November 27, 2023

Ms. Clothilde V. Hewlett
Commissioner, Department of Financial Protection and Innovation
2101 Arena Blvd.
Sacramento, CA 95834
Submitted electronically to regulations@dfpi.ca.gov

Re: PRO-01-21

The undersigned groups – the Center for Responsible Lending, Consumer Federation of California, National Consumer Law Center, and Office of Kat Taylor – appreciate the opportunity to comment on the recent changes to the Department of Financial Protection and Innovation's (DFPI or Department) Proposed Regulations Under the California Consumer Financial Protection Law and the California Financing Law, California Deferred Deposit Transaction Law, and California Student Loan Servicing Act, PRO 01-21.

These comments address changes to the regulation of income-based advances and other fintech cash advances and on the amendments to the California Financing Law (CFL) clarifying the scope of the CFL and the charges subject to it.

I. Overview

The DFPI's regulatory proposal for income-based advances recognizes, rightly, that these products must be regulated as credit. This is so because the DFPI has correctly determined that "income-based advances" are loans under the CFL and that all costs associated with a transaction, whether voluntary or not, are "charges" under that statute. Those determinations are absolutely critical to any regulatory approach to fintech cash advances, and the DFPI must maintain those aspects of regulatory text in the final draft rules.

Because DFPI so correctly understands the true nature of fintech cash advances, we are deeply disturbed by DFPI's proposal to eliminate the requirement that income-based advance providers that register under the California Consumer Financial Protection Law (CCFPL) comply with the cost caps under the CFL. It will harm consumers to allow income-based advance providers to continue to operate without any cost limitation, which DFPI should restore.

It is especially dangerous and unjustified to extend this exemption to fake earned wage advance lenders and other direct-to-consumer fintech cash advances. The proposed definition of "income-based advance," covering advances "based on income the provider has reasonably

determined to have accrued," is far too loose, both in covering accrued "income," not just wages, and in allowing models that have no connection to time and attendance systems or payroll. These advances are unquestionably loans that should be covered under existing licensing and cost limitations. Any alternative registration regime should be limited, at most, to employer-integrated programs that do not debit consumer bank accounts.

A stricter definition is also essential to prevent traditional payday lenders or CFL lenders from claiming that they, too, "reasonably determine" accrued income and can use the alternative registration path. The definition of "income-based advance" should be further limited to advances that, together with all costs, are $300 or less and that are not deferred deposit transactions.

In addition to restoring the cost limits, DFPI must prohibit the other especially harmful aspects of these products by banning repeat bank account debits and the inclusion, by default, of "tips" and other purportedly voluntary payments.

Finally, if the DFPI is not going to restore the requirement that registrants comply with the CFL cost caps, we urge the Department to view these rules as just the beginning of addressing the regulatory regime for fintech cash advances. Not all providers of these loans will fall under the definition of income-based advances, and evasions should not be permitted in other markets. Moreover, the registration provisions will expire, and any separate registration regime must only be temporary. Thus, we urge DFPI not to wait four years, and to bring income-based advances fully within the CFL as soon as possible, even DFPI declines to do so at the present time.

II. DFPI Must Not Exempt Income-Based Advance Lenders from Complying with the CFL's Cost Caps.

We are dismayed by the Department's current proposal for section 1462, which allows income-based advance providers to register with the DFPI pursuant to the CCFPL, and exempts them from the requirements of the CFL, *without* needing to comply with the CFL's limits on charges. In our previous comments to the Department, we did not object to a temporary exemption for income-based advances from full CFL licensure so long as that this exemption was conditioned on compliance with the core protection of CFL's cost caps (as DFPI initially proposed). Unfortunately, the Department now proposes to dispense with this crucial protection, which will mean that income-based advance providers will not be subject to any meaningful consumer protections in the near term. This proposal is a serious misstep that must be rectified.

