Center for Economic Integrity

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September 11, 2019

Mr. Mark Brnovich
Office of Attorney General
2005 N. Central Avenue
Phoenix, Arizona 85004

Re: Align Income Share Funding in Arizona Regulatory Sandbox Program

Dear Attorney General Brnovich,

We urge you to reconsider your decision to admit Align Income Share Funding to participate in the Arizona Regulatory Sandbox Program without requiring the company to comply with Arizona's usury cap and the other consumer protections in the Consumer Lender law. We respectfully request that you re-examine this financial services firm and upon re-examination, revoke sandbox participation for their Income Sharing Agreement (ISA) product.

The Arizona Regulatory Sandbox

In 2018, HB 2434 created a "regulatory sandbox" that allows the Office of the Arizona Attorney General (OAG) to approve a temporary test of a new product or service regulated under Title 6 or Title 44, Chapter 2.1 or 13 of the Arizona Revised Statutes, including money transmitters and consumer lenders, without the license or authorization otherwise required by those laws. The "sandbox" law does require lenders to comply with consumer protections in the Consumer Lender law, including the usury cap and fee limits, and expands that protection for loans up to $15,000.[1] This provision was added by the legislature specifically to protect Arizona consumers from usurious lending products in the sandbox and was essential to approval of the sandbox bill. The sandbox law also requires lenders to comply with other consumer protections in the Consumer Lender law.

Align's Income Share Agreements

Align Income Fund Sharing purports to "invest" in consumers by loaning them money up to $12,500 to be repaid in two to five years at a payment rate of up to 10 percent of the borrower's income. The company is quoted as saying that the average contract is around $5,500. Unlike income share agreements (ISAs) used as an alternative to student loans, the

[1]https://apps.azleg.gov/BillStatus/GetDocumentPdf/460996 HB 2434 as enacted 2018.

Align product is a cash loan made to consumers to make purchases. If a consumer has no income during the repayment term, Align is not paid for that period of time. If the consumer's income rises, the amount owed to Align increases. The company claims that its income share agreement is not a loan subject to Arizona's credit laws.

The description of the Align ISA on the OAG's website is "A business model for income-sharing agreements that provide qualified consumers with a fixed amount of money in exchange for a percentage of the consumer's future income over a scheduled period of time, subject to contingencies involving periods of unemployment or lowered income."[2]

In your May press release announcing the latest participants in the sandbox, it states: "Participating in the Arizona sandbox will provide regulatory certainty to Align as it seeks to demonstrate that it is a different service than consumer lending and should not be regulated as such. Ultimately, the Department of Financial Institutions will determine whether a consumer lending license is required at the end of the two-year testing period."

While we can understand that a company would want the "regulatory certainty" to operate without complying with Arizona's consumer protection laws, we do not understand why the Arizona Office of Attorney General would accept the company's statement that it is offering something other than a loan product without taking into consideration the interests of consumers by allowing an unregulated lender into Arizona. The Income Share Agreement product offered by Align is a consumer loan product.

<u>Align's ISA Does Not Comply with the Consumer Protections of the Consumer Lender law</u>

By permitting Align to operate outside of Arizona's Consumer Lender law, the usury cap and none of the consumer protections of the Consumer Lender law apply to this product. It is highly likely that the cost of Align's loans will exceed the usury cap of 36 percent for loans up to $3,000 and 24 percent for the amount of loans over $3,000 up to $15,000 plus the five percent administrative fee (max $150) permitted by law.

Under Arizona's Consumer Lender law, the maximum APR for a $2,000 consumer loan repaid in two years is 41 percent APR, including interest and the 5% administrative fee permitted by law. A $10,000 five-year loan under the maximum rate and fee permitted is 30 percent APR. Arizona voters voiced their strong support for the state usury law in 2008; 60 percent of voters rejected the payday loan industry's Prop 200. In the decade since that vote, the Arizona legislature has refused to reauthorize payday loans or to enact legislation creating new high-cost loan products.

[2] https://www.azag.gov/fintech/participants

There is no rate information posted on the Align website or on the Fintech page at www.azag.gov to inform consumers of the comparable cost of cash from Align prior to applying for the product. The Align contract first page does not include the standard Truth in Lending Act disclosures of the finance charge, total of payments, and Annual Percentage Rate.

