May 17, 2023

Araceli Dyson
Department of Financial Protection and Innovation
2101 Arena Boulevard
Sacramento, California 95834
Via email to: regulations@dfpi.ca.gov

RE: CCFPL, CFL, CDDTL, and SLSA – Registration Requirements under the CCFPL - PRO 01-21

Dear Ms. Dyson,

The California Low-Income Consumer Coalition (CLICC) writes in response to the Department of Financial Protection and Innovation's (DFPI) request for comment related to the registration requirements under the California Consumer Financial Protection Law (CCFPL).

CLICC is a statewide coalition of more than a dozen providers of free legal services. The organizations came together in 2017 to pool their resources, experience, and expertise and establish a permanent presence for low-income consumer advocacy in Sacramento. CLICC and its members work to build a marketplace in which consumer rights and economic justice are fully recognized and firmly established.

CLICC welcomes the proposed regulations under the CCFPL to protect low-income and vulnerable students, employees, and consumers from predatory lending, debt settlement, and income-based advance practices.

In 2020, CLICC joined dozens of other community, nonprofit, and small business, and consumer lending organizations as part of the base of support and advocacy for AB 1864, the CCFPL, which authorizes the promulgation of these regulations.[1] The CCFPL enhanced the DFPI's oversight authority to cover previously unregulated business activities, including debt collection, debt settlement, and other financial enterprises. To achieve the legislature's purpose of protecting consumers from discrimination and unfair, unlawful, deceptive, and abusive acts and practices, the CCFPL empowers the DFPI to impose registration and reporting requirements on covered activities. The regulations now proposed by the DFPI are necessary to specify which activities

[1] https://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201920200AB1864

are subject to regulation, to set out a process for registration and annual reporting, and to clarify the applicability of the California Financing Law (CFL) to these activities.
The proposed rule represents a step forward in protecting California's low-income consumers and puts our state at the forefront of consumer protection efforts. That said, the rule can be further strengthened by allowing for greater transparency with regard to certain information included in the applications and annual reports.

CLICC offers its support for the DFPI's proposed rule, and respectfully offer the following recommendations to strengthen the final rule.

Background: Income-Based Advance Products

Over the past decade, the market for tech-enabled income-based advance products has grown rapidly, opening the door for "the biggest change to the payroll industry in decades."[2] Many of the California's largest employers, including Amazon, Walmart, and Dollar Tree offer what is commonly referred to as "earned wage access" to their employees.[3] Income-based advance products are typically targeted at low-wage, hourly workers living paycheck to paycheck. Providers insist that their products are not loans, and therefore not subject to state interest rate caps and usury limits.[4]

In 2021, the DFPI entered memoranda of understanding (MOUs) with five income-based advance providers to enable them to continue operating in California before and during the current regulatory process.[5] These MOUs did not clarify whether income-based advances were subject to the CFL's interest rate limits. Absent regulatory clarity, income-based advance companies saddled consumers with high fees and engaged in unfair and deceptive practices. According to data collected by DFPI while the MOUs were in place, the charges, fees, and "tips"[6] collected by income-based advance providers translated to interest rates above 300%, on par with predatory payday lenders.[7] And usage of these products indicated that consumers were

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[2] Emily Bary, In the employer struggle to find workers, there may be a $12 billion fintech opportunity, Market Watch (July 16, 2021), https://www.marketwatch.com/story/inside-the-12-billion-opportunity-to-speed-up-access-to-paychecks-11626459962.

[3] While several different terms are used to refer to this category of financial technology products—including "earned wage access" and "earned wage advance"—these comments will refer to them as "income-based advances" to be consistent with the DFPI proposed regulations.

[4] See, e.g., DailyPay, Whose Loan Is It, Anyway? (Jan. 9, 2020), https://www.dailypay.com/resource-center/blog/whose-loan-is-it-anyway/ ("DailyPay simply functions as an ATM for an employee's own earnings").

[5] https://dfpi.ca.gov/2021/01/27/the-dfpi-signs-mous-believed-to-be-the-among-the-nations-first-with-earned-wage-access-companies/

[6] Some income-based advance providers, such as Earnin, purport to be fee-free but encourage customers to pay "voluntary" tips on each transaction of up to $14.[6] A New York class-action lawsuit (since settled) alleged that Earnin penalized customers who gave low tips or no tips by lowering the borrowing limit on future advances. It further alleged that the default tip was $9 and that app users were required to manually select another tip amount. For a user who accessed $100 twice per pay period, a $9 tip would translate to 432% APR.