First and foremost, it is unwise from a policy perspective to enact a registration regime that allows registrants to avoid the CFL's cost caps. As the DFPI is aware, fintech cash advance lenders employ an array of pricing models that often obscure the true cost of the advance from borrowers and charge far more than permitted under the CFL. Across the industry, these advances carry a very high average cost of credit. As DFPI's data analysis found, the charges paid by consumers to both tip-based and non-tip companies exceeded an average of 330% annual percentage rate (APR), comparable to the average APRs for licensed payday lenders in California. As with traditional payday loans, fees multiply, as DFPI found that consumers on

average take out 36 advances a year and as many as 100. Consumers also pay heavily through so-called "voluntary" payments; three companies collected over $23 million in California in one year. Of course, consumers are harmed when they pay a high cost to access credit.

The DFPI's initial proposal protected consumers from this harm by limiting the amounts that fintech cash advance lenders could charge. In fact, that proposal struck a balance (too generous to industry, in our view) by permitting lenders to charge APRs of 213% and beyond for these loans, which is certainly sufficient return for providers to offer them. It is dismaying that the DFPI has abandoned the core consumer protection proposed in its first draft of the regulations.

Moreover, as we previously commented,[1] the CCFPL does not provide DFPI with the authority to waive or ignore the legislature's statutory commands. The CFL's cost caps are the most important aspect of the legislature's statutory scheme in the CFL, and nothing in the CCFPL gives businesses clearly subject to the CFL any leeway to skirt the core protections of the CFL (and other consumer protections laws). The Legislature adopted the CCFPL to give the Department the authority to register and regulate novel financial products *not already subject to a licensing regime*. *See* Fin. Code § 90009(a)(2)(A) (CCFPL registration unavailable for entities offering products pursuant to a statutory license). Having determined, rightly, that fintech cash advances are loans, the DFPI errs by purporting to waive the California statutory rules applicable to lenders, especially the cost caps that form the backbone of the CFL.

Accordingly, the DFPI must revive the struck language in section 1462(a)(3) or, at a minimum, remove section 1462(a).

III. It is Especially Dangerous and Unjustified for the Department to Exempt Fake EWA Lenders and Other Direct-to-Consumer Cash Advances that Have No Connection to Time and Attendance Systems or Payroll.

As proposed, the Department's definition of "income-based advance" would cover not only employer-based providers that are connected to employers' time and attendance systems and receive payment from payroll deduction or another method directly from the employer, but also to direct-to-consumer advances that have no connection to employers. Whatever the arguments about those models that have a closer to connection to actual wages, there is no justification for exempting from the CFL direct-to-consumer advances that are simply a fintech payday loan.

The Department proposes to amend its definition of "income-based advance" to require, among other things, that the advance be "based on income the provider has *reasonably determined* to have accrued" to the worker's benefit. Section 1004(g) (emphasis added). We strongly oppose this change, and urge the DFPI to revert to the prior draft language or, better yet,

[1] *See* Comments of CRL and NCLC to DFPI Re: PRO 02-21, Proposed Rulemaking under the California Consumer Financial Protection Law: Earned Wage Access at 15, 22 (Mar. 15, 2021), *available at* https://www.nclc.org/wp-content/uploads/2022/08/CRL_CA_DFPI_EWA_Comments-1.pdf

adopt our suggestion[2] to more expressly clarify that only employer-integrated lenders can qualify as "income-based advance" providers.

Because the definition of "income-based advance" determines which lenders are permitted to register with DFPI and delay complying with the CFL, the DFPI's proposed change here will allow non-employer integrated providers that are unquestionably lenders avoid any obligation to comply with the law.

While we are opposed to exempting any earned wage advance lender from substantive regulation (even if temporary), such an exemption is plainly unwarranted for direct-to-consumer lenders, which have even weaker arguments that they are not covered by existing law. Unlike employer-integrated lenders that see actual time and attendance data, direct-to-consumer lenders rely on various techniques to guess whether employees have earned but unpaid wages and, if so, how much. The pretense that the advances are earned wages is just that, a pretense. Their techniques to estimate earned wages, which are necessarily less accurate at determining the amount of earned wages, are simply an underwriting method.