The sample contract Exhibit C on page 18 of 23 compares the cost of an ISA to three scenarios, but this cost comparison information is apparently not available when consumers are shopping. We appreciate that Align responded to our request for a copy of a contract being used in Arizona, but the cost disclosures example is blank.

It is likely that the Align ISA will come at high cost.[3] Align's contract Exhibit D lists only credit products as options to compare with the Align Income Share Agreement. It is worth noting the OAG approved an exhibit that compares the cost of the ISA with two *payday loan credit products that are illegal in Arizona*. Exhibit D lists online payday loans at 391% and online unsecured installment loans at 279% as cost comparisons to the effective cost of the Align ISA. Both of the comparison payday loan products are subject to the Arizona Consumer Lender law's usury cap, even when offered online by out-of-state companies.[4]

If an Arizona consumer earning $50,000 per year gets $4,000 from Align and agrees to repay 10% of income for two years, she will be required to pay $10,000 or $6,000 more than she received. If this were a Consumer Loan with Truth in Lending Act disclosures, this loan would cost 109.86 percent APR, *more than twice Arizona's usury cap*.

The Align ISA does not meet other consumer protections required of Consumer Lenders. For example, Align's fee schedule includes several charges that are not specified as permitted for Consumer Lender loans. Align's "true-up" annual payment to reflect changes in borrower income is not consistent with the Consumer Lender law's requirement that loans be repaid with "approximately equal periodic installments." Balloon payments are not permitted for Consumer Lender loans but could be the result of Align's true-up extra payment.

Align is not eligible to enter Arizona's Regulatory Sandbox Program

Align claims that the product is an investment, not a loan. Comments attributed to staff at the OAG point out that if Align is not offering a loan, the company would not be required to be

[3] "Could Income Share Agreements Displace Payday Loans?," PYMTS, May 29, 2019, https://www.pymnts.com/news/alternative-financial-services/2019/align-income-share-funding-agreement-payday-loans/

[4] AZDFI Alert CL/CO-16-01, "Unlicensed Consumer Lender Transactions," June 9, 2016 at https://dfi.az.gov/sites/default/files/FE-AD-PO-Regulatory_and_Consumer_Alert_CL_CO__06%2009-16-2016.pdf

licensed as a Consumer Lender to operate in Arizona.[5] For that reason Align should not be eligible to enter the Arizona sandbox, since eligibility applies only to companies that would be required to be licensed under Title 6, which includes the Consumer Lender law, or Title 44, Chapter 2.1 or 13.[6]

A.R.S. 41-5604 requires the OAG to consult with the applicable agency, in this case AZDFI, to ascertain if the applicant would need to be licensed as one of the financial services subject to Title 6 or Title 44, Chapter 2.1. It would appear that a closer examination in coordination with AZDFI may indeed nullify the basis for which Align was allowed to enter into the Arizona sandbox. If Align is not required to be a licensed Consumer Lender absent the Sandbox option, it is not eligible to be admitted to the sandbox under the law enacted in 2018 and in effect when Align was admitted to the sandbox.

<u>Conclusion</u>

Admission of Align Income Share Funding to the Arizona Regulatory Sandbox Program without applying the protections of the Consumer Lender law puts Arizona consumers at risk of paying usurious interest rates and being subject to unfair contract terms that should be subject to the required protections in Section 6-114, Section 6-632, Section 6-635, Subsections A, B and C and Section 6-637 as required by A.R.S. §41-5605.B (3). We urge you to withdraw authorization for Align Income Share Funding to participate in the Arizona Regulatory Sandbox Program. Failing that, we urge you to require Align to comply with the Consumer Lender law protections incorporated into the Sandbox law.

Sincerely,

Kelly S Griffith

Kelly Griffith, Executive Director,
Southwest Center for Economic Integrity

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[5] Howard Fischer, Capitol Media Services, "Consumer lending through 'income sharing' contracts now OK but unregulated in Arizona," May 24, 2019
https://tucson.com/news/local/consumer-lending-through-income-sharing-contracts-now-ok-but-unregulated/article_afc8cc8e-318b-5380-a0f3-94eb4f5f85e6.html

[6] A.R.S. § 41-5601.3 "Financial product or service" means a product or service that requires licensure under Title 6 or Title 44, Chapter 2.1 or 13 or a product or service that includes a business model, delivery mechanism or element that may otherwise require a license or other authorization to act as a financial institution or enterprise or other entity that is regulated by Title 6 or Title 44, Chapter 2.1 or 13." