Department of Legislative Services

Maryland General Assembly
2024 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 254 (Chair, Economic Matters Committee)(By Request - Departmental - Labor)

Economic Matters

Commercial Law - Credit Regulation - Predatory Loan Prevention (True Lender Act)

This departmental bill prohibits a person from engaging in certain activities to evade requirements relating to lending (or the extension of credit) under Maryland law. Further, the bill establishes that a person is a lender (subject to Maryland law) under specified conditions or if the totality of circumstances otherwise indicates that the person is the lender and the transaction is structured to evade the requirements of the applicable Maryland law, as specified.

Fiscal Summary

State Effect: The bill's changes, including any additional enforcement activities by the Office of Financial Regulation (OFR) within the Maryland Department of Labor (MDL) can be handled with existing budgeted resources. No material impact on revenues.

Local Effect: None.

Small Business Effect: MDL has determined that this bill has minimal or no impact on small business (attached). The Department of Legislative Services concurs with this assessment.

Analysis

Bill Summary:

General Prohibitions

The bill prohibits a person from engaging in any device, subterfuge, or pretense to evade the requirements of Title 12 of the Commercial Law Article (which governs credit regulation in the State), including by:

- making a loan or an extension of credit that is purported to be (1) a personal property sale and leaseback transaction or (2) a cash rebate for a pretextual installment sale of goods or services; or
- making or offering (or assisting or arranging for a debtor to obtain) a loan or an extension of credit with a greater rate of interest, consideration, or charge than is authorized by Title 12 of the Commercial Law Article through any method.

A loan or an extension of credit made in violation of the above requirements is void and unenforceable as to any principal, fee, interest, or charge.

Applicability

A person is a lender subject to the requirements of Title 12 of the Commercial Law Article (regardless of any claim by the person to be acting as an agent, as a service provider, or in another capacity for a covered lender) if:

- the person holds, acquires, or maintains (directly or indirectly) the predominant economic interest in the loan or extension of credit;
- the person markets, brokers, arranges, or facilitates the loan or extension of credit and holds the right, requirement, or first right of refusal to purchase the loan or extension of credit or a receivable or interest in the loan or extension of credit; or
- the totality of the circumstances indicates that the person is the lender and the transaction is structured to evade Title 12 of the Commercial Law Article.

Circumstances that weigh in favor of a determination that a person is a lender include those in which the person:

- indemnifies, insures, or protects a covered lender for any costs or risks related to the loan or extension of credit;
- predominantly designs, controls, or operates the loan or credit program;
- holds the trademark or intellectual property rights in the brand, underwriting system, or other core aspect of the loan or credit program; or
- purports to act in the State as an agent or service provider or in another capacity for a covered lender while acting directly as a lender in other states.

Current Law/Background: Title 12 of the Commercial Law Article encompasses a range of financial regulation requirements and activities (including the specification of maximum permissible interest rates that may be charged to Maryland consumers under the State's consumer lending laws).

OFR states the intent of the bill is to delineate factors for determining which party is the "true lender" to the consumer in a "rent-a-charter" arrangement, therefore allowing the relevant parties to more easily determine whether they must be licensed in Maryland and adhere to the State's interest rate limitations. The bill generally considers the totality of the circumstances to determine who is the lender in a transaction.

Recent History of "Interest Rate Exportation"

OFR advises that, under long-standing federal law, Maryland's laws limiting interest rates do not apply to national banks or banks chartered by other states. Consequently, these banks may extend loans to Maryland consumers at interest rates permissible under the laws of their "home" (*i.e.*, non-Maryland) states that can significantly exceed Maryland interest rate caps. Thirty-five states have higher interest rate caps (or no cap) than Maryland permits on small dollar loans.

Because of the supremacy of federal law, Maryland cannot enact legislation preventing these banks from charging Maryland borrowers interest rates otherwise allowed by their home states. (The practice of charging the highest interest rate available in a state where a lender is located on credit it extends to borrowers residing in other states is often referred to as "interest rate exportation.")

Historically, national and out-of-state banks started interest rate exportation in volume through credit card lending, and over time, as technology has improved and consumer lending expanded nationally, those financial institutions expanded exportation of interest rates to all types of lending products. However, while national and out-of-state banks have long exported their higher interest rate products into Maryland, they have typically not been the entities that are engaging in predatory lending practices.

Impact of Fintech Companies

OFR advises that high-interest products started becoming a problem (both locally and nationally) between 10 and 15 years ago when payday and other nonbank lenders such as financial technology companies (Fintechs) started partnering with banks located in states authorizing high interest rates (*i.e.*, to effectively use the bank's interest rate exportation right to offer high-cost loans in other states). This arrangement is commonly known as "rent-a-charter." OFR states that the combination of the interest rate exportation laws and willingness of certain banks in states with high interest rate caps to partner with Fintechs and other lenders (*e.g.*, payday lenders) has led to predatory and abusive practices that have harmed Maryland consumers.

So-called “true lender laws” are named for the analysis used by courts to determine the party that is (as the name implies) the “true lender” to the consumer in a rent-a-charter arrangement. If the bank is determined to be the true lender, then the interest rate exportation is deemed legal and the high interest not violative of the consumer’s home usury limits. However, if the Fintech or other partner is deemed to be the true lender, then the exportation of the interest rate is not permitted under federal law and the high-interest rate lender’s loan is deemed to violate the usury laws of the consumer’s state of residence. True lender laws are therefore designed to prevent Fintechs and other potential bank partners from avoiding state interest rate caps by partnering with a bank located in a state allowing high consumer interest rates.

The rent-a-charter arrangement has been controversial and both state and federal financial regulators have made various attempts to address the situation in the context of payday lending. OFR has also taken action and is currently pursuing an enforcement action against an out-of-state bank and its Fintech partner for high-cost lending activities in Maryland. However, litigation is historically a slow process. (OFR notes that a similar case in Colorado took over three years to resolve.)

According to OFR, the bill models a Maine law by creating a statutory regime to provide rules for determining when a Fintech is the true lender (and hence must adhere to Maryland’s interest rate caps and other consumer protections). OFR further states that a statutory solution will align Maryland with the increasing number of states that are addressing the problem of high interest rate exportation and reduce the number of predatory lenders marketing their products to Marylanders.

Additional Information

Recent Prior Introductions: Similar legislation has not been introduced within the last three years.

Designated Cross File: None.

Information Source(s): Office of the Attorney General (Consumer Protection Division); Maryland Department of Labor; U.S. Department of the Treasury (Office of the Comptroller of the Currency); Department of Legislative Services

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ANALYSIS OF ECONOMIC IMPACT ON SMALL BUSINESSES

TITLE OF BILL: **Commercial Law - Credit Regulation - Predatory Loan Prevention (True Lender Act)**

BILL NUMBER: HB0254

PREPARED BY: Amy Hennen

PART A. ECONOMIC IMPACT RATING

This agency estimates that the proposed bill:

__X__ WILL HAVE MINIMAL OR NO ECONOMIC IMPACT ON MARYLAND SMALL BUSINESSES

OR

___ WILL HAVE A MEANINGFUL ECONOMIC IMPACT ON MARYLAND SMALL BUSINESSES