

IUCCC CHAPTER 7 SMALL LOAN QUESTIONS & ANSWERS July 1, 2012

Question: What remedies may be imposed if a licensed lender makes a loan that does not qualify as a small loan under IC 24-4.5-7-104, is for a term shorter than that specified in IC 24-4.5-7-401(1), or is made in violation of:

IC 24-4.5-7-201 - Finance charges

IC 24-4.5-7-401 - Term of loan; consecutive small loans; extended payment plans

IC 24-4.5-7-402 - Limits based on borrower's income; payments; loan documents; rescission; renewals prohibited

IC 24-4.5-7-404 - Limits and number and amounts of outstanding loans; lender's verification; third party data base; civil penalties; excess finance charges; verification of Social Security number

IC 24-4.5-7-410 - Prohibited acts by lender

Answer: Per IC 24-4.5-7-102(3) such a loan is subject to the Code, and the department **may** conform the finance charge for a loan described in this subsection to the limitations set forth in IC 24-4.5-3-508 (maximum rates for supervised loans).

Refundable violations under IC 24-4.5-7-102(3) will be calculated by reducing the finance charge to 36%.

The exception is on a loan rescinded by a borrower within one business day from the date of the loan, and in this case no finance charge is earned.

Question: Can a lender require that a borrower give them authorization to debit their checking account through an Automated Clearinghouse (ACH) authorization as part of the standard language in the small loan agreement? See IC 24-4.5-7-104(b) and 7-109(1).

Answer: Yes, because a small loan has one scheduled payment. The voluntary election rule applies to credit payable in installments.

Question: IC 24-4.5-7-110 defines gross monthly income as that income received in the 30-day period preceding the borrower's application for a small loan. Can the lender count all gross income in the 30 day period if the borrower is actually paid 3 times bi-weekly or 5 times weekly during that 30-day period?

Answer: No. The 30 day period was adopted to prevent monthly income recipients being refused loans because they had no income in the previous period defined by statute (28 days).

The lender should multiply the borrower's regular gross income by the number of times they are typically paid in a 30-day period. For example, a person paid weekly will normally be paid 4 times in that period, so the regular gross income would be multiplied by 4 to determine the gross monthly income. For a person paid bi-weekly, it would be multiplied by 2. Actual practices of lenders will be monitored at the time of examination.

Question: What is regular gross pay as outlined by IC 24-4.5-7-110?

Answer: Regular gross pay is that documented income the borrower receives on a regular basis from wages, salary, retirement benefits, or social security income, or other defined benefits.

Question: What method or formula is used to determine the maximum amount a borrower can be loaned on a small loan if the borrower has another small loan outstanding?

Answer: The combined amount on two small loans may not exceed \$605, exclusive of finance charges, and the maximum is also limited by monthly gross income. A borrower's eligibility amount is computed by determining the outstanding balance (original principal amount, plus NSF fee, minus partial payments) on an existing loan, and deducting that amount from \$605. Once again, this aggregate amount is limited further by the monthly gross income test.

Question: What must a small loan licensee maintain to substantiate the amount of regular gross income the borrower has earned when determining the loan amount permitted under IC 24-4.5-7-402(1)?

Answer: The borrower is to provide tangible proof of all income received during the 30-day period prior to the loan application before a loan is made. This would protect the lender from using incorrect information and ensure their compliance with the statute. In those instances where all documentation is not available, the lender should document why the records are not available. The DFI will look at what is in file and attempt to be as fair as possible, but cautions that lack of records should be the exception rather than the rule.

The DFI will accept pay stubs issued within 30 days of the loan date for borrowers paid more than once in the 30 day period provided the lender does not take advantage by continually using an inflated pay record to make higher loans.

Question: What is the maximum percentage of monthly gross income a consumer can borrow on a small loan transaction, or a combination of transactions?

Answer: The principal amount and finance charge (total of payments) on the small loan to be issued, plus any other small loan balances (computed by adding the principal plus the finance charge plus NSF fee, and deducting all partial payments) the borrower has outstanding with any lender, may not exceed 20% of the borrower's monthly gross income. The 20% requirement will apply to all loans rather than per lender.

Question: May the borrower pamphlet required under IC 24-4.5-7-301(4) be given to the borrower either as a separate pamphlet or incorporated as part of the loan document?

Answer: Yes, either is acceptable.

Question: After a borrower has completed the cycle of an initial small loan and five subsequent consecutive small loans outlined by IC 24-4.5-7-401(2), what options are available to the lender and borrower?

