Members Brief

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Payday Lending in Ohio

Many low-income Ohioans utilize payday loans to help meet their financial obligations. Because the cost of a payday loan can be quite high compared to a borrower's income, some borrowers repeatedly renew their loans to pay off previous ones. This fact has generated a great deal of controversy and resulted in several revisions to Ohio's lending laws over the years. This Members Brief discusses the history of payday loan legislation in Ohio and describes the current Short-Term Loan Law.

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Everyone gets hit with the occasional unexpected expense. For some people with little income or savings, this can be a big problem. Other people may encounter trouble paying regular, recurring expenses even without an unexpected expense. They need money, but their options are limited:

- They can cut their budget only so much;
- Putting off paying bills causes other problems;
- They may not be able to get a traditional loan from a bank or a loan from family or friends;
- Their available credit card line may be inadequate;

- They may not have anything worth pawning.[1]

This is where payday lenders come in.

While there is no universal definition of a "payday loan," the term typically describes an unsecured, small dollar, short-term loan, the repayment of which is to occur on the borrower's next payday.[2] The borrower typically will provide a post-dated check to the lender for the amount borrowed plus the finance charge and fees, or authorize electronic payment from the borrower's bank account. On the maturity date, if the borrower does not repay the loan, the lender cashes the check or electronically withdraws the amount owed from the borrower's bank account.

Payday lending has generated a great deal of controversy over the years, the core issues being the high cost of these loans in terms of interest rates and fees and the tendency of borrowers to repeatedly renew the loans. But the payday lending industry has countered that making these loans available provides a valuable service for a number of consumers. Consequently, payday lending poses a difficult policy issue – how to keep credit available to people with little income while curbing predatory practices. Further complicating the issue is that payday lenders have operated under a variety of business models, making regulation of the industry difficult.

Payday lending expanded in Ohio following 1996 legislation authorizing check-cashing businesses to make small loans. In 2008, the General Assembly repealed this authority and established the Short-Term Loan Law. But no lenders obtained a license under this law for almost ten years. Lenders instead opted to make payday-type loans under other lending laws in Ohio that were more favorable to the lender. However, in October 2018, the 132nd General Assembly enacted H.B. 123, which made reforms with the goal to find a balance between business interests and consumer protections, and also to require lenders who wished to offer payday-type loans to obtain licensure under the Short-Term Loan Law exclusively.[3]

A brief history of payday lending, 1996 to 2018

In Ohio, the expansion of payday lending began in 1996 with the enactment of H.B. 313. It authorized licensed check-cashing businesses to make certain small loans if they obtained a separate "check-cashing loan" license from the Division of Financial Institutions of the Department of Commerce.[4] These loans could not exceed $800 and could not have a duration of more than six months. Licensees could charge loan origination fees ($5 per $50 up to $500 of the loan amount, and $3.75 per $50 of the loan amount between $501 and $800) and interest at a rate of 5% per month or fraction of a month on the unpaid principal. Due to the short-term nature

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[1] The PEW Charitable Trusts, Safe Small-Dollar Loans Research Project, Payday Lending in America: Who Borrows, Where They Borrow, and Why (July 2012) (PDF), which may be accessed by conducting a keyword "payday lending" search at pewtrusts.org.

[2] Although some depository institutions, such as banks, offer payday-type loans, this brief discusses the law as it pertains to nondepository lenders.

[3] The PEW Charitable Trusts, Ohio Law Offers Balanced Model for Payday Loan Reform (November 12, 2018), which may be accessed by conducting a keyword "Ohio balanced model payday loan reform" search at pewtrusts.org.

[4] Former R.C. 1315.39 to 1315.44.

of the loan, the annual percentage rate (APR), when calculated to represent the total cost of the loan, could be 390% or higher, depending on how many times the loan was renewed.[5] By 2008, the Division of Financial Institutions had issued over 1,500 check-cashing loan licenses.[6]

Proponents of payday lending argue that these loans are the only way many low-income or fixed-income individuals can obtain financing to cover unexpected expenses, and that alternatives are more costly, as in bank overdraft fees or bad check fees. Those opposed to payday lending claim, however, that most payday loans are used to cover ordinary living expenses – not emergencies. As a consequence, the high interest rates and fees, combined with the short-term nature of the loans, lead many consumers into a cycle of debt, often taking out additional payday loans to pay off previous ones.[7]

The often-contentious debate culminated in the passage of H.B. 545 in 2008. The act repealed the Check-Cashing Loan Law and established the Short-Term Loan Law. It provided some consumer protections for borrowers by restricting the loan amount to $500 for a duration of not less than 31 days. Also, the maximum APR a lender could charge was 28%. H.B. 545 was challenged by a referendum petition, but the voters approved the act, and H.B. 545 took effect.[8]

