIC-supervised banks, even in states where those rates are illegal.

On a bipartisan basis, Congress recently expressed its strong disapproval of predatory rent-a-bank schemes when it adopted a Congressional Review Act resolution to overturn the Office of the Comptroller of the Currency's (OCC) "fake lender" rule.[107] This bipartisan legislation was also supported by 25 State Attorneys General, the Conference of State Bank Supervisors, the National Association of Consumer Credit Administrators, the National Association of Federal Credit Unions, Credit Union National Association, 138 scholars from 44 states, and more than 400 civil rights, community, consumer, disability rights, faith, housing, labor, legal services, senior rights, small business, and veterans organizations from all 50 states. [108]

In signing the resolution, President Biden, stated:

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[105] SBPC, CFA, et. al, Comments to CFPB re Request for Information Regarding Employer-Driven Debt (Docket No. CFPB-2022-0038) (September 9, 2022), https://consumerfed.org/wp-content/uploads/2022/09/Employer-Driven-Debt-RFI-Coalition-Comment.pdf.

[106] NCLC, *State Rate Caps for $500 and $2,000 Loans* (July 2021), https://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/FS_State_Rate_Caps_2021.pdf.

[107] Sylvan Lane, *The Hill*, "Senate votes to repeal OCC 'true lender' rule" (May 11, 2021), https://thehill.com/policy/finance/552992-senate-votes-to-repeal-occ-true-lender-rule/.

[108] Stop the Debt Trap Coalition, *Who Supports Overturning the OCC's "Fake Lender" Rule?*, (April 2021), https://consumerfed.org/wp-content/uploads/2021/04/Who-Supports-the-CRA.pdf.

> "The … bill will protect borrowers against predatory lenders. In many states, these lenders are kept in check by caps on how much interest they can charge, but some loan sharks and online lenders have figured out how to get around these limits … -- by using a partnership with a bank to avoid the state cap and charging outrageous interest… -- some as high as 100 percent interest, which is astounding… "These are so called "rent-a-bank" schemes. And they allow lenders to prey on veterans, seniors, and other unsuspecting borrowers... trapping them into a cycle of debt. And the last administration let it happen, but we won't."[109]

Despite this bipartisan rebuke, rent-a-bank schemes persist. We are currently aware of six rogue FDIC-supervised banks that are helping multiple predatory lenders peddle loans with interest rates as high as 225% APR, even in states where that rate is illegal.[110]

B. Consumer Risks

Complaints to the CFPB about these predatory lenders illustrate the abusive and deceptive practices used by these companies.[111] Consumers have cited rates of 96% to 189%, sometimes in states where those rates are illegal and even to servicemembers, veterans or their family members. Rates this high create payments for months and years with little reduction to the loan balance.

According to consumer complaints, the application process is a nightmare from start to finish. Consumers are lured in with promises of full interest rebates if paid in 90 days, but then find it difficult to avoid interest. Further, consumers complain of only having access to an application on a cellphone where it's difficult to read the fine print, which includes critical information about high interest rates and other terms. Plus, consumers complain of administrative errors which can lead to deprivation of the rebate or missed payments.

Once the loan is taken out, paying it back is difficult with consumers complaining of improper processing of automatic payments. This can lead to late payments or inability to get the interest rebate. When consumers run into these hardships, they are faced with little or no response from disputes and rude or unhelpful customer service.

Moreover, consumers face harm to their credit reports, including when loans are reported incorrectly or fully paid back, and difficulties from debt collection, with collectors even failing to

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[109] Remarks by President Biden Signing Three Congressional Review Act Bills Into Law: S.J.RES.13; S.J.RES.14; and S.J.RES.15 (June 30, 2021) https://www.whitehouse.gov/briefing-room/speeches-remarks/2021/06/30/remarks-by-president-biden-signing-three-congressional-review-act-bills-into-law-s-j-res-13-s-j-res-14-and-s-j-res-15/.

[110] NCLC, High-Cost Rent-a-Bank Loan Watch List (last visited September 3, 2022), https://www.nclc.org/issues/high-cost-small-loans/rent-a-bank-loan-watch-list.html.

[111] *See* Stop the Debt Trap Coalition, *Predatory Puppy Loans by TAB Bank and EasyPay Financ*e (February 2022), https://www.nclc.org/images/pdf/high_cost_small_loans/IB_Easypay_Puppy_Loans_Feb22.pdf;
Stop the Debt Trap Coalition, *Predatory Auto Repair Loans By TAB Bank and EasyPay Finance* (May 2022), https://consumerfed.org/wp-content/uploads/2022/05/Financial-Services-TAB-Bank-Auto-Repair-Loan-Report-5-11-22.pdf;
Stop the Debt Trap Coalition, *Predatory Lenders TAB Bank and EasyPay Finance Harm Veterans and Military Servicemembers with Loans up to 189% APR* (May 2022), https://consumerfed.org/wp-content/uploads/2022/05/Predatory-Lenders-TAB-Bank-and-EasyPay-Finance.pdf;
Stop the Debt Trap Coalition, *Congress Must Protect Consumers from Predatory Lending* (2021), https://consumerfed.org/wp-content/uploads/2021/03/Rent-A-Bank-Stories_By-State-2021.pdf.

correct credit reports after loans are paid in full. As is clearly elucidated through complaints to the CFPB and lawsuits, consumers are faced with deceptive practices, predatory rates, and no recourse after taking out these loans.