Answer: If five consecutive small loans have been made to a borrower after the borrower's initial small loan (total of six loans), another small loan may not be made to that borrower within seven days after the sixth loan is paid in full.

Recognizing the existence of the payday lender database, and consistent with the wording of the statute, the 7-day cooling off period will be applied on an industry wide basis, rather than a lender basis.

The first exception to this rule is if the borrower has not defaulted on the fifth consecutive small loan the borrower shall be permitted to request an extended payment plan.

The second exception is when a borrower has loans with two separate lenders. When a loan sequence reaches the 7-day cooling off period with one of the lenders, the other lender may continue to offer the borrower consecutive small loans until that sequence reaches the 7-day cooling off period, or until the consecutive small loan count is broken with that lender.

Borrowers may request an EPP if they have not defaulted on the outstanding small loan and if they owe on a 3rd, 4th, or 5th consecutive small loan. The EPP must have at least 4 equal installments covering not less than 60 days. The lender may not assess any fee or charge for an EPP. The EPP must be in writing and signed by both the borrower and the lender. A borrower may not enter into another small loan with any other lender while engaged in an EPP except as detailed below. An EPP is an extension of an outstanding small loan and not a new loan.

If a borrower uses the EPP on a 5th consecutive small loan, the borrower may not enter into another small loan transaction with any lender until 7 days after the EPP is paid in full.

There is an exception if a borrower has loans with two separate companies. In this instance, when a borrower is in an EPP with one of the lenders, the other lender may continue to offer the borrower consecutive small loans until that sequence reaches the 7-day cooling off period, or until the consecutive small loan count is broken with that lender.

Question: Does the DFI have an approved disclosure for the extended payment plan (EPP) as outlined in IC 24-4.5-7-401(3), effective July 1, 2007?

Answer: A model form is posted on the DFI website. A lender may use this sample form, create a similar form, or separate the disclosure of the EPP from the contractual provisions concerning the EPP.

Question: When will the 7-day "cooling-off period" required by IC 24-4.5-7-401(2) begin to be calculated if the borrower pays off their account in full prior to, or after, the maturity date of the loan?

Answer: On the date paid in full.

Question: What types of changes to a licensee require notice to the Department?

Answer: IC 24-4.5-3-505(6) and (7) require notice of branch changes, changes in officers, conviction of a felony, etc. IC 24-4.5-3-515 details the process for notification to DFI of a Change of Control. Lenders should also review IC 24-4.5-7-405 regarding other business conducted at licensed locations. Finally, lenders should be aware that additional branch locations would require evidence of increased bonding as outlined in IC 24-4.5-7-413.

Question: Why is the Department requiring the use of a third party Database by all licensed small loan lenders?

Answer: IC 24-4.5-7-404(5) requires the Department to monitor the effectiveness of private consumer reporting services in providing verification of outstanding loans, and to determine if one or more of these reporting services is deemed "commercially reasonable." Upon making such a determination, the Department is to notify each licensee of the existence of the Database product that meets this test, and to require the use of the Database by each licensee. The Department has been presented with a Database product from a provider deemed to have met the test of "commercially reasonable."

Question: What is the purpose of the statutory requirement of using a Database?

Answer: The purpose of the Database is to ensure compliance with the following statutory limitations:

- a. IC 24-4.5-7-404(3): A lender shall not make a small loan that, when combined with the outstanding balance on another outstanding small loan owed to another lender, exceeds a total of \$605, excluding finance charges.
- b. A lender shall not make a small loan to a borrower who has two (2) or more small loans outstanding, regardless of the total value of the small loans.

Question: What was the mandatory effective date for each licensee to comply with database requirements?

Answer: Each licensee was required to be operational with a Department designated commercially reasonable third party Database provider no later than November 1, 2005.

Question: What is required of each licensee in regard to using the Database when making a loan?

Answer: Each licensee must register each loan with the third party Database prior to making the loan. The licensee must obtain a transaction authorization number ("TAN") for placement on the loan agreement to confirm the inquiry and the borrower's eligibility.

Question: What is the process for registering loans on the Database?

Answer:

- a. Licensee conducts a search of the Database based upon either a social security number, alien registration number, or ITIN number of the borrower seeking a new small loan. The Database will provide the result of the search to the inquiring licensee;
- b. If the borrower is eligible for a new small loan, the licensee may submit all of the required information on an applicant necessary to have the small loan registered with the Database;
- c. Upon receipt of the required information, the Database provider will open a small loan, assign a TAN, and the TAN will be communicated to the licensee as evidence that the transaction has been recorded with the Database;
- d. The licensee shall place the TAN on the small loan agreement; and
- e. Provide a copy of the agreement to the borrower.

