RULES COMMITTEE: 5-18-11
ITEM: H.2

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Councilmember Ash Kalra
Vice Mayor Madison Nguyen
Councilmember Xavier Campos
Councilmember Sam Liccardo

SUBJECT: SEE BELOW

DATE: May 11, 2011

Approved Date 5/11/11

SUBJECT: RESOLUTION IN OPPOSITION TO AB 1158 (INCREASING PAYDAY LOAN AMOUNTS)

RECOMMENDATION:

That the Rules and Open Government Committee place on the agenda for an upcoming afternoon session of a City Council Meeting an item to draft a resolution that respectfully registers opposition to California Assembly Bill 1158 (Calderon) that would increase the maximum amount of a payday loan from $300 to $500, while charging users with up to 459% APR in a short repayment term (usually two weeks to 30 days) in the City of San José and the rest of the State of California.

BACKGROUND

Current California law allows a borrower to write a check for a maximum of $300 to borrow $255. The high cost of payday loans (459% APR), together with the short two-week repayment term, can lead to cash-strapped borrowers not being able to meet their basic expenses and pay off their loan at their next payday. It follows, then, that increasing the amount of debt borrowers of payday loans owe will only increase the likelihood that they will not be able to pay off the loan at their next payday, and therefore be more likely to enter a cycle of increasing debt.

With shrinking profits in other states, payday lenders are turning to California in an attempt to preserve their profit margins on the backs of struggling Californians, by seeking to increase the allowable loan amount to $500. Local governments have recognized that this bill is a step in the wrong direction; in January, the Santa Clara County Board of Supervisors unanimously voted to adopt a resolution against the usurious interest rates and predatory business model of the payday lenders, calling on the California State Legislature to enact a 36% APR interest rate cap on payday loans. The County expressed its opposition to AB 1158 in letters and oral testimony to the Assembly committee that heard the bill last month. In February, the San Diego City Council unanimously adopted a similar resolution. In addition, media outlets' editorial boards have come out

unanimously adopted a similar resolution. In addition, media outlets' editorial boards have come out strongly against the bill, including the San José Mercury News on May 4, 2011, and the Sacramento Bee on May 9, 2011.

Opponents of AB 1158

Leading the way among the many opponents of AB 1158 is the Center for Responsible Lending, founded in 2002 by the nonprofit Center for Community Self-Help. Their vision is to have a "fair, responsible and transparent market for sustainable loans that build wealth and a stronger economy for all." Their up-to-date information provided by high-quality, innovative research helps to quantify the extent and impact of abusive lending practices that the citizenry of San José have been subjected to.

In addition, 41 local community organizations—part of the Coalition Against Payday Predators (CAPP)—and a number of statewide organizations have joined in the opposition of the bill. The statewide organizations include, but are not limited to:

· Dolores Huerta Foundation
· Catholic Charities of California United
· Silicon Valley Community Foundation
· California Labor Federation - AFL/CIO

These well-respected community organizations' opposition to this irresponsible increase in payday lending is rooted in the belief that by allowing payday lenders to increase loan amounts, we simultaneously encourage payday loan borrowers to be placed on a path that leads directly to thousands of dollars in fees per year and the looming possibility of unending debt.

Creating a cycle of poverty

Statistics show that low income families easily get caught up into a cycle of predatory and excessive lending practices from payday lending establishments. With highly-visible signs and convenient neighborhood locations, payday loans beckon borrowers with promises of quick cash and no credit checks. Far less noticeable are the loan terms that include high-cost fees and triple-digit interest rates. Instead of a small amount owed for a couple of weeks, borrowers become trapped in thousands of dollars of debt from fees and interest that can last a year or even longer. Most payday borrowers have nine repeat loans per year and up to 459 percent interest. The problems with payday lending have grown so bad that they are likened to "legal loan sharking" that creates a cycle of debt that can eventually lead to insolvency and poverty. With so many families in our area already living within the fringe of poverty levels, no fiscally and socially responsible person can suggest that increasing payday loan levels can be beneficial to the most financially susceptible members of our community.

This cycle was dramatically highlighted by the testimony of one San José resident, Sarah Portales, who testified before our Rules Committee on December 15, 2010, and before the Assembly Banking and Finance Committee on April 25, 2011. Ms. Portales, a single mother who has worked for 16 years as a custodian at San José State, spoke of the dozens of payday loans she had taken out and how she was trapped by the ever-mounting fees she was required to pay on the loans.

Matters of public safety

Beyond the negative financial impacts that plague the customers of payday lenders, we find that these establishments usually hold large amounts of cash on hand and often lack basic levels of security. This has directly correlated to enticing the criminal element that wish to capitalize on the opportunity to acquire large sums of cash by using an increasing amount of force and intimidation, often occurring with incidents of aggravated assault, and in at least one San José payday lending criminal case, attempted murder with a firearm.