But, from 2008 to 2018, no lenders obtained licensure under the Short-Term Loan Law. Instead, payday loans were made by businesses under the General Loan Law or the Small Loan Law or through third-party loan brokers under the Credit Services Organization (CSO) Law.[9] The lending authority granted by each body of law differed with respect to loan amount and duration, maximum interest rates, permissible fees and charges, frequency of obtaining loans, as well as other loan conditions. The fees assessed by loan brokers licensed as CSOs that facilitated payday loans were unregulated. As a result of these differences, payday loans made under these laws were more costly for borrowers and, therefore, more financially advantageous for lenders than those that could be made under the Short-Term Loan Law.[10]

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[5] See LSC's Final Analysis of H.B. 545 of the 127th General Assembly (PDF), which is available on the General Assembly's archives website at archives.legislature.state.oh.us.

[6] "The History of Payday Lending in Ohio," from a continuing legal education seminar on Regulating Investment and Financial Services, presented by Jacqueline Mallett, Consumer Finance Chief Counsel, Division of Financial Institutions on July 27, 2012.

[7] The PEW Charitable Trusts, Safe Small-Dollar Loans Research Project, Payday Lending in America: Who Borrows, Where They Borrow, and Why (July 2012) (PDF), pg. 13.

[8] R.C. 1321.35 to 1321.48; November 2008 State Issue 5, see Ohio Secretary of State, 2008 Election Results, which is available on the Secretary of State's website, ohiosos.gov, under "Elections & Voting," then "Election Results and Data."

[9] R.C. 1321.51 to 1321.60, 1321.01 to 1321.19, and Chapter 4712; see LSC's Fiscal Note & Local Impact Statement for H.B. 123 of the 132nd General Assembly (PDF), pg. 2, which is available on the General Assembly's website; legislature.ohio.gov.

[10] R.C. Chapter 4712; Center for Responsible Lending, Issue Brief (July 2010) (PDF), which may be accessed by conducting a keyword "crl payday lenders brokers brief" search on google.com; Housing Research & Advocacy Center, The New Face of Payday Lending in Ohio (March 2009) (PDF), which may be accessed by conducting a keyword "new face of payday lending in Ohio" search on google.com.

Current Short-Term Loan Law – Ohio Fairness in Lending Act

In July 2018, the 132nd General Assembly passed H.B. 123, commonly known as the Ohio Fairness in Lending Act. The intent, as explained by the act's proponents, was to find a balance between both lender and borrower interests and to steer lenders who were offering payday-type loans and wished to continue to do so from licensure under the Small Loan, the General Loan, or CSO laws instead to licensure under the Short-Term Loan Law.[11]

In other words, payday lenders operating in Ohio, offering loans that are $1,000 or less or for a duration of one year or less, could no longer operate under any law other than the Short-Term Loan Law.[12] Based on a 2016 count by the Pew Charitable Trusts, the number of storefront locations offering payday loans, and thus potentially subject to licensure under the Short-Term Loan Law, was approximately 650. Based on the Division of Financial Institutions' eLicense Center, as of August 29, 2022, there were 118 active Short-Term Loan Law licensees in Ohio.[13]

Another variation on the payday loan is the auto title loan, under which the borrower pledges the borrower's motor vehicle as collateral. These types of loans are prohibited under the Short-Term Loan Law, but may be available under different licensing laws.[14]

The following table shows some of the loan terms under the Short-Term Loan Law.

Loan Terms	Short-Term Loan Law (R.C. 1321.35 to 1321.48)
Maximum loan amount *(R.C. 1321.39(A))*	$1,000
Duration of loan *(R.C. 1321.39(B))*	Up to one year
Maximum interest charges *(R.C. 1321.40(A))*	28% per year
Other permissible fees or charges not included as interest *(R.C. 1321.40(B) to (E))*	Monthly maintenance fee of not more than 10% of loan or $30, whichever is less (fee cannot be added to loan balance to which interest is charged);

[11] The PEW Charitable Trusts, Ohio Law Offers Balanced Model for Payday Loan Reform (November 12, 2018).

[12] R.C. 1321.141, 1321.39, and 1321.592. Loans under the Consumer Installment Loan Act (CILA) (R.C. 1321.62 to 1321.702) do not generally fit the description of a payday loan. Loans under CILA are for a minimum of six months and generally must be paid back in equal installments.

[13] The PEW Charitable Trusts, Ohio Has the Highest Payday Loan Prices in the Nation (December 2016) (PDF), which may be accessed by conducting a keyword "Ohio payday loan prices" search at pewtrusts.org; Ohio Department of Commerce Division of Financial Institutions eLicense Lookup.

[14] R.C. 1321.41(H).

