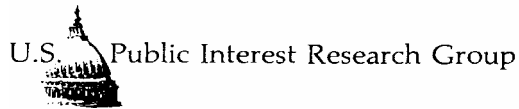




Publisher of Consumer Reports



Consumer Federation of America



Consumer @ction



March 7, 2005

The Honorable Daniel K. Akaka
United States Senate
Washington, DC 20510

***RE: SUPPORT FOR AKAKA CREDIT COUNSELING AND PAYDAY LOAN
AMENDMENTS TO BANKRUPTCY BILL***

Dear Senator Akaka:

The undersigned national consumer organizations strongly support your amendments to the bankruptcy bill (S. 256) that would encourage more responsible lending by payday loan companies and keep more consumers in credit counseling and out of bankruptcy.

Making Credit Counseling a More Successful Alternative to Bankruptcy

S. 256 requires consumers to seek credit counseling within six months of filing for bankruptcy. However, the credit card companies that created credit counseling have taken steps in recent years that undermine it as a viable alternative to bankruptcy for some consumers. By slashing funding for legitimate credit counseling agencies and charging consumers in credit counseling higher interest rates than in the past, credit card companies are leaving debt chocked Americans with few options other than bankruptcy.

If Congress is going to require that consumers enter credit counseling before filing for bankruptcy, it must ensure that credit counseling is truly an effective and viable alternative to bankruptcy. This amendment would stop a credit card company from attempting to collect on debts in

bankruptcy unless the creditor has a policy of waiving interest rates for consumers who enter credit counseling.

Consumers who enter a credit counseling “debt management plan” agree to discontinue credit card use and to make one consolidated payment to the credit counseling agency, which then forwards the funds to the appropriate credit card company. In exchange, creditors agree to offer two key “concessions” to help consumers pay off as much of their debts as possible: a reduced interest rate on the amount they owe and the elimination of fees that have accrued.

Unfortunately, credit card companies in recent years have become increasingly unwilling to reduce interest rates for consumers in credit counseling, which has led to more bankruptcy filings. According to a study by the National Consumer Law Center and Consumer Federation of America, five of 13 major credit card issuers increased the interest rates they offered to consumers in credit counseling between 1999 and 2003. Currently, only two major credit card issuers (Wells Fargo and American Express) completely waive all interest for consumers in credit counseling. The majority of other major credit card companies charge interest rates in credit counseling above 9 percent, with issuers like Capital One, General Electric and Discover charging rates of 15 percent or more.

The increasing refusal of creditors to offer low interest rates causes more consumers to drop out of credit counseling and to declare bankruptcy. According to a survey by VISA USA, one-third of consumers who failed to complete a debt management plan in credit counseling said they would have stayed on the plan if creditors had further lowered interest rates or waived fees. Moreover, almost half of those who dropped of the plan had or were going to declare bankruptcy.

It is ironic that the same creditors whose aggressive and reckless lending practices have contributed to the increase in bankruptcies in this country have weakened credit counseling in recent years. It is hypocritical for the credit card industry to demand that Congress give them bankruptcy relief while closing off credit counseling as an effective alternative for many consumers.

Prohibiting the Recovery of Predatory Payday Loans

This amendment would prohibit payday lenders from having a claim on these loans in bankruptcy. Lenders who entice cash-strapped consumers to write checks without money in the bank to cover them as the basis for making “payday loans” should not be allowed to use the bankruptcy courts to collect. Payday loans trap borrowers in a cycle of debt when consumers flip loans to keep their checks from bouncing.

Last year, consumers paid \$6 billion to borrow \$40 billion in small cash advances from over 22,000 payday loan outlets. These loans of \$100 up to \$1,000 are secured by personal checks or electronic access to bank accounts and must be repaid in full on the borrower’s next payday. Lenders charge annual interest rates on these loans that begin at 390 percent, with finance charges of \$15 to \$30 per \$100 borrowed.

Payday lending condones check-kiting as a financial management tool and encourages the unsafe use of bank accounts. Loans based on check/debit-holding get paid before other obligations, due to the severe adverse consequences of failing to make good on a check. Some lenders threaten

criminal prosecution or court martial of military consumers for failure to make good on the check used to get a payday loan. If the consumer files bankruptcy to stop the cycle of debt, some lenders then try to convince the bankruptcy court that the payday loans should not be discharged.

Consumers need comprehensive small loan protections, reasonably-priced alternatives to payday loans, and sound financial education. **In the meantime, Congress should prevent any lender that entices consumers to write checks without funds on deposit or to sign away electronic access to their bank accounts from also using the bankruptcy courts to collect on their usurious loans.**

If this nation is truly going to reduce bankruptcies, lenders must first exercise more responsible lending decisions and be more responsive to consumers who show a genuine interest in resolving their debt problems. We applaud you for moving to make payday and credit card lenders more accountable in their treatment of consumers.

Sincerely,

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