Reinvestment PARTNERS
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November 7th, 2016

Director Richard Cordray
Consumer Financial Protection Bureau
1275 First Street, NE
Washington, DC 20002

RE: Request for Information on Payday Loans, Vehicle Title Loans, Installment Loans, and Open-End Lines of Credit; Docket No. CFPB-2016-0026 RIN 3170-AA40

Dear Director Cordray:

Please accept this comment in response to the Bureau's FFI on Payday Loans, Vehicle Title Loans, Installment Loans, and Open -End Lines of Credit.

Reinvestment Partners is a non-profit group with a mission to seek economic justice. We achieve this goal using an interdisciplinary approach working with people, places, and policy. We provide direct services to consumers, either to protect them from financial harm or to improve their financial health. We are improving our immediate community through real estate development. We support small businesses working in our local food systems. In our policy work, we advocate on behalf of lower-income consumers and communities of color through efforts to promote systematic reforms to the financial system.

We support the Bureau's intention to examine how these products may raise potential consumer protection issues that were not otherwise addressed by CFPB 2016-0025.

We will focus primarily on three products outlined in the RFI: credit insurance, deferred interest contracts, and non-file insurance.

Credit Insurance

While credit insurance policies do offer protection against risk, the claims experiences do not justify the price of their premiums. Millions of consumers buy credit insurance policies, but even given the scale of the industry, competitive pressures have not worked.

In its study of insurance add-ons, Great Britain's Financial Conduct Authority ("FCA") said that the sale of these products was enabled through the fundamentally imbalanced relationship between retailer and consumer. In reviewing their research on payment protection insurance, the FCA said:

- 58 percent of those buying personal property insurance ("guaranteed asset protection" in their nomenclature) never considered a different policy.
- 69 percent of buyers could not name the price of the insurance.
- 19 percent forgot that they had purchased the product after three months.
- Customers usually paid more than twice as much for the product when they purchased it as an add-on compared to when they bought asset protection on a stand-alone basis.

The FCA found that "the add-on mechanism is associated with weaker engagement with purchase decisions and therefore weaker pressure on sellers to offer good value and high-quality products. This increases the point-of-sale advantage enjoyed by those selling general insurance products as an add-on and provides an opportunity and an incentive for firms to sell products that might not meet consumers' needs or charge high price markups that can lead to poor value for consumers.[1] "

All of the characteristics noted above by the FCA are also present in the United States. The absence of meaningful supervision of credit insurance stands out, given its widespread use and substantial expense. Insurers wrote more than one million credit insurance and property credit insurance policies in North Carolina in 2013.

POLICY TYPE	PREMIUMS	NUMBER OF POLICIES	AVERAGE PREMIUM
Credit Life	$ 23,021,792	425,175	$ 54.15
Credit A & H	$ 38,477,614	239,697	$ 160.53
Credit IUI	$ 33,767,801	176,091	$ 191.76
Credit Property	$ 22,704,518	360,096	$ 63.05
SUMS	*$ 117,971,725*	*1,201,059*	

Source: NC Commissioner of Banks, Consumer Finance Annual Report

[1] Financial Conduct Authority. "General Insurance Add-Ons: Provisional Findings of Market Study and Proposed Remedies." March 2014.

Some lenders have reported that they sold a credit insurance policy to more than four of ever five borrowers[2]. Although this market has reached scale, borrowers do not enjoy bargaining power, but instead are price-takers.

We have concerns that consumers may be led to believe that lenders condition the approval of a loan on the purchase of one or more credit insurance policies.

The price of credit insurance exceeds the protection that it confers to consumers against risk. From the consumer's perspective, life insurance, medical insurance, and property insurance all deliver better loss ratios results. [See Appendix One] The loss ratio statistic, recognized as the most appropriate metric for gauging value, supports our contention. The following inputs are used to derive a loss ratio:

Loss Ratio = Claims paid/earned premiums

In most insurance sectors, loss ratios exceed 75 percent (see Chart One). The remainder of premium revenues are devoted to administrative expense, commissions, and return on investment. The next table compares the aggregated loss ratios of different insurance products:

Year	Credit		Property	Medical	
	Life	Accident & Health		Individual & Group	Medicare Supp.
2009	45.1	43.4	72.4	84.7	79.6
2010	47.6	45.2	73.7	83.9	78.6
2011	48.5	41.8	79.5	83.1	79.8
2012	45.7	41.2	74.4	84.4	77.5
2013	47.7	36.7	67.1	84.4	76.2

Source: National Association of Insurance Commissioners

These differences are dramatic. Two related factors explain this situation.

