The Fight to Stop Predatory Lending in Pennsylvania

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The Federal Reserve has lowered the federal funds rate twice in the past four months. These cuts can sometimes help would-be borrowers by reducing interest rates for things like automobile loans or credit card debt. Or so one would think. For a large number of Philadelphians, particularly those already saddled with debt and without significant savings, these cuts do nothing to stave off the groundswell of predatory lenders seeking to take advantage of the economically vulnerable.

While some loans may appear to help borrowers in the short term, the reality is that predatory lending traps its victims in debt, leaving them without enough money to pay for even basic expenses such as food and housing. Getting caught in a cycle of predatory lending can mean never-ending interest payments and long-term debt that makes financial security for the borrowers impossible. The fallout from predatory loans affects not only the individuals and families targeted by these lenders, but the whole city—while the lenders simply profit and walk away.

Enforcing and preserving consumer protections are a critical component to reducing poverty in Philadelphia. Organizations like Community Legal Services (CLS), together with the private bar, have worked for years to advocate for Philadelphians who have fallen prey to predatory lenders. That effort is central to CLS' larger goal of reducing poverty in Philadelphia; fighting poverty means not only making sure people have money in their pockets, but that predatory institutions are not able to take it out. When predatory lending is curtailed, our city as a whole benefits.

On Oct. 17, Justice Rising Advocates, CLS' young professionals group, presented a CLE on predatory lending. Attendees heard from experts in the field and learned about the key issues impacting victims of predatory lending. This article highlights some of the key areas of concern regarding predatory lending.

The Fallout of Predatory Mortgage Lending

Even a decade after the collapse of the subprime mortgage market helped trigger the great recession, Philadelphians are still reeling from the aftershocks. Once the mortgage bubble popped, countless individuals faced foreclosures due to predatory lending practices, such as "no doc" loans, where the lender would issue loans without proper underwriting and the loans would be stacked with fees, balloon payments and unaffordable terms. The result has been that Philadelphia, long a city of homeowners, saw an 8% decline in home ownership between 2007 and 2017.

While current mortgage lending protections at both the federal and state level have helped stave off predatory lending, new issues continue to develop. Abuses in the reverse mortgage market, predatory rent-to-own schemes, and predatory property wholesalers are three such schemes that have made a resurgence in the post-recession era. CLS has been diligently addressing these issues through ongoing consumer protection vigilance, policy advocacy and litigation.

The Impact on Small Businesses

When owners of small businesses need capital to get their businesses off the ground, predatory merchant cash advance companies try to take advantage of them. One key instance where small businesses often fall prey to harmful practices is through "confessions of judgment," a contractual agreement that requires small businesses to accept liabilities without going through the court proceedings offered to consumers. Confessions of judgment have been banned for consumers since the 1980s, but small businesses are often subject to these agreements as part of complex contracts they sign but may not fully understand.

As Shane Heskin, an attorney at White and Williams testified to Congress, "My clients are very good at what they do. They know how to fix a boat. They know how to install a sink. But that doesn't mean they know how to read a contract in eight-point font. It doesn't mean they know the legal ramifications of signing a confession of judgment."

When a small-business owner contractually agrees to a confession of judgment, it essentially means they agree to automatically lose if there is a dispute between them and a lender. The lender can accuse them of not paying and then submit the confession of judgment to the small-business owner's bank, leaving the small-business owner without the necessary funds to run their business and forcing many to close.

Pennsylvania's Strong Consumer Protection Laws

So-called "payday" loans are small, short-term loans that may carry huge interest rates exceeding—in some parts of the country—annual percentage rates of 300% or more. Their name comes from the fact that the loans are supposedly designed to be repaid on the borrower's next payday in two weeks or a month. While often pitched as "quick fix" loans to cover short-term expenses, payday loans in practice can trap low-income consumers in debt, forcing the borrower into repeatedly taking out high-fee, high-interest loans (and often with additional penalties for extending repayment terms). According to a 2006 report by the Department of Defense on predatory lending practices, these loans may include other onerous terms as well, such as high-cost ancillary products whose cost is not included in computing interest rates and provisions that waive the borrower's right to meaningful legal redress. Predatory lending to members of the armed services was so harmful that the Department of Defense even concluded that the practice even "undermined" our "military readiness" as a nation.

Pennsylvania has one of the strongest legal regimes in the country for protecting borrowers from predatory short-term, high interest rate loans. Our state is one of 16, plus the District of Columbia, that has kept predatory payday lenders at bay, saving Pennsylvania residents more than $272 million dollars a year. Pennsylvania law strictly limits the interest rates that can be charged on small consumer loans, including through the Consumer Discount Company Act and the Loan Interest and Protection Law. Pennsylvania's consumer-friendly laws have also been paired with robust public enforcement. The commonwealth's banking department, for example, has successfully enforced our law against out-of-state lenders making loans over the internet to Pennsylvanians, an enforcement action that was unanimously upheld by the Pennsylvania Supreme Court in *Cash America Net of Nevada v. Commonwealth, Department of Banking*, 8 A.3d 282 (Pa. 2010).

In the past few years, however, there have been efforts to change Pennsylvania's laws in ways that would allow predatory lenders to make inroads into the state and prey on vulnerable borrowers.

Just last session, House Bill 2429 was proposed in Pennsylvania, which would have allowed payday lenders to target Pennsylvania consumers as "loan brokers," charging unlimited fees that would not be deemed "interest." While that bill was defeated—thanks in part to advocacy efforts by groups like Community Legal Services—predatory lenders have proven endlessly creative in finding ways around consumer protection regimes.

The most recent attempt to evade Pennsylvania law involves lenders who use the guise of Native American tribes as fronts to evade consumer protection laws. As sovereign parties, Native American tribes are able to charge higher interest rates than those allowed under Pennsylvania law. Payday lenders are beginning to "rent" tribes in attempts to circumvent Pennsylvania law. The Attorney General's Office, working with Irv Ackelsberg, of Langer, Grogan, & Diver, has sued to stop the firms that are attempting to use tribes to cover their illegal lending practices. ▪

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