

Consumer credit allows families to manage their budgets and pay for unexpected expenses. Texas' Consumer Credit Code limits the rate of interest that lenders can charge and prohibits loan terms that are abusive to borrowers.

Texas has set reasonable limits on interest rates since it was a republic. Such usury limits balance the interest of lenders with those of borrowers and prevent "loan sharking" and other abusive practices. Though current statutory limits on interest rates still allow lenders to charge high rates to riskier borrowers, lenders have also used loopholes in the law to increase their interest charges far above the statutory caps.

Unfortunately, loan sharking is back. Some lenders exploit loopholes in our credit laws and charge far more than the credit code allows. These loans—termed "sale-leaseback" agreements—use a personal check for collateral and often carry interest rates of several hundred percent. Ostensibly short term loans designed to help borrowers through a crunch to the next paycheck, they can quickly devolve into a long term credit problem if the borrower can't pay back the amount borrowed plus the fee in the initial two weeks. Consumer complaints filed with the Office of Consumer Credit Commissioner outline the desperation of borrowers who struggle to make their payments and never see a decline in principal. Many people end up paying far more in fees than they ever borrowed and still cannot pay off the initial loan.

To make sure borrowers pay these usurious rates, lenders require a personal check, so if the borrower can't make a payment, the lender can cash or threaten to cash the check.

A Usury Loophole- The Sale-Leaseback Arrangement

Lenders say its not a loan, but to the people who "sell" their microwaves, TVs, or washing machines and can't "buy" them back after two weeks, it feels like loan sharking.



Without sufficient funds to cover the check, the borrowers risk jail if they cannot keep up with the steep interest charges.

Indeed, it is not only the usurious interest, but the threat to use our court systems to enforce these loans that makes the loans particularly abusive. If these loans were not disguised they would clearly be illegal under Texas' longstanding usury protections. Lenders disguise them to get through a loophole in the law – one that should be closed.

Lenders say these transactions are not loans. Under a sale-leaseback arrangement, a lender supposedly "buys" an item, such as an appliance, from the consumer for an amount of money (the amount borrowed) and "leases" it back for a "rental" payment (the interest charge). Although the lender claims to purchase the item, the "sale" really is an attempt to disguise the true nature of the transaction - a loan - and the item remains with the consumer at all times. The interest rate charged for these types of loans may exceed 700 percent APR.

The Texas Finance Commission has authorized check-secured "payday" loans under Texas laws. The "sale-leaseback" system is an attempt

to avoid rules put in place for "payday" loans that protect consumers from a downward debt spiral. Though these rules still allow for very high interest rates, they prohibit multiple rollovers and therefore protect consumers from a plunge into uncontrollable debt.

Very high interest rates financially devastate Texas families. Such abusive lending practices provide a glimpse into what might happen if Texas were to repeal its existing usury limits for consumer loans.

Recommendations

- Keep existing consumer protections for consumer loans. Usury limits on loans of only a few hundred dollars are already quite high, and should not be increased.
- Close the existing loopholes that allow abusive practices like sale-leasebacks. Assure consumers that they will pay reasonable rates, under fair terms, when they borrow money.
- Modify regulation of credit transactions,

if necessary, only for those who can afford to bring attorneys and accountants to negotiate the terms offered (like large business transactions).

In Short

Usury laws have protected borrowers from loan sharking since Texas was a republic. Elimination of rate caps would allow lenders to take advantage of the most vulnerable people, and exacerbate the already troubled finances of many families.