First, we believe that low loss ratios owe to the fact that insurers pay high commissions. While commissions are standard practice in many insurance markets, a standard fee charge is usually less than ten percent of the earned premium. But in credit insurance, overall commission expenses can sometimes exceed fifty percent. Some insurers have reported years where claims payouts were less

[2] Conn's HomePlus Annual Report 2012 10-K, page 17:

than twenty percent of earned premiums. Often, commission expense exceeds costs for paying claims. The next table details the operating expenses of Fortegra Financial during fiscal years 2011 through 2013.

	2011	2012	2013
Net Losses/Loss Adjustment Expense	**$37,949**	**$40,219**	**$41,567**
Member benefit claims	$4,409	$4,642	$46,019
commissions	**$126,918**	**$128,741**	**$154,606**
personnel costs	$26,021	$28,475	$39,487
other operating expenses	$23,739	$24,233	$35,117
Depreciation and Amortization	$2,662	$3,275	$4,858
Amortization of intangibles	$2,819	$2,742	$5,527
interest expense	$4,690	$4,334	$3,621
gain/loss on sale of subsidiaries	$ 477	$ -	$(402)
TOTAL	$229,684	$236,661	$330,400

Source: Fortegra Financial 10-k, SEC

Over this three-year period, claims expenses in Fortegra's Payment Protection Division amounted to less than 22 percent of operating expense. Commissions were Fortegra's largest cost center. In all, they represented more than 51 percent of costs.

Florida Insurance Commissioner Tom Gallagher made this comment:

> What I've seen is the profit isn't sitting there in the insurer as much as it's sitting there in the marketer. You all have had tremendous contests with each other on how much can you give away. And the problem is, in my opinion, that we need to have the product available, it needs to be sold to people that want it, but it needs to be sold without these huge commissions there that are encouraging sales, in some cases, where it maybe shouldn't be sold and maybe isn't even wanted, even though most of our states says that … it's certainly a choice. The bottom line is, in many cases, that people don't know it's a choice and that's because of these forty to sixty percent commissions[3].

[3] National Association of Insurance Commissioners, Hearing on Credit Insurance, November 9th, 1990. Washington, DC. http://naic.org/documents/prod_serv_special_cre_cb.pdf

Because lenders consent to sell policies from only one insurer, borrowers are vulnerable to coercive business practices. Exclusive arrangements remove competition from the marketplace and naturally lead to higher policy premiums. Exclusivity at the point-of-origination undermines consumer choice. But it also increases the chance that lenders will be able to offer policies that undermine consumer protections.

Gallagher's comments hint at another concern – that the sale of credit insurance often stems from aggressive efforts to convince consumers to buy products that they do not need.

Coercion at the Point-of-Sale

The CFPB should investigate the sale of credit insurance for instances of where lenders may have coerced borrowers to buy products that they otherwise would have not chosen to purchase. If it is the case that pick-up rates vary significantly at different lenders or across different stores operating under the same non-bank lender, then it could be the case that some managers are giving the impression to borrowers that the approval of a loan is conditioned upon the purchase of a credit insurance policy. If the percentage of loans sold with a credit insurance policy is higher in low usury cap states, then investigators should determine if there are corporate policies in place to force borrowers to buy insurance.

Additionally, we believe that there should be a 5-day waiting period between the origination of a loan and the issuance of a new credit insurance policy. Creating a waiting period would have the effect of introducing competition to the marketplace. Lenders would still be able to sign exclusive contracts with insurers, but the new environment would give consumers time to comparison shop for a better policy.

The Expense of Credit Insurance Increases Costs of Borrowing

We reviewed 38 contracts made by seven different installment lenders. In 24 of those 38 cases, consumers purchased a credit insurance policy. Twelve bought three or more. Among those who did take out an insurance policy, the average state APR of their loan was 30.3 percent.

Even though credit insurance acts as a barrier against loan default, the premium cost (s) is not included in the calculation of an APR. We are concerned that the sale of credit insurance is being used to evade state usury caps. The next table shows how much the cost of borrowing goes up when a consumer uses one of these products. In most instances, the premium expenses have pushed the real costs of borrowing above 36 percent.

This data comes from actual contracts submitted by the installment lenders as part of evidentiary discovery in federal bankruptcy courts.

