NEIGHBORHOOD TRUST FINANCIAL PARTNERS

Neighborhood Trust Financial Partners' Comment in Response to CFPB's Proposed Interpretive Rule on 'Earned Wage' Products

Docket No. CFPB-2024-0032

Key Headlines

- We support the proposed interpretive rule and applaud the CFPB for its efforts to address regulatory confusion and increase scrutiny over earned wage access products. However, we want to highlight that the proposed interpretive rule is insufficient for addressing the full scope of negative impacts of these products. While cost is a concern, the most significant problem with earned wage access products is that they're designed to trap users in borrowing cycles.
- Information, including APR disclosures, is generally insufficient to deter usage of predatory products, as demonstrated by the payday lending industry.
- For many consumers, earned wage access apps are not being used in lieu of subprime credit cards or other expensive products, but rather have created an entirely new form of borrowing and dependence that didn't previously exist. And this "earned wage" debt is piling on top of other forms of debt, exacerbating people's debt burdens.
- Earned wage access products are merely rearranging, masking and perpetuating the same challenges that low-income earners have been facing for decades. While there indeed is a slice of the market that just needs help bridging the gap between paydays but otherwise earns income that is greater than or equal to their expenses, this is not the reality for many (if not most) EWA users.
- While both employer-based and direct-to-consumer earned wage access products carry a risk of facilitating borrowing cycles, we believe that direct-to-consumer products are much more dangerous to consumers' financial security.

The Harmful Features of Earned Wage Access Products

While we support the goal of this interpretive rule to increase cost transparency, that alone is not sufficient for tackling the harm caused by these products. The biggest problem with earned wage access isn't the cost – it's the trapping mechanisms built into how these products function, which facilitate inescapable borrowing cycles and dependence on these apps. Examples of these trapping mechanisms include:

- A payback structure that relies on balloon payments on payday that can potentially siphon off 50% or more of a paycheck. This balloon payment often leads to a cash flow shortage and the need to borrow again, sparking a debt cycle.
- The ability for workers to secure multiple loans during the same pay period can lead to them being overextended on payday, resulting in added costs from overdraft fees.
- Seamless reborrowing processes provide access to new loans in a few clicks, again risking becoming overextended and dependent on continued borrowing.

One of our financial coaching team's first introductions to earned wage access apps was in 2019 when a client shared in a session that she was using Earnin' to "access her paycheck sooner," but was stuck using it every paycheck because of the lump sum repayment structure. Her coach remembers her saying "it's totally free, they just give you the option to tip to help support the company, so I usually tip a few dollars because I like to pay things forward when I can." It's worth noting that this coach's guidance was therefore not about telling the client to stop paying the tip each time, particularly given that her motivation for paying it was so kind-hearted, it was instead focused on breaking the borrowing habit that kicked off the moment she downloaded the app.

Lessons from Past Payday Loan Regulations

In addition to cost transparency not addressing the biggest problem with earned wage access products, we believe that mandating that these companies provide more transparent disclosures is unlikely to meaningfully change consumer behavior or better protect consumers against exploitation. As we know from previous research, information is generally insufficient to deter usage of predatory products. Below are findings from Pew Research Center's research on payday loans in 2013, which, despite being more than 10 years old, feel remarkably timely and applicable to earned wage access apps. They also suggest that the CFPB ought to take similar action for earned wage access products as they did for payday loans, given the similarities in how consumers perceive and interact with these products:

EXHIBIT 6:

SIX REASONS WHY PEOPLE USE PAYDAY LOANS THEY CANNOT AFFORD

1. **Desperation**
More than one-third of borrowers say they have been in such a difficult situation that they would take a payday loan on any terms offered.

2. **Perception**
Borrowers perceive that payday loans do not create ongoing debt, or are "not another bill," although the loans do in fact create high-cost, ongoing debt.

3. **Reliance**
Borrowers rely on lenders for accurate information. Lenders sell payday loans that are packaged as a two-week product, although the borrower ends up indebted for five months on average.

4. **Focus on fee**
Borrowers focus on being able to afford the finance fee, rather than on how the lump-sum repayment will affect their budget.

5. **Trust**
Some bank deposit advance borrowers believe that bank payday loans are safer or more regulated than other payday loans.

6. **Temptation**
Some borrowers consider the loans "too easy" to obtain, because they are readily available, and borrowers have a consistent cash shortfall.