C. Recommendations

Interest rates are the most effective and straightforward way to protect consumers from predatory lenders. Although most states have interest rate caps, the prevalence of rent-a-bank loans illustrate the need to enact uniform, national protections. Congress should pass the Veterans and Consumers Fair Credit Act, introduced in the Senate by Senator Jack Reed (RI), Senator Chris Van Hollen (MD), and Chair Sherrod Brown (OH) with companion legislation in the House of Representatives introduced by Representatives Chuy García (IL) and Glenn Grothman (WI). This legislation would extend the MLA's 36% interest rate cap to veterans, Gold Star Families, unactivated reservists, and all Americans.

Enacted in 2006, the MLA institutes an interest rate cap inclusive of add-ons and fees on consumer loans for active-duty service members and their families and has curbed predatory lending for servicemembers.[112] Indeed, before it took effect, 1,577 servicemembers sought help from the Navy-Marine Corps Relief Society in 2004 to pay off predatory loans, but by 2018 that number had dropped to 3.[113]

A national rate cap is strongly supported by the American public with polls consistently showing that 70% of voters across party lines support capping interest rates at no higher than 36%.[114] In addition, every ballot measure held on the subject in recent years has passed with broad support, including most recently, in Nebraska where more than 80% of voters voted in favor.[115] Ballot measures have also been passed in Colorado, Montana, and South Dakota. Further, this legislation is supported by more than 220 organizations and academics representing all 50 states and the District of Columbia.[116]

The Veterans and Consumers Fair Credit Act would:

- Prevent hidden fees and loopholes, as the 36% rate cap would include not just periodic interest but also fees and add-ons. Loopholes in TILA's annual percentage rate undermine cost transparency and embolden evasions.

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[112] Department of Defense, *Report on the Military Lending Act and the Effects of High Interest Rates on Readiness*, (June 30, 2021), https://finred.usalearning.gov/assets/downloads/FINRED-MLA_ReportEffectsHighInterestRatesOnReadiness-May2021.pdf.

[113] Navy-Marine Corps Relief Society, Assistance provided to Active Duty and Retired Navy and Marine Corps Personnel Due to Pay Day Loan Involvement (2018), https://static1.squarespace.com/static/556718b2e4b02e470eb1b186/t/5c7d3ec0e79c70579f44162c/1551711937100/.

[114] CRL *Bipartisan Support for Stopping Predatory High-Interest Loans* (February 3, 2020), https://www.responsiblelending.org/research-publication/new-poll-bipartisan-support-stopping-predatory-high-interest-loans.

[115] Megan Leondhardt, *CNBC*, "Nebraska becomes the latest state to cap payday loan interest rates" (Nov 4, 2020), https://www.cnbc.com/2020/11/04/nebraska-becomes-the-latest-state-to-cap-payday-loan-interest-rates.html.

[116] CFA, NCLC, AFR, CRL, et. al, Letter to House Financial Services Committee re "Support for Veterans and Consumers Fair Credit Act" (September 27, 2021) https://consumerfed.org/wp-content/uploads/2021/11/Ltr-to-HFSC-in-Support-of-VCFCA-9.212.pdf.

- Maintain low industry compliance costs by simply expanding rules enacted by the MLA that are already in effect.
- Uphold stronger state protections. 36% is a relatively high rate and is only appropriate for smaller loans and as an upper limit. Half of U.S. states have interest rate caps lower than 36%, which will not be impacted by this bill as it allows for state law that provides greater protections to consumers
- Cover all lenders, including banks, which would protect consumers from evasions like those described above.

In addition, the FDIC should stop permitting its supervised institutions to front for predatory lenders evading state interest rate limits.[117] These schemes pose a range of legal, safety and soundness, and reputational risks to bank, including possible violation of several federal laws, including the MLA, Community Reinvestment Act (CRA), ECOA, EFTA, FDCPA, and the Fair Credit Reporting Act (FCRA). Not only are rent-a-bank schemes an abuse of the FDIC's bank charter, but they also lead to abusive lending practices by separating lender and borrower incentives. The FDIC has the tools available to end predatory rent-a-bank schemes, as it did roughly two decades ago, when it, and the other bank regulators, used its supervisory and enforcement authorities to stop banks from helping short-term payday lenders evade the law.[118]

6. Financial Inclusion

CFA is particularly concerned about products that claim to be promoting financial inclusion but, in reality, do quite the opposite. Without meaningful, holistic underwriting, affordable repayment options, and price transparency, products may do more to exacerbate financial exclusion rather than promote financial inclusion.

Many of these products use promises of limited or no credit checks which may entice consumers with thin or limited credit histories. Other products are aimed at consumers who are struggling to make ends meet or who struggle to access mainstream credit. However, failing to properly underwrite loans will simply lead to unaffordable debt for consumers.

7. Conclusion

The Consumer Federation of America appreciates the Senate Committee on Banking, Housing, and Urban Affairs for holding this hearing and the opportunity to testify. We look forward to working with the Committee to meaningfully address the potential risks that emerging fintech products pose for consumers.

[117] NCLC, CFA, et. al, Letter to Chair Martin Gruenberg (February 4, 2022), https://consumerfed.org/wp-content/uploads/2022/02/FDIC-rent-a-bank-letter-2022-2-4-final-corrected.pdf.
[118] *Id.*