State	Loan Amount	CI Premiums	TILA APR	Interest Rate with CI
MS	$1,667	$308	33.3%	64.0%
TX	$9,079	$2,368	16.8%	60.2%
IL	$10,800	$2,800	36.0%	57.2%
LA	$1,447	$88	35.9%	54.6%
FL	$2,476	$457	29.7%	52.9%
TN	$4,267	$676	28.8%	50.5%
GA	$5,176	$680	36.6%	48.5%
SC	$2,212	$212	36.0%	47.5%
LA	$1,554	$95	35.8%	46.4%
AZ	$4,577	$577	35.8%	46.2%
CA	$4,235	$435	35.0%	43.9%
VA	$3,337	$325	33.4%	42.8%
IL	$10,444	$2,293	25.6%	41.4%
KY	$2,153	$236	26.9%	39.7%
VA	$6,591	$546	32.8%	39.7%
TX	$6,419	$919	28.6%	38.5%
AL	$5,318	$253	32.4%	37.8%
LA	$5,961	$661	30.1%	37.6%
TX	$4,409	$410	30.4%	37.3%
LA	$2,129	$125	32.2%	37.1%
MO	$6,140	$348	31.5%	35.2%
TX	$6,072	$1,177	18.7%	35.0%
IL	$10,324	$324	26.1%	28.1%

Source: contracts retrieved from PACER by Reinvestment Partners in 2016.

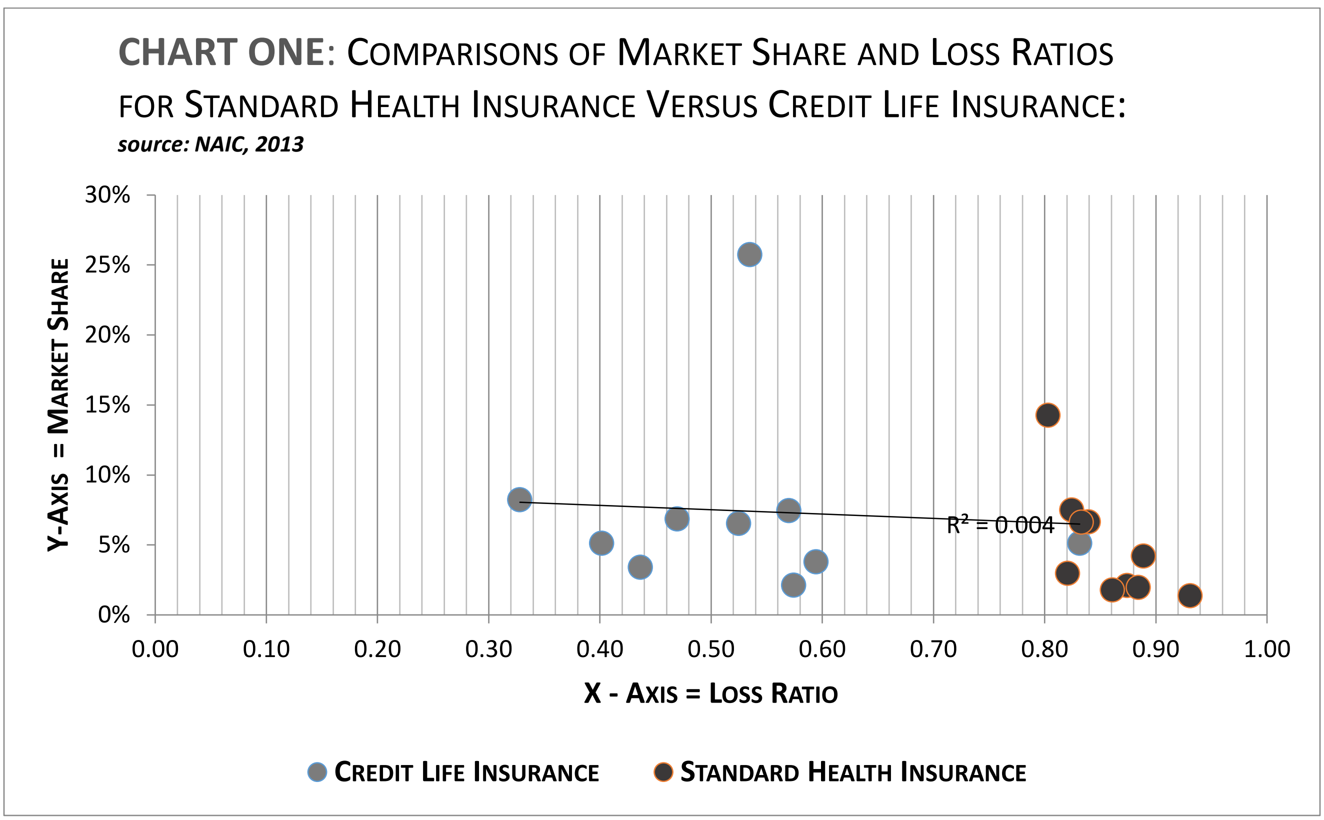
These are real contracts from consumers in this survey. The survey shows that they spent from between $95 to $2,800 on credit insurance policies. Additionally, credit insurance raised the overall cost of credit by 13.2 percentage points. On two occasions, rates went up more than 30 percentage points.

