

- SUBJECT:** Making acquisition charge on small consumer loans non-refundable.
- COMMITTEE:** Financial Institutions — favorable, without amendment
- VOTE:** 7 ayes — Averitt, Solomons, Denny, Grusendorf, Hopson, Marchant, Menendez
- 0 nays
- 2 absent — Pitts, Wise
- WITNESSES:** For — Sam Kelley, Texas Consumer Finance Association; Lee Moore, Texas Consumer Finance Association; Judy Perkins; Brad Shields, Security Finance
- Against — Rob Schneider, Consumers Union, Southwest Regional Office
- On — Leslie Pettijohn, Consumer Credit Commissioner
- BACKGROUND:** Subchapter F of the Finance Code, ch. 342 provides for fees that can be charged by lenders who make small cash installment loans up to \$480, often called “signature loans.” For loans of \$100 or more, the lender may charge a \$10 loan acquisition fee plus \$4 per month per \$100 as an “installment account handling charge.” This effectively is the origination fee and the interest on the loan. No other charges are permitted by the lender. If the borrower pre-pays the principal on one of these installment loans, then the lender must refund a pro-rated portion of the \$10 acquisition charge.
- DIGEST:** HB 198 would amend Finance Code, sec. 342.256 to require that the \$10 acquisition fee on installment loans between \$100 and \$480 be considered earned at the time the loan is made and not subject to refund, regardless of prepayment.
- The bill would take effect September 1, 2001 and would apply only to loans made on or after the effective date of the bill.
- SUPPORTERS SAY:** HB 198 would update an outdated provision and allow lenders to recover more of their legitimate costs in making small cash installment loans. The current \$10 acquisition fee and account handling fees were established in

1963. Since that time, the lenders' overhead and other costs have increased, while permissible fees have not. One signature loan company estimates that its costs increased 63.88 percent between 1990 and 1999 alone. Also, the maximum loan amount under the law has increased from \$100 to \$480 while the acquisition fee has remained unchanged. Allowing lenders to retain the acquisition fee when these loans are repaid early would help lenders cover some of their costs.

While this bill effectively would increase the lender's yield on loans that are repaid early, the increase would be small, and lenders spend far more than \$10 in making the loan. On a \$300, 10-month installment loan that is repaid in the third month, the refunded portion of the acquisition charge is now \$5.09; in the fifth month, the refund is \$2.73; in the seventh month, the refund is only \$1.09. Lenders are not asking to increase the \$10 acquisition charge, only to make it non-refundable so as to recoup part of their lending costs. Besides, most other loan acquisition fees are higher and are non-refundable.

HB 198 would not affect payday lenders or check cashers. Other statutory provisions and regulation by the Consumer Credit Commission protect consumers against unscrupulous lenders who churn out loans to earn new acquisition fees. Thus, this bill would strike a good balance between the financial interests of lenders and borrowers.

**OPPONENTS
SAY:**

HB 198 would increase the cost to those consumers who typically use signature loans to borrow less than \$300. Signature loans already are a very expensive type of loan for which the annual rate of interest can be 85-100 percent, depending upon the amount of the principal and the term of the loan.

Lenders tend to encourage pre-payment of loans through refinancing because lenders earn the majority of their interest early in the life of the loan and can charge another acquisition fee for the new loan. In fact, one of the nation's largest signature lenders refinances 78 percent of its loans. The proposed change, which would shift even more of the earnings to the beginning of the loan, only would increase the lender's incentive to refinance, thus further increasing the costs to consumers.

OTHER
OPPONENTS
SAY:

The real problem with signature loans is not the acquisition fee but how often these types of loans are refinanced. A better approach to protecting consumers would be to limit the number of times a signature loan can be refinanced.

NOTES:

The companion bill, SB 105 by Carona, was reported favorably, without amendment, by the Senate Business & Commerce Committee on February 7.