What Is Really Happening with These Products

A recent NYTimes article described that "the advances — at an average annual percentage rate of about 110 percent for employer-based services, the bureau's analysis found — are cheaper than traditional payday loans, which can carry rates of almost 400 percent. But they are more expensive than double-digit rates on 'subprime' credit cards available to people with poor credit."

It's true that for some consumers, these earned wage products have in fact replaced payday loans (which is definitely a positive outcome). But for other consumers, they've created an entirely new form of borrowing and dependence that didn't previously exist, and this "earned wage" debt is piling on top of other forms of debt, including subprime credit cards.

The key puzzle piece missing from the Times' analysis is that people are already relying on credit cards, *in addition* to their earned wage apps. Consumers cannot suddenly begin replacing their earned wage apps with other products that have lower APRs just because they're now made more aware of the APRs. *They are already using those other products - and those credit cards are probably already maxed out.*

To paraphrase a quote in the same NYTimes article from Nadine Chabrier, a senior policy counsel with the Center for Responsible Lending: people are being coerced by these apps into "paying to get paid" – a problem that has been widespread for years. The movement to generate access to bank accounts and direct deposit was intended to address this very thing by equipping people to avoid check cashing fees. This movement has been largely successful, with unbanked and underbanked rates declining year over year. But this decline taken into context with the rapid growth of fee-driven earned wage apps, suggests that the root of the problem didn't go away, the fee collector just shifted. People are paying the same fees to get access to their own money as they always have, just to fintechs instead of check cashiers.

In addition to check cashing fees, we also hypothesize that these apps are absorbing dollars that would have previously been paid to banks, landlords, utility providers and creditors for missed payments, late payments and overdrafts. Again, consumers are still paying roughly the same amount out of pocket to access their paycheck and pay their bills, the costs associated with it have just changed hands.

Therefore, while regulation can mitigate some risks, these products inherently exploit underlying financial instability that requires deeper, systemic solutions to address. They are addressing a market need for higher wages amidst rising cost of living and increased individual financial responsibility, and exploiting behavioral economics principles to encourage people to borrow repeatedly. For many people, it is a real challenge when a bill is due between paychecks and they don't have the cash flow to pay it on time until payday. But even for these people - the best solution may not even be a wage advance, but flexibility from the bill collector to adjust the due date, which avoids the involvement and costs of a third-party company. And for most people, this flexibility isn't a sufficient solution anyway because they're existing in a budget deficit. When used by low-income workers to postpone a persistent budget shortfall, earned wage access apps by definition increase debt and financial fragility. Earned wage apps, the D2C ones in particular, are well aware of this reality but continue extending credit nonetheless.

Distinguishing between Employer-Based and Direct-to-Consumer Earned Wage Access

Lastly, while both employer-based and direct-to-consumer earned wage access products carry a risk of facilitating borrowing cycles, we believe that direct-to-consumer products are much more dangerous for a few main reasons:

- Employer-based products carry a lower risk of creating a disproportionate debt burden due to over-lending because they're tied to actual accrued wages.
- Employer-based products carry a lower risk of being stacked because a given employer is likely to only offer one payroll linked app.
- Employer-based products *potentially* carry a lower risk of being used for non-urgent expenses because workers may be more likely to feel a sense of oversight from their employer and therefore exercise greater restraint when using the product.
- Employer-based products offer the option for employers to cover any costs associated with borrowing against earned wages, *potentially* removing that burden from the borrower.

We believe that both employer-based and direct-to-consumer products are inserting third-party businesses with for-profit business models into the process of workers getting paid, which can create unnecessary costs and facilitate harmful borrowing cycles. But due to how differently they function and the fact that employer-based products have unique access to payroll data and seamless repayment, it's worth considering regulating them as distinct products under TILA. Therefore, this comment is intended to provide our perspective primarily on direct-to-consumer earned wage access products.

Conclusion

We hope that this new interpretive rule provides greater protection to consumers and fosters further discussion about the current credit landscape. From our perspective, the fundamental problems with the consumer credit industry have persisted for decades, despite surface-level changes. This rule will hopefully prompt not only stronger regulatory oversight of earned wage access products, but also encourage solutions that tackle the deeper problems driving the market demand for rapid access to credit and interrupt the current trend of profit-driven band-aid "fixes."

For any questions or follow-up discussion, please feel free to reach out to Rosie Silber-Marker at rsilbermarker@neighborhoodtrust.org.