In each case, lenders submitted these contracts to courts to support their assertion that the borrower accepted the proceeds from a loan that he or she had no intention of repaying. For the most part, the borrowers never made a single payment. Most (20 of 38) were taking out a new loan to refinance an existing loan. In some cases, the borrowers were refinancing prime-rate loans with new funds sourced from loans with interest rates of more than thirty percent. To do so, the borrowers were consenting to origination fees, document preparation fees, points, prepaid finance charges, and a host other one-time transaction costs.

While it may or may not be true that the borrower had the intent to repay the loan, we think it is important to consider how these defaults underscore that the lender did not adequately review the ability of the borrower to repay these loans. In most cases, the borrower made one or zero payments before he or she declared bankruptcy.

Competition will not remedy the situation

Competition does not influence consumer cost. The interests of retailers align against those of their customers. As a result, the natural consequence is for retailers to offer insurance based on the size of the referral commission. Chart One shows how prices in the market have not responded to risk. The chart uses loss ratios as a means of relating risk to premium price. Theoretically, loss ratios in a competitive market would drive market share. Market share would grow as loss ratio values fell. A company that priced its policies too high would lose market share. Competition is a function of the slope of the line. A competitive market would have a graph with a line that dropped from left to right; those insurers with lower loss ratios (x-axis) would have higher market shares (y-axis.)



Two important points: first, competition is insensitive to price. Second, loss ratio rates are significantly lower for credit life insurance than they are for individual and group medical insurance.

To highlight the failure of this subset of credit insurance products to track with market forces properly, consider how little of a difference the price makes regarding market share. In 2013, Pavonia Life Insurance Company of Michigan reported a loss ratio of 86.7 percent in North Carolina on its credit accident and health policies. This rate is well above the average in the market. If there was a transparent and competitive market in place, then consumers should have been flocking to Pavonia Life. But in spite of that, Pavonia Life had a market share of just 3.3 percent. On the other hand, Life of the South and Merit Life Insurance Company had low loss ratios but substantial market shares: They reported loss ratios of 24.8 and 26.3 percent, but enjoyed market shares of 15.0 and 13.3 percent, respectively[4].

The Bureau could consider addressing the cost of credit insurance by following a solution implemented in North Carolina in 2011. Beginning in the second half of 2011, North Carolina changed its rules governing the pricing of credit involuntary unemployment insurance. The effect of the change has been to re-orient insurance pricing away from market-wide prima facie rates and toward ratings that are driven by actual loss ratios on an insurer-by-insurer basis. According to staff at NC DOI, North Carolina is the only state to implement this kind of rule for pricing on credit involuntary unemployment insurance.28

Before the change, insurers had two choices on how to comply with pricing on credit involuntary unemployment insurance. On the one hand, insurers could demonstrate a loss ratio of 60 percent or more, based upon a rolling average over the three years ending in the prior year of the review. Alternatively, the insurers could opt to charge a rate at or below the maximum prima facie rate.

If an insurer chose to demonstrate compliance through claims experience (loss ratio), then they were required to submit evidence of that record. If they opted for the prima facie route, then empirical evidence was not necessary. It would be the rare exception when an insurer rejected the option to price under the prima facie approach. All insurers were reporting loss ratios below 60 percent, an outcome which suggests it was much more profitable to use the prima facie rate option. It was not uncommon for insurers to report IUI loss ratios below 30 percent.

[4] 4 NAIC, 2014 Credit Experience Report (Credit Life 5-Year Aggregate Loss Ratio 2010-4)

The language used to write the change, which did not have to go through the legislative process, was very narrow. The NCGA revised a section from NCAC 16.0501(b) to state: "The premium rates charged for credit unemployment insurance shall be reasonable in relation to the benefits provided as indicated by a minimum annual incurred loss ratio of 60 percent[5]."

If an insurer reported a low loss ratio over the previous three-year period, then the agency could set the future prima facie rate for that company to a level that would have produced the desired minimum loss ratio during the prior three-year period. The idea is rooted in fairness. If claims are low, then premiums should follow suit. If claims are high, then there is a legitimate basis for premiums to increase. The rate should reflect the risk – not the commission expense.

The new approach has forced many insurers to lower involuntary unemployment insurance premium prices. It has already saved consumers millions – probably an amount close to $2 million annually. It will take additional time to fully understand 11 NCAC 16.0501(b)'s ultimate impact. So far, the new rule has been in place during a period when unemployment rates and layoffs were in decline. We do not know how the model might perform at a time when unemployment was higher.