[7] https://dfpi.ca.gov/wp-content/uploads/sites/337/2023/03/2021-Earned-Wage-Access-Data-Findings-Cited-in-ISOR.pdf?emrc=08148f

falling into a "debt trap": on average, consumers were using income-based advance services 9 times per quarter, or 36 times per year.[8] Income-based advance products promise consumers quick cash, but—as advocates have warned—the hole they leave in the employee's paycheck can only be filled by taking another advance, not only trapping employees in debt but also in a low-paying job.[9]

In fact, income-based advances *are* loans in both form and function. The "de facto marker of a loan," as Professor Nikita Cuttino explains, is the "disaggregation of costs and benefits"; that is, deferring repayment so that the consumer receives the benefit of the transaction *before* the cost is due.[10] Employees who seek income-based advances receive the benefit at the time of the transaction and pay the cost when their next payday comes around. And while income-based advances generally do not charge "interest" as such, the charges, fees, and tips function the same way—compensating lenders for the time value of money—and can be just as harmful to consumers as a high-APR payday loan.

3.3 million—or one in three—households in California struggle to meet their basic needs.[11] Income-based advances promise a lifeline, then pull struggling consumers further underwater. The CFL, CCFPL, and CDDTL were enacted to protect consumers from harmful financial products, and they should be used to their full effect to regulate the income-based advance industry.

Analysis

DFPI's new proposed regulations clarify that income-based advances are loans and are subject to rate limits under the CFL. They set up a registration and data-collection regime that will allow the DFPI to ensure that EWA providers are compliant with the law and to inform future regulations and enforcement actions. These are all important and necessary protections for Californian consumers and CLICC supports the DFPI making these determinations. However, there are several areas in which the regulations could be strengthened. Most significantly, the nondisclosure policy limits consumers' ability to make informed decisions about income-based advance products and limits advocates' ability to identify noncompliant practices and make the DFPI aware of these issues.

1. **By clarifying that income-based advance products are loans, the proposed rule will protect consumers from predatory rates and require providers to disclose the true costs of their products.**

We applaud the DFPI's clarity in stating that all income-based advance products (whether employer-integrated or direct-to-consumer) are loans and are subject to rate caps under the CFL.[12]

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[8] Id.
[9] NCLC Comments at 26.
[10] Cuttino at 1539.
[11] https://insightcced.org/wp-content/uploads/2021/05/INSIGHT_CostofBeingCalifornian_6_web.pdf
[12] Regs at § 1461(a).

The DFPI's authority under the CCFPL is broad by design and includes the authority to regulate the income-based advance industry.[13] Specifically, the legislature instructed the DFPI to interpret and implement "all California credit cost provisions [including rate and fee caps] as to their applicability to consumer financial products and services."[14] Pursuant to this authority, the DFPI interpreted the rate cap provisions of the CFL as they relate to income-based advances.
The DFPI correctly interpreted the definition of credit under the CFL to apply to income-based advances. This argument is legally sound— consistent with the language and purpose of the statute and understandings of the meaning of credit by California courts. The state legislature itself has mandated that the DFPI and courts interpret the CFL "liberally" to protect borrowers.[15] Historically, California courts have embraced consumer protections related to the sale or assignment of wages. For example, interpreting the Labor Code in *Lande v. Jurisich*, the California Court of Appeal found that "the Legislature obviously sought to reach every form of instrument which would result in the impounding of a wage earner's wages before he received them."[16]

The DFPI proposed regulations cover most of the various forms of income-based advances. EWA products take many different forms, in part for the purpose of evading regulations and rate caps. Some providers contract directly with employers and have access to time and attendance records (DailyPay, PayActiv); other companies purport to provide access to earned wages but have no direct relationship with the employer or access to payroll information (Earnin); a third category of companies provides single-installment cash advances through apps (Dave, Brigit). All of these business models are covered by the proposed regulations, with the exception of obligor-based advances. CLICC welcomes this wide-angle approach, which (1) prevents providers from circumventing the rules with creative business models, (2) allows consumers to choose among different models knowing they will be afforded the same legal protections, and (3) fosters competition among providers—one of the stated purposes of the CFL[17]—and thereby benefits low-income consumers. As for obligor-based advances (which are currently excluded from the proposed regs), to the extent that an obligor-based advance charges fees, interest, or "tips" in excess of the allowed administrative fee, they should be treated as loans under these regulations.

