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Major Banks Aid in Payday Loans Banned by States

By JESSICA SILVER-GREENBERG

Major banks have quickly become behind-the-scenes allies of Internet-based payday lenders that offer short-term loans with interest rates sometimes exceeding 500 percent.

With 15 states banning payday loans, a growing number of the lenders have set up online operations in more hospitable states or far-flung locales like Belize, Malta and the West Indies to more easily evade statewide caps on interest rates.

While the banks, which include giants like JPMorgan Chase, Bank of America and Wells Fargo, do not make the loans, they are a critical link for the lenders, enabling the lenders to withdraw payments automatically from borrowers' bank accounts, even in states where the loans are banned entirely. In some cases, the banks allow lenders to tap checking accounts even after the customers have begged them to stop the withdrawals.

"Without the assistance of the banks in processing and sending electronic funds, these lenders simply couldn't operate," said Josh Zinner, co-director of the Neighborhood Economic Development Advocacy Project, which works with community groups in New York.

The banking industry says it is simply serving customers who have authorized the lenders to withdraw money from their accounts. "The industry is not in a position to monitor customer accounts to see where their payments are going," said Virginia O'Neill, senior counsel with the American Bankers Association.

But state and federal officials are taking aim at the banks' role at a time when authorities are increasing their efforts to clamp down on payday lending and its practice of providing quick money to borrowers who need cash.

The Federal Deposit Insurance Corporation and the Consumer Financial Protection Bureau are examining banks' roles in the online loans, according to several people with direct knowledge of the matter. Benjamin M. Lawsky, who heads New York State's Department of Financial Services, is investigating how banks enable the online lenders to skirt New York law and make loans to residents of the state, where interest rates are capped at 25 percent.

For the banks, it can be a lucrative partnership. At first blush, processing automatic withdrawals hardly seems like a source of profit. But many customers are already on shaky financial footing. The withdrawals often set off a cascade of fees from problems like overdrafts. Roughly 27 percent of payday loan borrowers say that the loans caused them to overdraw their accounts, according to a report released this month by the Pew Charitable Trusts. That fee income is coveted, given that financial regulations limiting fees on debit and credit cards have cost banks billions of dollars.

Some state and federal authorities say the banks' role in enabling the lenders has frustrated government efforts to shield people from predatory loans — an issue that gained urgency after reckless mortgage lending helped precipitate the 2008 financial crisis.

Lawmakers, led by Senator Jeff Merkley, Democrat of Oregon, introduced a bill in July aimed at reining in the lenders, in part, by forcing them to abide by the laws of the state where the borrower lives, rather than where the lender is. The legislation, pending in Congress, would also allow borrowers to cancel automatic withdrawals more easily. "Technology has taken a lot of these scams online, and it's time to crack down," Mr. Merkley said in a statement when the bill was introduced.

While the loans are simple to obtain — some online lenders promise approval in minutes with no credit check — they are tough to get rid of. Customers who want to repay their loan in full typically must contact the online lender at least three days before the next withdrawal. Otherwise, the lender automatically renews the loans at least monthly and withdraws only the interest owed. Under federal law, customers are allowed to stop authorized withdrawals from their account. Still, some borrowers say their banks do not heed requests to stop the loans.

Ivy Brodsky, 37, thought she had figured out a way to stop six payday lenders from taking money from her account when she visited her Chase branch in Brighton Beach in Brooklyn in March to close it. But Chase kept the account open and between April and May, the six Internet lenders tried to withdraw money from Ms. Brodsky's account 55 times, according to bank records reviewed by The New York Times. Chase charged her $1,523 in fees — a combination of 44 insufficient fund fees, extended overdraft fees and service fees.

For Subrina Baptiste, 33, an educational assistant in Brooklyn, the overdraft fees levied by Chase cannibalized her child support income. She said she applied for a $400 loan from Loanshoponline.com and a $700 loan from Advancemetoday.com in 2011. The loans, with annual interest rates of 730 percent and 584 percent respectively, skirt New York law.

Ms. Baptiste said she asked Chase to revoke the automatic withdrawals in October 2011, but was told that she had to ask the lenders instead. In one month, her bank records show, the lenders tried to take money from her account at least six times. Chase charged her $812 in fees and deducted over $600 from her child-support payments to cover them.