Potential Consumer Harm From Default Interest Rates, Late Payment Penalties, Teaser Rate Loans, or Other Back-End Pricing Practices: **Deferred Interest on Installment Loans not regulated by the CARD Act or by CFPB 2016 0025**

Deferred interest programs may create incentives for borrowers to take out loans that they cannot afford. Some lenders offer deferred interest programs, knowing that their customers are unlikely to satisfy the conditions of the program. As structured, these products can create a payment shock, and ultimately they may put consumers into debt traps. Some lenders who offer these loans as a tool for promoting the sale of high-margin retail goods may ignore the need to make a full ability-to-repay judgment.

- No balloon payments as a condition of receiving a zero or reduced interest rate.
- In any process of reviewing an application for a loan with a deferred interest promotion, lenders should have to underwrite for a borrower's ability to repay the entirety of a loan. It is not enough that a borrower can afford to make payments on a loan provided that the

[5] 11 NCAC 16.0501 Minimum Incurred Loss Ratio 11 NCAC 16.0501 Minimum Incurred Loss Ratio

interest rate is zero or reduced. The lender should underwrite as if the borrower was making a full payment of principal and interest.

- Lenders should not use the Rule of 78ths in connection with a deferred-interest program. We are concerned that in an environment where many loans are refinanced, the slower amortization schedule in the Rule of 78ths method undermines the ability of consumers to escape a debt trap.

It can cost a consumer hundreds of dollars – or even thousands in a few instances – if he or she misses a single payment in some deferred-interest programs.

Example: Conn's Credit

Conn's Credit ("CC") provides in-store financing to a subset of merchandise buyers at Conn's HomePlus ("CHP") stores. CC finances consumers that will not qualify for loans from independent third-party lenders with its Ye$Money in-house financing program. Ye$Money is a deferred interest installment term [not a credit card or revolving line] loan product that offers no interest payments on purchases of goods for the first 6 to 12 months of a loan. The loans amortize over longer periods. Purchase APRs range from 18 to 36 percent, depending upon the state where the loan is originated.

Three aspects of Ye$Money are designed to create debt traps:

- A consumer must pay off the loan early to receive the free interest. Almost half of all consumers who take out a Ye$Money loan ended up paying the accrued interest. But Conn's has established terms to their loans that are very unusual. To begin with, a consumer must pay off all of the outstanding debt with a balloon payment to avoid paying for accrued interest. Even though the loan length might be for as long as XX months, the balloon is due much earlier – usually within six to nine months. We suspect that there is a connection between this less-than-one-year periodicity and the expectation of a future tax refund. In essence, retail staff may be encouraging customers to gamble on the chance that they will qualify for enough of a tax refund to settle their debt.
- The borrower must make a full payment every month to avoid immediate disqualification from eligibility for financing: The borrower must remain current every month. In our opinion, this is a cynical calculation. CC only serves the lowest tier of credit. The weighted average credit score of CC's Ye$ Money loan program fluctuates between 590 and 610.

- Consumers have to meet a minimum purchase requirement to qualify for financing. To get the promotional rate of interest, a customer must spend at least $699.99, and in the case of the sale of lower margin inventory, they have to buy at least $999.99 in goods.

As if to add to the degree of deception, payments include interest. The interest is rebated back at the time when the balance is satisfied.

In Promotional Deferred-Interest Financing, "zero is not zero."

While the basic rules of the contract may be a given, the structure of the program is designed to maximize customer failure. Only one-third of CC's borrowers avoid paying interest when they take out an "interest-free" Ye$Money loan. Given that the average credit score of their customer base is 591, Conn's knows that its customer base has a high propensity to miss payments at some point in the life of the loan. In fact, at the end of FY 2014, Conn's said that almost twenty-five percent of all accounts were late during that specific month.

In most types of loan contracts, a borrower will pay a late fee of between $15 and $35 for missing a payment. In a deferred interest contract, the penalty for a missed payment is far greater.

The next table shows how much a consumer would pay for missing a single payment in the tenth month of a deferred-interest loan of a 36-month amortization period. The results are sorted by APR and loan amount.

