

## MEMORANDUM

**DATE:** March 17, 2021  
**TO:** House Industry, Business and Labor Committee  
**FROM:** Corey Krebs, Assistant Commissioner  
**SUBJECT:** Testimony in Support of Senate Bill No. 2103

Chairman Lefor and members of the House Industry, Business and Labor Committee, thank you for the opportunity to testify in support of Senate Bill No. 2103. The purpose of this bill is to address weaknesses in current law as identified by industry professionals, attorneys, and department staff. We have considered the input of these stakeholders and this bill strikes a balance, eliminating unnecessary burdens where possible, modernizing consumer protections to be consistent with those of other states, and clarifying language within existing law.

Senate Bill 2103 includes amendments to Chapters 13-04.1-02.1, 13-05-02.3, 13-08-12, 13-04.1-09.2, and 13-04.1-09.3 of the North Dakota

Century Code relating to money brokers, collection agencies, and deferred presentment service providers.

Please note, that we are asking for an amendment to this bill. Following the passage of this bill in the Senate, we heard concerns from several companies on unintended consequences of the original wording. We have worked with these companies and the Attorney General's office on an amendment which should address these concerns. I will address the specific wording changes of the proposed amendment in each respective section of the bill.

Section 1 of the Bill would amend 13-04.1-02.1 related to exemptions to the money broker statute. Money brokers are persons or entities who engage in the act of arranging or providing loans or lease financing. The rule establishes licensing requirements, bonding requirements, and a framework over the process to help protect the public from misleading or predatory practices and individuals. The rule also specifically exempts groups and individuals from these rules if the risks are otherwise controlled or mitigated.

One group that is specifically exempt is state or federal agencies or their employees. It is assumed the intention was for this employee exemption to apply to their actions executed in their capacity as government employees. For example, an employee of the North Dakota Housing

Finance Agency would be specifically exempt from this law as this state agency mission involves lending and controls exist over this agency. What is not clear is if other employees acting outside of their role as a government employee are also exempt. For example, would an employee of the Department of Transportation be exempt by virtue of that employment with the state even if the loans being granted were not part of their duties as an employee of the state, rather a secondary business venture? This bill adds clarifying language to ensure only lending activity related to the individual's duties as a government employee is exempt from this statute.

This bill also adds two new exemptions from the money broker licensing requirement, the first of these being certain certified development corporations. Much of the activity performed by certified development corporations currently subject to the money broker regulation is part of their work with Small Business Administration loans. These loans are subject to review by this government agency, thus the risks to consumers or businesses are greatly limited. Many also offer other loan products in addition to their Small Business Administration loan activity. If these additional loan product offerings were primarily to promote community development or home ownership rather than being a profit center for the certified development corporation, under this proposal, the company can

continue to be exempt. This exemption will limit any cost or burden for these companies if they are engaging in low-risk activity or review from the Small Business Administration.

The department reached out to the industry for their input on this exemption. The response received was generally positive. There was one request for a greater level of exemption. The request was to exempt loan products which were written with terms that were more profitable to the company than those outlined in this bill. This broader exemption was considered but ultimately was not incorporated into this bill. This exemption is limited to low-risk activity, activities which were clearly to promote community development or home ownership. Higher return products may or may not be written for this purpose, thus pose a higher risk to consumers and are not eligible for an exemption. It is important to note that if a community development corporation wishes to engage in higher return lending which is not exempt, they can do so after obtaining a money broker's license, ensuring a base set of protections are in place just as they do today. This exemption makes compliance easier for companies that wish to engage in low-risk activity.

The second exemption created with this bill is for nonprofit corporations that offer a limited number of loans, again with terms that make it clear they

were designed for community development purposes. Here again this exemption was discussed with the industry and it appears to meet their needs while limiting consumer risk.

Section 2 and section 5 of this bill are related to each other. Section 5 repeals 13-04.1-09.2, which relates to protections for small dollar loans, and in its place, section 2 establishes 13-04.1-09.3 as the framework for loans written under chapter 13, including small dollar loans. This change makes North Dakota's rule more similar to rules of other states.

The current rule, 13-04.1-09.2 is problematic for several reason. First and foremost, it is unnecessarily complex in the formula used to calculate maximum finance charges for small dollar loans. The result of this complex formula is one of the lowest returns allowed by any state for small loans, which could limit credit options for consumers. It also establishes no interest rate framework for loans above \$1000 and no framework governing fees, making us only one of two states not addressing late fees. This makes our law inconsistent with most other states and applicable federal law. Finally, lenders can exploit weaknesses in the current rule to structure credits in such a way to circumvent most of the protection in this law.

It is interesting to note, that consumer advocacy groups have long criticized the payday loan industry for predatory loan practices. In North

Dakota, we have not heard issues with the payday loan industry, likely due to the strong controls we have over this industry. However, we do see issues with money brokers, particularly online lenders offering small dollar loans. It appears there are loopholes that are resulting in practices which may not have been intended by the legislative body when the original small dollar loan protections were adopted.