COORDINATION

This memo proposes drafting a resolution that respectfully registers opposition to California Assembly Bill 1158 (Calderon) on behalf of the City of San José Council and the community at large. This memo was crafted utilizing information provided by the Center for Responsible Lending, and senior staff from the Office of Economic Development Work2future division.

POLICY ALIGNMENT

The City of San José has been a leader financial and social responsibility, as well as having developed policy goals and standards to curtail damaging and financially ruinous legislation that would impact the most vulnerable of its citizens.

In the City's 2011 Legislative Guiding Principals, section C (Protect and Increase Local Funding; No Unfunded Mandates) and section F (Promote Livability, Sustainable Development, and Environmental Protection) subsections 13 and 8 respectively state:

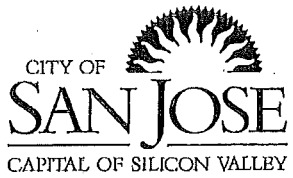
> *C. Protect and Increase Local Funding; No Unfunded Mandates, 13*: Support advocacy efforts that promote the development and implementation of a revised poverty formula, which will provide a more accurate account of the City's high cost of living and the ability of families to meet their basic needs, allowing the City to qualify far more funding programs that use the poverty formula as a tool to determine funding awards.
>
> *F. Promote Livability, Sustainable Development, and Environmental Protection, 8*: Seek to protect the community and residents from certain reverse annuity mortgages or specialized loan product~ that place seniors or persons with limited English skills in danger of foreclosures.

Although the terminology "payday lending" is not specifically mentioned, any reasonable person can understand that their inherent purpose is to protect those who may fall prey to dangerous lending practices, while taking into account the reality of the high costs of living in our area that require families to take drastic measures in order to make ends meet. As a result, these families frequently turn to payday lending for what they think of as a respite, only to find themselves in a cycle of debt as time goes on. Much like the reverse mortgage products listed as suspect under the second guiding principal set forth above, payday loans are a threat to the economic vitality of many San José families and neighborhoods.

In addition, in February of this year, the City Manager's Office, in coordination with the District 2 Council Office and Public Interest Law Firm, successfully applied for a $50,000 grant from Silicon Valley Community Foundation (SCVF) for "city ordinances that restrict payday lending." By registering opposition to increasing payday loan limits requested in AB 1158, the City honors the initial intentions of our grant application from the SCVF while demonstrating its steadfast resolve towards fulfilling its own Legislative Guiding principles regarding responsible lending practices and effectively plays a part in bringing an end to predatory lending within its city limits, and beyond.

Attachment:
Rules Committee memo from Councilmember Kalra and Councilmember Campos, 12/9/2010 – "Regulation of Payday Lending".

COUNCIL AGENDA: 00-00-00
ITEM: xx



Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Councilmember Ash Kalra
Councilmember Xavier Campos

SUBJECT: SEE BELOW

DATE: December 9, 2010

Approved

Date December 9, 2010.

SUBJECT: REGULATION OF PAYDAY LENDING

RECOMMENDATION

1. Direct Staff to apply for a grant in the amount of $50,000 to $200,000 being offered by the Silicon Valley Community Foundation related to the establishment of anti-payday lending policies, and to report to the Community and Economic Development Committee on the status of the grant application on the earliest date possible following the announcement of the grant awards in February 2011.

2. If funding is awarded, direct Staff to:

   a. draft an ordinance establishing a temporary citywide moratorium prohibiting the acceptance or processing of any permits or licenses, including building permits, related to the establishment of a new payday loan business, and prohibiting the establishment of any new payday loan business for which no permit would otherwise be required;

   b. draft an ordinance that would:

      i. require the issuance of a special use permit prior to the establishment of a new payday loan business;

      ii. enact distance, density, and zoning restrictions for payday loan businesses so that such businesses are a reasonable distance away from other payday loan businesses, residential zones, schools, liquor stores, card rooms, medical marijuana dispensaries, adult book/video stores, adult movie theaters, adult entertainment establishments, and massage parlors; and

      iii. require greater disclosure of the terms of a payday loan, minimal security measures for payday businesses, performance standards to prevent visual blight, and restrict the hours of operation for payday loan businesses; and

   c. coordinate and conduct an appropriate stakeholder outreach process.

BACKGROUND

A payday loan is a short-term cash loan that is guaranteed by a personal check given by the borrower to the lender. In exchange for the loan, borrowers will either write a personal check to the lender for the loan amount plus the finance charge or will sign over electronic access to their bank accounts for the agreed-upon repayment amount. The lender will hold the check for the loan period (usually until the borrower's next payday), and if the borrower is unable to repay the loan amount plus the finance charge on the due date, the lender will deposit the borrower's check. Recent studies show that nearly half of California payday borrowers take out payday loans at least once a month, and more than a third of borrowers have taken out loans from multiple payday lending companies at the same time.