Table: Sum of Lost Interest, sorted by APR and loan amount

	$1,000	$2,000	$3,000	$4,000	$5,000	$6,000	$7,000	$8,000	$9,000	$10,000
15%	$117	$235	$352	$469	$586	$704	$821	$938	$1,055	$1,173
18%	$143	$285	$428	$570	$713	$856	$998	$1,141	$1,283	$1,426
21%	$169	$337	$506	$674	$843	$1,011	$1,180	$1,348	$1,517	$1,685
24%	$195	$390	$585	$780	$975	$1,170	$1,365	$1,560	$1,755	$1,950
27%	$222	$444	$666	$889	$1,111	$1,333	$1,555	$1,777	$1,999	$2,222
30%	$250	$500	$750	$999	$1,249	$1,499	$1,749	$1,999	$2,249	$2,499
33%	$278	$556	$834	$1,112	$1,391	$1,669	$1,947	$2,225	$2,503	$2,781
36%	$307	$614	$921	$1,228	$1,535	$1,842	$2,149	$2,455	$2,762	$3,069

Rule of 78ths. Two-way data table prepared by Reinvestment Partners

For example, if a consumer took a $5,000 loan bearing an interest rate of 29.99 percent, and the loan amortized over 36 months, if the borrower missed a payment in month ten then he or she would suddenly owe $1,249 in interest that would otherwise have remained in an interest-free accrued status. In Question 2, the Bureau asks if there are products being offered to consumers that would harm them in the event of a liquidity crisis. This loan structure is designed to do just that, and as Conn's customer has a sub-600 FICO score and mean income of $38,400[6], it is being aimed squarely at the type of consumer least able to withstand a short-term liquidity problem. With this structure, a borrower only has to be ten days late – less than one pay period – before suffering a sizable financial set back.

Conn's is among the many non-prime consumer installment lenders that use the Rule of 78ths to apply payments to a borrower's debt obligation. In order to pay off a five thousand dollar loan in the 12th month, the borrower would need to make a payment of $4,911.

The next table shows how much a borrower would need to contribute at the end of 12 months to satisfy a deferred-interest promotion associated with a loan that amortized over 36 months, using a constantly amortizing loan payment schedule.

Table: Necessary Balloon Payment Needed to Satisfy Deferred-Interest Promotion

	$1,000	$2,000	$3,000	$4,000	$5,000	$6,000	$7,000	$8,000	$9,000	$10,000
15%	$715	$1,430	$2,145	$2,860	$3,575	$4,290	$5,005	$5,720	$6,435	$7,149
18%	$724	$1,448	$2,172	$2,897	$3,621	$4,345	$5,069	$5,793	$6,517	$7,241
21%	$733	$1,466	$2,200	$2,933	$3,666	$4,399	$5,132	$5,865	$6,599	$7,332
24%	$742	$1,484	$2,226	$2,968	$3,710	$4,452	$5,194	$5,936	$6,678	$7,420
27%	$751	$1,501	$2,252	$3,003	$3,754	$4,504	$5,255	$6,006	$6,757	$7,507
30%	$759	$1,518	$2,278	$3,037	$3,796	$4,555	$5,315	$6,074	$6,833	$7,592
33%	$768	$1,535	$2,303	$3,070	$3,838	$4,605	$5,373	$6,141	$6,908	$7,676
36%	$776	$1,551	$2,327	$3,103	$3,879	$4,654	$5,430	$6,206	$6,981	$7,757

Two-way data table prepared by Reinvestment Partners

We believe that only a small minority of typical non-prime consumer installment loan borrowers would have enough cash on hand to pay down the balloon due in almost any of the cells of the previous table. To the extent that repayments do occur on time, we are concerned that most successful repayments occur by using a tax refund.

[6] Conn's Investor Day Presentation. Analyst and Investor Day September 22-23, 2014

The Lack of an Ability-to-Repay Standard is Designed to Create Debt Traps

Conn's does not use an ability-to-repay to determine which customers to offer its promotional interest. Here is what management said about the plan for zero-interest financing:

> "The promotional receivables are being originated at all of our stores. And when we talk about promotional, **it's not based on any underwriting standards**[7]."

A "transaction profitability" decision framework naturally supersedes an underwriting approach based upon ability-to-repay. The decision is instead a product of merchandise margin and expected credit revenue after accounting for set-asides.

> "Our approval and decline decisions are based **<u>on expected transaction profitability</u>**…Our ability to incrementally approve customers being declined today and still deliver our target 20 percent return on equity increases as the interest yield and the retail gross margin increase. The additional expected credit losses would be more than paid for by the increased gross profit.[8] "

As the company has said to its investors, there turns from its in-house financing produce increase profits not just from interest revenue but also from the margin on inventory. To the consumer, the difference in cost between a loan with an interest rate of 60 percent used to finance the purchase of low-margin goods and the cost to buy a high-margin good with financing below state usury caps is nil.

In a 2014 investor presentation, Conn's noted that the average price of a television sold in one of its stores in the 1st quarter of 2015 was $1,131. According to the company, this compares to an average industry-wide price of $439[9]. In our opinion, this is an evasive means of creating interest revenue. In discussing how credit and high margin retail can work in synch with each other, Conn's management told investors:

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7 –Conn's CEO Theodore Wright during a call to investors on April 3rd, 2013.