Loan Terms	Short-Term Loan Law (R.C. 1321.35 to 1321.48)
	Loan origination charge of 2% of loan (only for loans of $500 or more, and fee cannot be added to loan balance to which interest is charged); Check collection fee of $20 plus any amount passed on from the financial institution; Check cashing fee of $10.
Collateral (*R.C. 1321.41(H)*)	Lender may not accept the title or registration of a vehicle, real property, physical assets, or other collateral as security

Interest and fees

The Short-Term Loan Law permits lenders to charge interest at an APR of up to 28%. In this context, "interest" means all charges payable directly or indirectly by a borrower to a lender as a condition of a loan, including fees, service charges, renewal charges, and any ancillary product sold in connection with a short-term loan. "Interest" does not include the monthly maintenance fees, the loan origination charge, the check collection charge, or the check-cashing fee. The law prohibits a lender from charging, in connection with a loan, credit insurance premiums and charges for any ancillary product sold. And the law caps all fees and charges at 60% of the originally contracted loan amount.[15]

Among other things, the loan contract has to include the following statement:

> **WARNING: The cost of this loan is higher than the average cost charged by financial institutions, such as banks or credit unions, on substantially similar loans. A financial institution may be able to offer you a similar loan at a lower cost.**[16]

Terms based on borrower's income

Unless extra steps are taken by the lender, the borrower must have at least 91 days to repay the loan. The loan can be for a duration of 90 days or less if the borrower's total monthly payment to the lender is not more than 6% of the borrower's verified gross monthly income or 7% of the borrower's verified net monthly income, whichever is greater. The lender must make a reasonable attempt to verify the borrower's income prior to initiating the loan, and at a minimum must obtain from the borrower a recent pay stub or other written evidence of recurring

[15] R.C. 1321.35(D), 1321.403, and 1321.41(C).

[16] R.C. 1321.39(C)(3).

income, such as a bank statement. If the loan duration is 91 days or longer, the lender must determine the recommended length of a loan based on the borrower's verified monthly income and provide this recommendation to the borrower. But, there is no obligation for the parties to follow this recommendation.[17]

Restrictions on the frequency of obtaining loans

To address the concern of some borrowers' tendency to remain in a cycle of debt, the law prohibits a lender from making a short-term loan to a borrower if an outstanding loan exists between that borrower and the lender, a person related to the lender by common ownership or control, or an employee or agent of the lender. This prohibition does not apply when a loan is simply being refinanced.

Also, if refinancing, the lender cannot charge another maintenance fee. Further, if the loan is refinanced prior to its maturity date, or if the loan is prepaid in full prior to that date, the lender must refund to the borrower a prorated portion of the interest, monthly maintenance fees, and all other charges. The lender cannot charge the borrower a fee for prepaying the loan in full prior to the maturity date.

The law also caps the principal that may be outstanding for a particular borrower. Specifically, it prohibits making a short-term loan to a borrower if the loan will result in a total outstanding principal of more than $2,500 in short-term loans made by all lenders to that borrower at any one time. Prior to making a loan, the lender must require each borrower to sign a written declaration that the borrower is eligible to receive a loan, and must make a concerted effort to verify the borrower's eligibility.[18]

Cancellation policy

The law gives the borrower the right to rescind or cancel the loan by returning the originally contracted loan amount by 5:00 p.m. of the third business day following the day the borrower enters into the loan contract.[19]

Repeated electronic withdraws

To protect borrowers from possible overdraft fees if they do not have sufficient funds in their bank account, the law requires the lender to notify the borrower that electronic payment is optional and to inform the borrower that the borrower has the right to revoke or remove authorization for electronic payment at any time. The law prohibits a lender from drafting funds electronically from an institution without the borrower's written approval. In addition, the lender cannot attempt to collect from a borrower's account after two consecutive attempts have failed, unless the lender obtains new written authorization.[20]

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[17] R.C. 1321.39(B), 1321.391, and 1321.46.

[18] R.C. 1321.401, 1321.402, and 1321.41(E), (J), and (R).

[19] R.C. 1321.39(C)(7) and (E).

[20] R.C. 1321.39(C)(8), 1321.41(M), and 1321.411.

Demand feature limitations

The Short-Term Loan Law also limits a lender's use of a "demand feature" in a short-term loan. Under a demand feature, if the borrower fails to meet the repayment terms for any outstanding balance, the lender terminates the loan before the maturity date and demands repayment of the entire outstanding balance. A demand feature is permitted only if:

- At least ten days after the payment was due, the lender gives the borrower written notice of the loan's termination; and
- The lender collects only the outstanding balance, prorated interest, and the fees earned up to the point of termination.[21]

Contacting the borrower

Once the loan is made, the lender can contact the borrower regarding certain topics only when the contact is for the borrower's benefit. Generally, these topics include upcoming payments, payment options, payment due dates, and the effect of default. After default, the affected topics are expanded to include receiving payments or other actions permitted by the lender, advising the borrower of missed payments or dishonored checks, and assisting the transmittal of payments via a third-party mechanism.[22]

[21] R.C. 1321.41(V).

[22] R.C. 1321.41(T).