Question: What information should be provided to a borrower when the licensee determines that they may not enter into a new loan due to Small Loan Act (SLA) limitations?

Answer: The licensee must provide a written explanation stating the specific reason under the SLA for the declined eligibility. For example, the licensee may not enter into a small loan with a borrower that already has an outstanding small loan with this lender, has two outstanding small loans with other lenders, is in a waiting period with this lender, or other reasons associated with the SLA. If the reason for the declined eligibility is based on information obtained from the Database, then the written explanation should include the customer service telephone number for the Database provider.

Question: What if a consumer states that the information being given to the licensee via the third party Database about the consumer's current outstanding loans is inaccurate?

Answer: The consumer should be able to obtain information directly from the third party Database provider as to the consumer's ineligibility for a new small loan.

Question: What is the licensee's responsibility for updating the Database when cash or a check is presented for deposit as payment in full?

Answer: Each lender must immediately update the database to indicate that the transaction is "closed":

- a. upon receipt of cash from the borrower to redeem the check; or
- b. when the borrower's check is deposited or presented for payment or when an electronic debit is executed. The timing of this deposit/presentation is subject to the policy of each lender. An account is considered closed when the lender deposits the check.

Lenders are not permitted to institute policies or procedures involving delayed deposits designed to limit the ability of borrowers to engage in other small loan transactions

Question: What must a licensee do with respect to the Database when a borrower's check is returned unpaid by the financial institution?

Answer: If a check or electronic debit does not clear the financial institution, the licensee must immediately reverse the prior payment entry on the Database to re-open the loan.

Question: If a borrower makes a partial payment, is the lender required to update the account in the database?

Answer: A lender shall report partial payments to the database when such payments are made, and such payments will affect the calculation of the amount the consumer is eligible to borrow.

Question: What must a licensee do when a borrower exercises his/her right to rescind a loan?

Answer: The licensee must immediately close the loan in the Database using procedures prescribed by the Database provider. A loan is deemed "rescinded" if the borrower pays off the loan in full within one business day.

Question: Can a licensee close a loan in the Database when the loan is sold to a third party collection agency?

Answer: The policy of the Indiana DFI is unpaid loans are to remain open on the database. The lender should not close loans that are sold to third party collection agencies.

Question: Can a licensee close a loan in the Database when the loan is charged off?

Answer: The policy of the Indiana DFI is unpaid loans are to remain open on the database. The lender should not close loans when they are charged off.

Question: What access options will licensees have with respect to communicating with the Database?

Answer: Each licensee must have either real-time integrated access through the licensee's in-house system, or connect via Internet access to the third party Database.

Question: How must a licensee proceed in the event its in-house integrated system or Internet capability is down?

Answer: In the event the licensee's system prevents electronic access to the Database, the licensee must use alternate procedures established by the Database vendor to check borrower eligibility, register the loan, and secure a TAN prior to making a loan. Once the licensee's systems issues are resolved, the licensee must update the Database with any additional information about the transactions (e.g., payments received, etc.) as soon as possible, but not later than 24 hours after Database access is restored. If a licensee cannot meet this timetable for updating the Database, the Department must be notified immediately. Also, any time the licensee's system is down for more than four hours, the licensee must notify the Department immediately.

Question: How must a licensee proceed in the event that electronic access to the Database is unavailable due to the Database vendor's systems problems?

Answer: In the event electronic access to the Database is unavailable due to the Database vendor's systems problems, the licensee must proceed using the Database provider's alternate procedures to check borrower eligibility, register the loan, and secure a TAN. Once the Database provider resolves its systems issues, the licensee must update the Database with any payments received as soon as possible, but not later than 24 hours after the system is restored. If a licensee cannot meet this timetable for updating the Database, the licensee must notify the Department immediately.

Question: How must a licensee proceed in the event that no electronic or alternate means of access to the Database is available due to the Database vendor's systems problems?

Answer: The licensee will revert to its prior procedures (customer certification, internal systems) for determining borrower eligibility while the Database is unavailable. The Database provider will supply the licensee with a notice, via electronic mail or facsimile, indicating the unavailability of the Database. The Database provider will also provide the Department with immediate notice of their unavailability via email or facsimile. A copy of this notice shall be attached to each small loan agreement during the period of unavailability, and another copy retained in the loan file. The licensee will be required to attempt to register each new loan transaction during the period of unavailability unless a specific period of outage is indicated by the Database provider. Once the Database operation resumes, the licensee must access the Database and enter all new loans and update the Database with any loan payments as soon as possible, but not later than 24 hours after the system is restored. If a licensee cannot meet this timetable for updating the Database, the licensee must notify the Department immediately.