8- Conn's COO Michael Poppe, June 6, 2013
http://www.sec.gov/Archives/edgar/data/1223389/000122338914000006/conn0131201410-k.htm

9 2014, June: Investor Presentation.
http://files.shareholder.com/downloads/CONN/3171621391x0x759056/EDE1686D-5172-4B3D-8530-40E21129D0FA/June_2014_Investor_Presentation_Final_.pdf

> "We see our financing rate as a very low cost alternative for this consumer. They have not to-date, and we haven't seen in any meaningful scale, anybody offering a rate competitive to the rate we're offering this consumer. And the reason we believe that exists is, and we talk about it in our slide deck, here's a slide about the barriers to entry and kind of what's our competitive advantage and simply, if you're doing the lending side only and you don't have the full retail transaction, because we really set the whole business model on the entire transaction, retail and credit combined, and we report the credit segment independent of the retail segment.[10]"

Other competitors have similarly deceptive deferred-interest programs. At Sleepy's, for example, consumers must make a balloon payment no later than in 12 months on a loan with an amortization period of 72 months to qualify for zero-interest financing. The lender is Synchrony. The associated interest rate is 29.99 percent. If a consumer missed a payment in the 10th month, then the consumer loses $824.05 on a $5,000 loan.

The example of Conn's is but one instance of practices that undermine the interests of consumers. The use of teaser rates, when coupled with balloon payment terms as a condition for receiving a promotion, are designed to hurt consumers who otherwise lack for enough financial liquidity to overcome a short-term cash flow deficit.

To Review, CFPB Should Pursue these Policies to Regulate Deferred Interest Loan Promotions on Installment Term Loans:

- Lenders should not be able to force borrowers to complete a balloon payment as a condition of receiving a promotional rate of interest.
- Interest accrued under a deferred interest promotion should not be credited under the Rule of 78ths.
- The Bureau should determine if a lender is providing "in-house" financing for the purpose of stimulating sales of its high-margin inventory, and if so, it should evaluate if the program is designed to evade relevant laws.
- Lenders must apply an ability-to-repay standard in underwriting loan applications. When underwriting for a loan with an upfront period of deferred interest, the

[10] Conn's Investor Relations.

underwriter should use consider the initial loan payment and the accruing interest as a basis for affordability.

VI. Potential Consumer Harm from Ancillary Products:

Non-file insurance

Non-file insurance provokes concerns related to debt collection practices. In our opinion, lenders should not be able to simultaneously take a security interest in a borrower's personal property while also asking the borrower to pay a fee for non-file insurance. This practice would seem to be a contradiction. After all, if a lender has requested the ability to take property as a protection of default, then why would it also feel the need to purchase insurance indemnifying it against the need for making a filing in a local court? In spite of that contradiction, many lenders use this is as a standard course of business. In its 2011 report to the North Carolina General Assembly, the Office of the North Carolina Commissioner of Banks indicated that personal property was pledged to secure 58 percent of all consumer loans. Of those instances where the borrower listed collateral, he or she also paid a fee for non-file insurance 93 percent of the time[11].

World Acceptance, a consumer installment non-bank financial services company headquartered in South Carolina, has an explicit corporate policy of selling non-file insurance on loans that are originated with a security interest in personal property. In its 2013 Annual Report, the company wrote:

> "World Acceptance purchases non-file insurance from the Life of the South ("LOTS") insurance company. They pass that cost on to consumers. If and when a consumer defaults on their loan, World files a non-file insurance claim. LOTS pays World Acceptance for the defaulted debt that is still outstanding…Substantially all new customers are required to submit a listing of personal property that will serve as

11 http://www.nccob.gov/public/docs/Financial%20Institutions/Consumer%20Finance/NCCOBReport_Web.pdf

**(although lenders purchase and hold the non-file policy, it is generally the case that the premium paid by the lender is equivalent to the non-filing insurance fee charged by the lender to the consumer[11])*

> collateral to secure the loan, but the Company does not rely on the value of such collateral in the loan approval process and generally does not perfect its security interest in that collateral[12]."

We believe that the listing of personal property only serves to increase the ability of the company to encourage borrowers to refinance their loans. According to World Acceptance, approximately 77 percent its new loans represent the refinancing of an existing loan. Another 9.9 percent are the result of a new loan issued to a former customer.

In and of itself, so much refinancing should raise concerns over the lack of an adequate ability-to-repay standard in place. But there is another sinister factor in place. World Acceptance has a policy of allowing customers to skip their next month's payment when they choose to refinance. Armed with a non-file insurance policy, the Company can stimulate more refinance loan applications with the leverage of removing personal property from a borrower's home. With the potential for creating substantial embarrassment to the borrower, the situation presents an opportunity for abusive practices.