EarnIn, for example, appears to rely upon scraping bank history data and various methods of "verifying earnings," which can be as undemanding as a "one-time" verification of a worker's work email.[3] If EarnIn is simply verifying *employment* for at least some borrowers, that is very different from verifying *earnings*. Lending based on the borrower having a job is, of course, what payday lenders do, and it is especially unjustified for the Department to provide a regulatory free pass (even if temporary) to "income-based advance" lenders who appear to use similar methods.

Equally critical, these direct-to-consumer lenders cannot receive repayment through a payroll deduction or other method directly from the employer and so must debit a user's bank account. That consumer repayment makes crystal clear that these are loans under existing laws and further pierces the myth that the advances were wage payments. Moreover, debiting bank accounts can trigger overdraft and NSF fees, and providers may not honor promises to reimburse such fees. Providers also do not protect consumers from late fees or returned check fees on other obligations after repayment of the cash advance drains their account.

To make matters worse, the Department proposes to include direct-to-consumer loans in the definition of "income-based advance" with a highly amorphous standard requiring only that the lender "reasonably determine[]" that the worker has accrued "income" – not even limited to wages. It is far from clear what limits the term "reasonably determine" imposes. As a result, providers may have significant latitude to use verification methods of questionable accuracy,

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[2] Comments of CRL, CFC, and NCLC in PRO 01-21 (hereinafter "CRL et al. comments") (May 17, 2023) at 12-13, *available at* https://dfpi.ca.gov/wp-content/uploads/sites/337/2023/08/32-PRO-01-21-Center-for-Responsible-Lending-et-al-5.17.23.pdf

[3] Earnin, *What are work email earnings?*, *available at* https://help.earnin.com/hc/en-us/articles/360048838514-What-are-work-email-earnings-#:~:text=EarnIn%20offers%20options%20for%20community,address%20or%20share%20the%20information.

such as relying on bank account statements like traditional payday lenders, possibly up to and including just taking the consumer's word for it.

In fact, a whole host of fintech cash advance lenders that currently do not even purport to advance wages are liable to come up with some sort of argument that they are "reasonably determining" accrued income and so are eligible for a near-term exemption from the CFL, even if these providers do not do anything meaningful to "determine" that users have earned but unpaid income. This includes even lenders that provide cash advances repaid from public benefits income, such as MoneyLion. These include:

- Klover, which offers a "cash advance … up to $2000 – even if your payday is 2 weeks away."[4] Klover advertises "zero interest or late fees. Like, legit zero-zero."[5] But Klover does collect "voluntary tips," "express fees" up to $8.49 that vary by the amount of the advance, and "subscription fees" of $3.99. [6]

- Dave, another non-bank "banking" app, which advertises "up to $500 advances with "no interest or fees."[7] Dave collects "tips" and "donations," and also charges an "Optional Express Fee" of $1.99 to $5.99, depending on the amount advanced.

- MoneyLion, another non-bank banking app, which offers "0% APR" cash advances up to $500 for "Instacash"[8] and up to $100 for "SafetyNet."[9] MoneyLion collects "tips" plus "Turbo fees" of $4.99 for instant delivery of a $40 advance. MoneyLion notes: "Any kind of income or recurring deposits, including government benefits, can help you qualify."[10]

- Brigit, previously offered advances "up to $250 with "No credit check. No interest. Pay it back without hidden fees or 'tips.'" But the Federal Trade Commission found that advances were only available through the Plus Plan, which cost $9.99/month, that few consumers were able to borrow anything close to $250, and that Brigit trapped people into paying the monthly fee and make it difficult to cancel.[11] Brigit still offers "instant cash" with "No interest or tips, ever," but it no longer promotes advances "up to $250."[12]

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[4] https://www.joinklover.com/ (visited Nov. 20, 2023).

