

BILL ANALYSIS

C.S.S.B. 1143
By: Carona
Financial Institutions
Committee Report (Substituted)

BACKGROUND AND PURPOSE

Currently, many consumers in Texas have few choices if they have an immediate need to borrow small amounts of cash. Banks and traditional finance companies will either not loan small amounts or will turn away many borrowers due to poor credit histories. Pawnbrokers make small loans, but pawnbrokers require that the borrower be without the use of the pledged personal property during the term of the transaction. National payday loan chains operate in Texas, but they are not regulated by the State. Further, many borrowers are “unbanked” and therefore do not have a checking account available to take out a payday loan. Payday loans also tend to cost the borrower upwards of \$20 per \$100 borrowed for two weeks.

The purpose of this bill is to create a new type of credit transaction, a Limited Recourse Secured Loan. It is a loan for a short period of time where the borrower pledges personal property to secure the loan, but is allowed continued possession and use of such property during the loan term. Like a pawn loan, the borrower is not personally obligated to repay any amount. Upon default, the lender’s only recourse is to seek possession and sale of the pledged personal property pursuant to the Uniform Commercial Code. Unlike a pawn loan, the borrower is entitled to any surplus received from such sale beyond the amount owed on the loan. The rate charged by this type of lender is significantly less than what is currently charged by unregulated payday lenders in the State.

C.S.S.B. 1143 allows for a loan to be secured by personal property with limited recourse against the borrower.

RULEMAKING AUTHORITY

It is the committee's opinion that rulemaking authority is expressly granted to the Finance Commission in SECTION 1 (Section 344.301, Finance Code) of this bill.

ANALYSIS

C.S.S.B. 1143 amends Subtitle B, Title 4, Finance Code, as follows:

The substitute creates a new section entitled "Limited Recourse Secured Loans" with definitions of "borrower", "Lender", "Limited recourse secured loan", and "Pledged property."

The substitute provides regulations for the licensing and application requirements for potential lenders. The lender must also apply for a bond. The license must be displayed in each lending office and is subject to suspension, revocation, or surrender by the Consumer Credit Commissioner.

The substitute provides the maximum amount of the loan (\$2000 or fair market value) and loan term (not less than 7 days or more than 30 days) including renewals (not more than five additional periods.) The personal property pledged must be owned by the borrower without being encumbered.

The substitute provides for a maximum interest (3% per month) and fees (1/10th of principal amount of loan.)

The substitute provides for the ability of the lender to contract for a security interest subject to Chapter 9, Business and Commerce Code. The substitute also requires a notice and waiting period for the repossession of property subject to the security interest.

The substitute provides for limited recourse against the borrower unless borrower engages in fraud or has encumbered property in violation of the agreement. The substitute also requires disclosures to be made on the loan agreement pursuant to the federal Truth In Lending Act as well as short-term loan disclosures.

The substitute provides prohibited acts by lenders including a private remedy for undisclosed, improperly disclosed, or excessive charges.

The substitute authorizes the Consumer Credit Commissioner to examine and investigate lenders including procedural guidelines. Lenders must also file an annual report with the commissioner.

EFFECTIVE DATE

September 1, 2005

COMPARISON OF ORIGINAL TO SUBSTITUTE

C.S.S.B 1143 modifies the original by adding language that redefines the term "pledged property."

The substitute modifies the original by adding language that prohibits motor vehicle dealer in any state from obtaining a license. It does not prohibit licenses for persons who use the services of an unaffiliated public or private auction to sell recovered pledged personal property, if the sale complies with the provisions of the chapter.

The substitute modifies the original by adding the term "third party" to encumbrances of pledged personal property.

The substitute modifies the original by increasing the number of additional loan periods from 4 to 5.

The substitute modifies the original by changing the maximum rate of fees from nine percent a month to 1/10 of the principal amount of the loan on the first \$1000 (or 10 percent), plus a fee that does not exceed seven percent of any portion of the principal in excess of \$1000. The substitute removes language that provides the administrative fee is to be considered earned at the time a loan is made and is not subject to refund. The substitute adds language that provides the lender is entitled to earn interest and fees on prepayment in full of a loan.

The substitute modifies the original by adding language that provides that a contract for a limited recourse secured loan must be written in plain language designed to be easily understood by the average consumer.