After establishing that the covered activities are subject to the CFL's rate caps, the DFPI gives this point teeth by further clarifying that "[c]harges include, without limitation, subscription fees, expedited funds fees, account transfer fees, and gratuities"; that is, providers can no longer evade the CFL's rate caps by collecting hidden fees and deceiving consumers into paying supposedly voluntary charges and tips.[18] Like the CCFPL, the CFL is intended to be interpreted broadly: the legislature mandated that the CFL be "liberally construed and applied to promote its underlying purposes," which include protecting "borrowers against unfair practices by some lenders." The income-based advance industry's deceptive practices have been well documented: companies use dark patterns—interface design tricks and psychological tactics—to manipulate consumers into

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[13] CCFPL
[14] Fin. Code § 90009(f)(2).
[15] Fin. Code § 22001(a)(4).
[16] *Lande v. Jurisich*, 59 Cal.App.2d 613 (Cal. Ct. App. 1943).
[17] Fin. Code § 22001.
[18] Regs at § 1004(c);

paying “voluntary” tips, along with expedited funds fees, account transfer fees, and monthly subscriptions for services marketed as “fee-free.”[19] For example, a class-action lawsuit (since settled) alleged that Earnin—an income-based advance company that solicits “tips” from users—penalized those who gave low tips or no tips by lowering the borrowing limit on future advances.[20]

By clarifying that income-based advances are subject to the CFL’s rate caps, the DFPI leads the way in ensuring that low-income consumers have access to income-based advances without being exploited by unscrupulous providers.

2. **The registration process allows for data collection and monitoring that will strengthen future regulation and enforcement activities.**

The proposed regulations establish a well-designed data collection protocol for the income-based advance industry to determine (among other things) what frequency and amounts consumers borrow and the associated charges. They ensure that newly-covered entities and entities already subject to the DFPI’s authority be monitored with similarly thorough and robust data collection requirements. This data collection protocol will enable the DFPI to monitor compliance with the CFL rate caps and take enforcement action when needed to protect consumers.

3. **The proposed rules should be clarified and strengthened to better protect California’s low-income consumers.**
    a. **Registrants should be required to affirmatively state that registration is not an endorsement.**

Section 1012(b) requires providers to “disclose in any advertisement or communication to a consumer that the registrant is registered with” the DFPI. Subsection (a) of that section states that it is a deceptive practice “for a registrant to represent, directly or indirectly, that the registrant’s acts, practices, or business have been approved” by the DFPI. Nevertheless, a reasonable consumer may interpret the disclosure required by § 1012(b) to imply that the business has been approved by the DFPI. To prevent such an interpretation, the § 1012(b) disclosure should be amended to include the following language: “[Registrant’s] registration status does not constitute a determination that [Registrant]’s acts, practices, or business model complies with any law or regulation.”

b. **Information collected at time of registration: Registrants should provide representative agreement between provider and obligor.**

Section 1026 should be amended to require registrants in an employer-integrated model to provide representative agreements between the provider and the obligor. This is consistent with the requirement for education financing registrants to provide the agreements between the loan servicer and the provider (§ 1025) and is necessary to ensure that proper procedures are in place

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[19] https://prospect.org/power/05-01-2023-fintech-ewa-payday-loan-scam/.

[20] The Earnin app sets a default tip of $9 for a $100 transaction (for a user seeking two advances per pay period, that equates to a 432% APR). Users who want to leave a lower tip must manually reset the tip amount each time. *Stark v. Activehours, Inc.*, No. 5:19-cv-7553, *9 (N.D. Cal. Nov. 15, 2019).

to ensure accuracy of collection from payroll. It may also shed light on how obligors are instructed to handle situations in which a provider seeks to collect from an account on which a garnishment has been served.

c. Information collected through annual reports: Registrants should collect additional data on collection attempts.

The regulations require income-based advance companies to report whether collection attempts succeed on the scheduled collection date. This information is important to approximate the frequency that consumers are charged overdraft fees as a result of failed collection attempts. To further prevent overdraft fees, income-based advance companies should be required to report on whether their collection models are adjustable based on reported pay date and how frequently consumers are asked about their current pay date, in case of changes. These regulations should also impose a limit on the number of collection attempts allowed.

Note: There is a typographical error on page 7, § 1004(c). The sentence says, "'charges' include amounts received by a person from a consumer for payment of optional or discretionary services elected by the consumer in connection with *education financing*" [emphasis added] but should say "in connection with *income-based advances*."

Conclusion

The proposed rule represents a step forward in protecting California's low-income consumers and puts our state at the forefront of consumer protection efforts. That said, the rule can be further strengthened by adopting the preceding recommendations. We appreciate the opportunity to share our comments and welcome further engagement with the DFPI.

Sincerely,

California Low-Income Consumer Coalition