Question: What records must be kept by the licensee in regard to the Database?

Answer: All records of a small loan transaction including loan disclosures, payment histories, collection account information and Database information must be retained for at least two years after the account is paid in full as outlined in IC 24-4.5-3-505(1).

Question: What is the licensee's responsibility for the accuracy of its borrowers' information on the Database?

Answer: Licensees shall immediately update loans registered with the Database to ensure that all identifying information regarding both the borrower and the transaction is accurate.

Question: Has the Department imposed any "Know Your Customer" record keeping requirements?

Answer: Yes. All licensees must implement procedures to verify the unique social security number or TIN provided by the borrower is legitimate. Photocopies of documents used to verify the accuracy of the unique number must be retained in borrowers' files.

Question: How will the Department utilize the information stored in the Database in its regulatory efforts?

Answer: The Department will review reports generated from the Database to ensure compliance with the provisions of IC 24-4.5-7-404(3). Database reports will be compared with the licensee's records to ensure proper implementation of this guidance. Database reports will also be used by Department examiners as a general examination tool.

Question: What will ensure that all licensees enter all transactions at the time a loan is made and at the time a loan is paid in full?

Answer: The Department fully understands that for a Database to be effective in ensuring compliance with the statutory requirements of the Act all licensees must be held fully accountable in terms of entries into the Database both for new loans and loans paid in full. The Database provider will make reports available to the Department to help determine compliance. Licensees will also be required to keep full records on all transactions. A licensee's failure to comply will prompt immediate corrective action by the Department up to and including license revocation procedures.

Question: Can a lender require a borrower to redeem a check issued in conjunction with a small loan for cash?

Answer: A lender may not require a borrower to physically return to a lender to redeem a check issued in conjunction with a small loan. It is the option of the borrower to return to a lender and redeem a check for cash, or to allow the check to be deposited or presented for payment.

Question: What affect does a bankruptcy filing have with respect to any open small loan?

Answer: A small loan will be "terminated" and must be closed in the database if the debt is specifically discharged in bankruptcy. Otherwise, the loan is treated as any other small loan - it remains outstanding until the debt is paid in full.

Question: How are maximum permissible finance charges computed on small loans?

Answer: The step rate structure is in place.
15% on the first \$250 of the principal,
13% on the amount of principal greater than \$250 and less than or equal to \$400, and
10% on the amount of principal greater than \$400.

Question: What fees are permitted on small loans?

Answer: The only fee permitted (in addition to the finance charge) on a small loan is one return item fee (NSF fee) for each returned or dishonored item. This additional charge may be assessed one (1) time regardless of how many times a check or an authorization to debit the borrower's account may be submitted by the lender and dishonored. The maximum amount of this fee is \$25.

A lender may still file legal action against a borrower, but cannot file/claim any additional costs incurred by the lender, such as attorney fees and treble damages, as per prior advice from the DFI. The court may award court costs and post judgment interest. A lender may present a borrower's check for payment or exercise a borrower's authorization to debit the borrower's account not more than 3 times. The 3 presentment limit is consistent with other check presentment regulations and ACH rules.

Question: What happens to the accounts of a lender who stops doing business in Indiana?

Answer: These situations are handled on case by case bases, but the Director may require certain actions by the database provider to reflect an updated status of the accounts.

Question: What are the civil penalty provisions available to the Director for violations of Section 7-404 regarding the database?

Answer: The Director may impose a civil penalty of \$100 per violation of this Section or any rule or policy adopted to implement Section 7-404. The Director may also impose a civil penalty not greater than \$10,000 per violation after notice and opportunity for a hearing when the Small Loan Act is violated in addition to any other penalty as outlined by IC 24-4.5-6-113.

Question: Do the provisions of the Small Loan Act apply to out-of-state or Internet lenders who solicit loans with Indiana residents?

Answer: Yes, the territorial application Section of the IUCCC has been modified as of July 1, 2007 to require these lenders to become licensed, and to comply with the Chapter 7, Small Loans, if they solicit from and make small loans to Indiana residents.

Question: Can income from more than one person be used to determine the total amount of eligibility on a small loan?

Answer: No. A small loan is limited to 20% of the monthly gross income of one borrower, and the loan is recorded on the database under one borrower's identification number. Any other person (such as a spouse) with income must qualify independently for a small loan and have that loan registered on the database under their identification number.