A recent study by the Consumer Federation of America (CFA) is very critical of the payday loan industry. The study noted that payday loans are commonly issued with an annual interest rate (APR) of 400% or more, and that some payday loans can result in interest rates as high as 780% APR. The average annual percentage rate (APR) in 2006 for such loans was a staggering 429%, according to the California Department of Corporations. Other studies state that interest rates for payday loans can ultimately reach 900%. The CFA also noted that payday loans are extremely expensive even when compared against a cash advance from a credit card. According to Consumers Union, the "fees for payday loans are extremely high: up to $17.50 for every $100 borrowed." Another study indicated that payday loan borrowers ultimately end up paying a total of $800 on an original loan of $325.

Although payday loans are often promoted as a solution for people in unexpected financial straits, studies have shown that if a borrower is facing financial hardship, a payday loan can actually worsen the situation. This is because the payday lender, by virtue of having the borrower's personal check or electronic access to the borrower's checking account, will have de facto priority over the borrower's other creditors and therefore will be paid before basic living expenses such as rent and utilities can be paid. In essence, the payday lender ends up having a priority lien on the borrower's bank account. Since most borrowers take out payday loans to cover a chronic shortage of income over expenses, rather than to cover emergencies, many cash-strapped borrowers experience another shortfall after their first loan.

Equally troubling are the many studies that demonstrate that payday loans tend to proliferate in lower-economic communities, and often tend to target low-wage workers, military personnel and young people. These studies conclude that since payday lending businesses charge such high interest rates and do nothing to encourage saving money or using traditional financial institutions, they have the effect of depleting the assets of low-income communities and young people. Payday lending has drained an estimated $247 million in fees from African-American and Latino households in California. The harm to military personnel and their families was so severe that in 2007, the federal government capped the APR of payday loans offered to service members or their dependents at 36%.

Lastly, payday lending businesses, especially when many are concentrated within a particular geographic area, are commonly associated with neighborhood blight and often become inviting targets for crime, due to the likelihood of such businesses having large amounts of cash on the premises. In fact, in mid-August, a robbery occurred at a check cashing store located in South San José during which two employees were held at gunpoint and one was shot.

Addressing the harmful impacts of payday lending now would be consistent with opinions and policy statements previously expressed by the City of San José and its residents. In December of

2008, Mayor Reed announced his support for the "Bank On San José" program, a local offshoot of a statewide initiative designed to encourage low and middle income residents to become more financially stable by taking advantage of mainstream financial institutions, rather than relying on institutions such as check cashing and payday loan business. In addition, San José's Human Rights Commission, in recommending that the City provide support for the Bank On San José program, specifically suggested that the City require check cashing and payday loan businesses to provide information about the "Bank On" program. Lastly, residents participating in workshops held by the San José Redevelopment Agency in 2008 and 2009 identified check cashing businesses as a specific type of business that the residents wanted to discourage.

ANALYSIS

The Silicon Valley Community Foundation (SCVF) recently issued a Request for Proposals (RFP) for "city ordinances that restrict payday lending." The RFP (attached) states that grants ranging from $50,000 to $200,000 will be awarded for policies aimed at limiting the harmful impact of payday lending. Application for this funding are due on January 5, 2011 and the grant awards will be announced in February of 2001. Given the fast-approaching deadline, we will have to move quickly to take advantage of this opportunity to address the predatory lending practices that target San José's lower-income residents.

Many local municipalities have already recognized the threat that payday lending poses to the community. Within the last seven years, San Francisco, Oakland, and Sacramento have enacted ordinances that placed limits and controls on the payday lending industry. It is time for San José to do the same. The unregulated growth of payday loan businesses is detrimental to the welfare of the citizens of San José, as dozens of payday lending businesses are presently operating in San José with little or no regulation or oversight. By adopting an ordinance that limits the establishment of new payday loan businesses, the City of San José will be furthering its stated goal of encouraging reliance on mainstream financial institutions rather than fringe lending businesses, and will be helping to protect lower-income communities, who are disproportionately impacted by the predatory nature of payday lending.

The Center for Responsible Lending asked Goodwin Simon Strategic Research to conduct a telephone survey of San José voters to explore issues related to efforts to limit or restrict payday loan stores in San José. Only 17 percent of San José voters have a favorable opinion of payday stores, while 52 percent have an unfavorable opinion of them. This 3 to 1 ratio demonstrates that payday loan stores do not start with a significant base of support among the electorate in San José. Voters were also asked their views on a proposed two-year moratorium on new payday loan stores in San José, and a resounding 63 percent would favor a moratorium, with just 22 percent opposed and only 15 percent not sure. Various land-use regulations polled even more favorably.

We recognize that the timeframe for this application is brief, but this opportunity to obtain substantial assistance in developing a policy that will protect the financial health of San José's lower-income communities is worth the effort

Attachment:

Silicon Valley Community Foundation Request for Proposals—"Economic Security Strategy: Anti-Payday Lending Policy Advocacy"