In part 1c, the Bureau asks if there are collection practices that make it viable for lenders to ignore the ability of consumers to repay a loan. In our opinion, the use of non-file, in combination with requiring that a borrower lists personal property as a condition of approval, creates an opportunity to lenders to make loans without vetting for an ability to repay. When that is combined with a policy of letting a borrower skip a payment as a courtesy for refinancing an existing debt, then it becomes that much easier to generate revenue on loans without having the consumer repay the principal. Finally, when the outstanding debt is repaid under the Rule of 78ths method of bookkeeping, then the consumer is that much more likely to fall into a debt trap.

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[12] World Acceptance. Annual Report for FY 2013 to the Securities and Exchange Commission.

Conclusion

We believe that there are substantial concerns here to warrant further investigation by the Bureau. These products, while not covered by the final rule for payday, vehicle title, and certain high-cost loans, do carry the ability to put consumers at risk of falling into debt traps.

Thank you for your ongoing service to consumers.

Sincerely,

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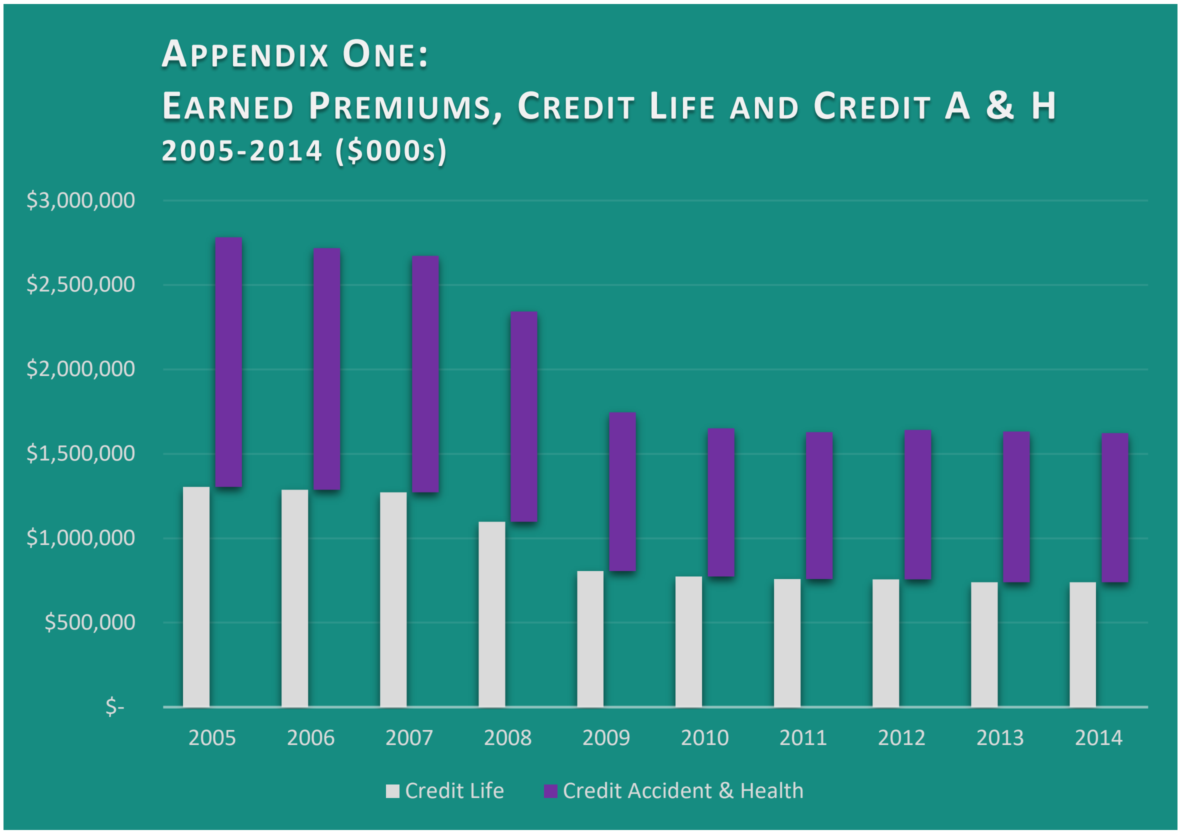
APPENDIX ONE:
EARNED PREMIUMS, CREDIT LIFE AND CREDIT A & H
2005-2014 ($000s)
$3,000,000
$2,500,000
$2,000,000
$1,500,000
$1,000,000
$500,000
$-
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
Credit Life
Credit Accident & Health