"I don't understand why my own bank just wouldn't listen to me," Ms. Baptiste said, adding that Chase ultimately closed her account last January, three months after she asked.

A spokeswoman for Bank of America said the bank always honored requests to stop automatic withdrawals. Wells Fargo declined to comment. Kristin Lemkau, a spokeswoman for Chase, said: "We are working with the customers to resolve these cases." Online lenders say they work to abide by state laws.

Payday lenders have been dogged by controversy almost from their inception two decades ago from storefront check-cashing stores. In 2007, federal lawmakers restricted the lenders from focusing on military members. Across the country, states have steadily imposed caps on interest rates and fees that effectively ban the high-rate loans.

While there are no exact measures of how many lenders have migrated online, roughly three million Americans obtained an Internet payday loan in 2010, according to a July report by the Pew Charitable Trusts. By 2016, Internet loans will make up roughly 60 percent of the total payday loans, up from about 35 percent in 2011, according to John Hecht, an analyst with the investment bank Stephens Inc. As of 2011, he said, the volume of online payday loans was $13 billion, up more than 120 percent from $5.8 billion in 2006.

Facing increasingly inhospitable states, the lenders have also set up shop offshore. A former used-car dealership owner, who runs a series of online lenders through a shell corporation in Grenada, outlined the benefits of operating remotely in a 2005 deposition. Put simply, it was "lawsuit protection and tax reduction," he said. Other lenders are based in Belize, Malta, the Isle of Man and the West Indies, according to federal court records.

At an industry conference last year, payday lenders discussed the benefits of heading offshore. Jer Ayler, president of the payday loan consultant Trihouse Inc., pinpointed Cancún, the Bahamas and Costa Rica as particularly fertile locales.

State prosecutors have been battling to keep online lenders from illegally making loans to residents where the loans are restricted. In December, Lori Swanson, Minnesota's attorney general, settled with Sure Advance L.L.C. over claims that the online lender was operating without a license to make loans with interest rates of up to 1,564 percent. In Illinois, Attorney General Lisa Madigan is investigating a number of online lenders.

Arkansas's attorney general, Dustin McDaniel, has been targeting lenders illegally making loans in his state, and says the Internet firms are tough to fight. "The Internet knows no borders," he said. "There are layer upon layer of cyber-entities and some are difficult to trace."

Last January, he sued the operator of a number of online lenders, claiming that the firms were breaking state law in Arkansas, which caps annual interest rates on loans at 17 percent.

Now the Online Lenders Alliance, a trade group, is backing legislation that would grant a federal charter for payday lenders. In supporting the bill, Lisa McGreevy, the group's chief executive, said: "A federal charter, as opposed to the current conflicting state regulatory schemes, will establish one clear set of rules for lenders to follow."

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Dimon Pledges to Change JPMorgan's Practices on Payday Loans

By JESSICA SILVER-GREENBERG

Jamie Dimon, the chief executive of JPMorgan Chase, vowed on Tuesday to change how the bank deals with Internet-based payday lenders that automatically withdraw payments from borrowers' checking accounts.

At an investor meeting on Tuesday, Mr. Dimon called the practice, which was the subject of an article in The New York Times on Sunday, "terrible." He said JPMorgan was examining the issue and would make changes.

While JPMorgan Chase does not make the loans directly, the bank, along with other giants like Bank of America and Wells Fargo, enable the online payday lenders to deduct payments from customers' checking accounts, even in the 15 states where the loans are banned entirely. The withdrawals sometimes continue even after customers have pleaded with the banks to prevent the lenders from tapping their accounts.

The banks are a critical link for payday lenders, which are increasingly moving online, to evade statewide caps on interest rates. The loans can carry annual interest rates above 500 percent. Without access to customers' checking accounts, the lenders, according to state and federal authorities, would not be as easily able to make loans to residents in states where high-interest payday loans are banned.

Lawmakers have taken aim at the issue, too. In July, Senator Jeff Merkley, Democrat of Oregon, introduced a bill that would restrict the payday lenders by forcing them to follow laws in states where the borrower is located, rather than where the lender is. Another crucial aspect of the bill, which is pending in Congress, is a provision allowing borrowers to more easily stop the automatic withdrawals.