[5] *Id.*

[6] https://www.joinklover.com/terms-and-conditions (visited Nov. 20. 2023)

[7] https://dave.com/ (visited Nov. 20, 2023).

[8] https://www.moneylion.com/instacash/ (visited Nov. 20, 2023).

[9] https://www.moneylion.com/safety-net/ (visited Nov. 20, 2023).

[10] https://www.moneylion.com/instacash/ (visited Nov. 20, 2023).

[11] Lesley Fair, Federal Trade Commission, Brigit's misleading financial practices were a bridge too far for consumers, FTC says (Nov. 2, 2023), https://www.ftc.gov/business-guidance/blog/2023/11/brigits-misleading-financial-practices-were-bridge-too-far-consumers-ftc-says.

[12] https://www.hellobrigit.com/instant-cash (visited Nov. 20, 2023).

To the extent that these proposed rules provide an exception, at least to some extent, to the licensure requirements of the CFL, it should be narrowly tailored and should not include providers who make cash advances with no connection to employers. These lenders are unquestionably making direct loans to consumers, and subjecting them to bank account debits, and thus should not be given a free regulatory pass.

IV. DFPI Must at Least Prohibit Repeat Bank Account Debits and Default Tip Amounts.

If the DFPI is nonetheless set on including these providers in the definition of "income-based advance," it must include additional protections during the registration period to protect consumers from the worst aspects of these providers' business model. Currently, the Department proposes to embed certain "consumer protections" in the definition of "income-based advance": requiring that borrowers not be personally liable for repayment and barring providers from engaging in debt collection activities. Those protections, however, are insufficient. It does not make financial sense for fintech cash advance providers to sue to collect on unpaid advances, so they already voluntarily abide by those rules.

Rather than essentially codifying providers' business model, the DFPI should try to actually protect consumers from the worst aspects of these providers' business model: potential overdraft and NSF fees, and pressure tactics to induce users to "tip." *See* ISOR at 62 (detailing ways that providers pressure users to tip). The latter protection is especially warranted because the DFPI no longer proposes to require companies to abide by the CFL cost caps, which the DFPI, rightly, originally conceived as a more effective way of policing these pressure tactics. *Id*.

Accordingly, if the Department is going to permit direct-to-consumer providers to register under the CCFPL it must require that those providers (a) not re-present failed bank account debits (thereby minimizing overdraft and NSF fees); and (b) set the pre-set default amount of any "tip" to $0. Section 1004(g) should be amended as follows (new language bolded and underlined):

> (3) The provider warrants to the consumer as part of the contract between the parties on behalf of the provider and, if applicable, any business partners partner(s) that:
>
> . . .
>
> **(C) For any provider that solicits gratuities, donations or other voluntary payments, that all such payments are optional and that the provider will set the default amount at $0.**
>
> **(D) For providers that debit the consumer's bank or prepaid account for repayment, if the provider's initial attempt to collect repayment is unsuccessful, the provider will not attempt to re-present the debit. For this paragraph, "unsuccessful" includes both instances where the provider collected nothing and instances where the amount collected was less than the dollar amount due.**

V. DFPI Must Ensure that Traditional Payday Lenders and CFL Lenders Cannot Use the Proposed Registration to Evade the Law.

By eschewing any regulation of fintech cash advance cost, the DFPI has created an incentive for traditional payday lenders to refashion themselves as "income-based advance" providers to avoid the cost and loan amount limitations in the Deferred Deposit Transaction Law. This possibility is not implausible given that the Department also proposes to expand the definition of "income-based advance" to include direct-to-consumer cash advance lenders that have no connection to employers or actual wages, and that are based on any "income" that has accrued – including public benefits. *See supra* at 3-6. It is a major mistake for the Department to create a regulatory approach (even if temporary) for fintech cash advances that payday lenders are likely to eye enviously.