These weaknesses and inconsistencies are a concern for two reasons. First, for North Dakota consumers it means that they have fewer safeguards from predatory lending practices than they would have if they were citizens of another state. Secondly, for lenders it means that the current law is a prime target for action from consumer advocacy groups. Consumer advocacy groups have sponsored voter-initiated measures as close to us as South Dakota. Voter initiated measures are great but are often simple prohibitions or limits that could make otherwise desirable practices unprofitable and have the unintended consequence of limiting consumer credit options. The Department is proposing this change as a well-reasoned rule which attempts to establish protections from predatory lending practices while not being unduly burdensome to limit consumer credit options.

Prior to drafting the proposed 13-04.1-09.3, the department researched comparable rules employed by other states and the federal

government. While a wide range of limitations exist, some limits such as a 36% limit on annual percentage rates (APR) seem to be emerging as the prevailing limit adopted by more and more states, probably because this is the limit also used by the federal government to protect military service members. Other limits where possible, such as limits on late fees, were selected for both simplicity in calculation and after considering the limits of surrounding states.

Finally, loan extensions, payment deferrals, and refinance fees are normal parts of loan administration, but can also be used to circumvent APR limitations or late fee charge limitations. Efforts were made to limit the ability to circumvent these rules including a prohibition on balloon payments and excess late or extension fees for small dollar loans. This avoids a complete prohibition of these activities, but also establishes a reasonable framework in which to use them to prevent predatory lending practices.

It should be noted that we do not believe many North Dakota lenders will be impacted by these changes. Most North Dakota lenders offer terms well below the limits proposed here. Most of the lenders the department sees engaging in these more aggressive lending practices are online only lenders without a physical presence in North Dakota and minimal lending activity in North Dakota.

We did hear from lobbyists after this bill was approved by the Senate. Their concern is that the wording of the bill would result in an “all in” approach to calculating the interest rate. It is the Department’s intention to calculate the maximum interest rate charge at the time of loan origination and the limit on charges and fees only include charges and fees mandatory for the extension of credit. The bill’s current wording did not do this. We worked with the Attorney General’s office and determined that replacing the words “or fee incident to” with “and fees mandatory for” on page 2 line 29 resolves this issue. The Department is asking for this change as part of the proposed amendment.

We also heard from lobbyists representing lenders that finance auto dealers’ inventory of cars for sale, a loan type known as floor plan loans. Their concern was that subsequent fees charged for advances on these lines of credit would be included in the maximum interest rate calculation and the late payment cap was low for large commercial loans. We consulted with the Attorney General’s office and confirmed that these advance fees would not be included with the bill’s current wording. However, to make it more clear, we are proposing additional wording changes to page 2 lines 28 and 29 as part of the proposed amendment. These changes make it clear that the maximum charges for loans under this section are not calculated on any



charges incurred subsequent to the credit or loan document origination or at the time advances are made under lines of credit.

We are also proposing an amendment to page 3 line 1 to ensure the cap on late fees does not create an artificial low limit on the large credits such as auto dealer floor plans. The maximum charges for delinquent loan payments would not apply to loans originated for more than \$50,000. The origination amount for revolving lines of credit is the maximum draw established at the time of origination, not the amount each advance on the line. The \$50,000 threshold was selected as it has been used by other states for exclusion from items such as disclosure requirements, thus creating an element of consistency. We believe that with this amendment we are creating sufficient consumer safeguards without creating undue regulatory hurdles or limits.

It is also important to point out that this rule only applies to those subject to the money broker regulation. This does not apply to banks or credit unions. When discussing this change with those industries, we have tried to make that clear. We have also pointed out that banks and credit unions are subject to greater federal government oversight than are money brokers which is the reason for a state rule applying just to money brokers.

Section 3 of the Bill would amend 13-05-02.3 related to exemptions to the collection agency statute. The rule establishes licensing requirements, bonding requirements, and a framework over the process to help protect the public from misleading or predatory practices and individuals.

Much like the money broker statute, certain government employees are exempt from the collection agency statute. This bill adds clarifying language to ensure only collection activity related to the individual's duties as a government employee is exempt from this statute.

This rule also has an exemption for licensed real estate brokers. The proposed change makes it clear the exemption is for activity related to that individual's professional license.

Finally, section 4 of this bill is a change related to 13-08-12 governing Deferred Presentment Service Providers also known as payday lenders. To limit the risk of predatory practices and to avoid the risk of a borrower falling into a debt trap, North Dakota's rule provides a strong framework for this type of lending. The current rule limits actions available to lender to prevent abuses, but it also inadvertently limits the ability of a lender to work with a borrower to work out of a difficult situation over time. Under the current rule the only tool available to the lender is to cash the check or turn it over to collections which can be expensive for both the lender and the borrower.

This proposed change gives an additional option, to pay it off over time if both the borrower and lender agree to the change.

Mr. Chairman, thank you for the opportunity to provide this testimony. I would be happy to answer any questions the Committee may have.