For payday loan customers, many of whom are shouldering a glut of overdue bills, the automatic withdrawals sometimes cause a wave of fees.

According to a report released this month by the Pew Charitable Trusts, an estimated 27 percent of payday loan borrowers say the loans caused them to overdraw their accounts.

In the Times article on Sunday, two JPMorgan Chase customers explained their travails in trying to persuade the bank to halt automatic withdrawals.

Ivy Brodsky, one customer in Brooklyn, was charged $1,523 in fees by Chase, after six Internet payday lenders tried to take money from her account 55 times in a single month. Ms. Brodsky thought the withdrawals would stop after she visited her Chase branch in March to close the account.

Subrina Baptiste, an educational assistant in Brooklyn, said the overdraft fees charged by Chase ate into her child-support income. Ms. Baptiste said she begged Chase to stop automatic withdrawals on loans she got in 2011.

Under New York law, the loans, which came with interest rates of more than 500 percent, are illegal.

Both Ms. Baptiste and Ms. Brodsky sued Chase in federal court in New York last year. JPMorgan Chase said in a statement on Tuesday that it was "in discussions with these customers to resolve their issues" and added that the bank apologized "to them for the problems they had."

JPMorgan officials are "taking a thorough look at all of our policies related to these issues and plan to make meaningful changes," the statement said.

A spokeswoman for the American Bankers Association did not have an immediate comment.

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Bleeding the Borrower Dry

New York is one of 15 states that have banned the predatory, high-interest loans that payday lenders commonly use to pillage low-income borrowers. But offshore lenders increasingly get around state laws by issuing predatory loans over the Internet. Worse still, as the Times's Jessica Silver-Greenberg reported recently, banks in the state are profiting from the loans by allowing the Internet lenders to automatically withdraw payments from the borrower's account, in some cases without his or her permission. When the borrowers — or their lenders — overdraw on the accounts, the banks get to collect fat overdraft fees.

About 12 million borrowers turn to payday lenders each year. The loan model that lures them in is based on deception. Customers are told, for example, that they can borrow small amounts, perhaps a few hundred dollars, which they are supposed to repay in full within a short period, typically two weeks. The promotional material does not let on that the loans, which carry annual interest rates of 500 percent or more, are structured in a way that inevitably turns a short-term obligation into long-term debt.

A new study by the Pew Charitable Trusts finds, for example, that only about 14 percent of borrowers can afford to take enough out of their monthly budget to repay the average payday loan. Instead, average borrowers carry a debt for five months, during which time they pay repeated fees to renew the loan. By the fifth month, someone who borrowed $375 will have paid about $520 in interest alone. Many also resort to borrowing from another payday lender. Not surprisingly, payday borrowers are more likely than others to default on credit card debt, to file for bankruptcy or to lose their bank accounts because of abuse of overdraft privileges.

New York State passed one of the strongest anti-usury laws in the nation in 1976, making it a felony for lenders to charge in excess of 25 percent interest. Even so, New Yorkers are still preyed upon by out-of-state payday lenders, which collect payments through an automatic withdrawal process.

Under federal law, bank customers have a right to revoke a creditor's automatic withdrawal privileges. They can also simply close an account whenever they choose. A federal lawsuit brought against JPMorgan Chase Bank by two customers in New York shows how difficult exercising these rights can be.

One plaintiff was besieged by payday lenders that had charged her an annual interest rate of nearly 800 percent — clearly illegal in New York — and continually tried to debit her bank account, triggering $34 overdraft fees. She asked the bank in March 2012 to close her account, but it remained open for two months, during which the lenders attempted to debit her some 55 times, ringing up $1,523 in overdraft and other fees.

Chase has promised to revisit its policies. But judging from consumer complaints nationally, this problem is not unique to New York. Congress and state governments need to crack down on these practices.

A bill pending in the Senate, known as the Safe Lending Act, would require all online lenders to comply with state laws that provide stronger consumer protections than the federal statutes. It would establish once and for all that payday loan borrowers have the right to stop lenders from raiding their bank accounts. State and federal regulators also need to prohibit banks from giving payday lenders access to the automatic payment system in states where predatory, high-interest loans are illegal.