This is yet another reason why we strongly urge DFPI to replace the cost limitation. If DFPI declines to do so, it must limit the registration option to employer-integrated models that do not debit bank accounts, as discussed above.

We also urge DFPI to add a provision making clear that the registration regime is not open to payday lenders. In addition, DFPI should allow the alternative registration regime only for small advances, as the harms escalate if larger loans are allowed to evade both the DDTL and the CFL. Thus, DFPI should add to the definition of "income-based advance" in proposed section 1004(g) the following (new language bolded and underlined):

<u>(4) The advance repayment, including all charges, is limited to $300 and is not a deferred deposit transaction.</u>

VI. The DFPI Must Continue to Identify Income-Based Advances as Loans and All Monies Received as Charges under the CFL.

It is critical that the DFPI has retained language in the proposed regulations clearly stating that an advance repaid by a worker's wages or other compensation for services is a loan subject to the CFL, that companies making such advances are "finance lenders" under that statute, and that all voluntary charges, including any tips and gratuities, received are "charges" under the CFL. Sections 1461, 1465. Our prior comments in this rulemaking explained in detail why the DFPI is correct on these issues, and DFPI must retain this language.[13]

While the impact of this language is limited in the near term given the DFPI's changes to section 1462(a)(3), it is nonetheless essential and must be retained in the final draft of the regulations. The clarifications will help prevent evasions by other lenders that are not providing income-based advances. For example, DFPI appropriately brought an enforcement action against SoLo Funds for violating the CFL.

In addition, DFPI can only adopt registration regimes on a temporary basis, and including the language in section 1461 and 1465 makes clear that these products will be regulated under

[13] CRL et al. comments at 3-9.

the CFL upon the expiration of the registration regime in section 1462 in four years. Thus, the Department must resist any further industry efforts to water down these provisions.

We also urge DFPI not to wait four years before revisiting the application of the CFL to income-based advances. DFPI has already been studying this market for several years, and consumers should not have to wait four more years for the industry to comply with critical consumer protections.

VII. The DFPI Rightly Struck Section 1463, Dealing with the CFL's Minimum Term Requirement.

We agree with the DFPI's decision to strike section 1463 of the draft regulations. In our prior comments, we opposed this section of the draft because it would have given *all* CFL lenders additional flexibility to offer harmful balloon payment loans.[14] It is also plainly unnecessary in light of the DFPI's decision not to require providers to comply with the CFL in the near term. Accordingly, this section should continue to be kept out of the final regulations.

VIII. We Urge the DFPI to Consider our Proposed Changes to the Data Collection Requirements.

In our prior comments, we offered numerous suggestions to section 1045, which deals with annual reporting requirements.[15] The DFPI does not appear to have accepted any of our suggestions, which is disappointing. We urge the DFPI to take another look at these suggestions that would improve the usefulness of the data that DFPI collect from registrants. In fact, the more detailed data collection regime that we proposed is all the more critical if DFPI will not subject income-based advances to CFL cost caps. Without cost caps, pricing will likely not be uniform so insight into how the industry operates is especially important.

For similar reasons, we also think it crucial that, as we suggested, DFPI commit to releasing an annual report that has aggregate data for these products. Such a report would be extremely helpful, given that there is limited public data about these products. Moreover, the CCFPL statute contemplates the legislature adopting a licensing regime based upon the DFPI's experience with registration. *See* Fin. Code § 90009(a)(2)(A). To better inform legislators and the public at large, we reiterate our call for the DFPI to routinely make public data about these products.

IX. Conclusion

Thank you for considering our comments. We urge DFPI to make further revisions to its proposed regulations to prevent consumer harm in the market for income-based advances. If further information would be useful, please reach out to Andrew Kushner at andrew.kushner@responsiblelending.org or Lauren Saunders at lsaunders@nclc.org.

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[14] CRL et al. comments at 20-22.

[15] CRL et al. comments at 14-18.

Yours very truly,

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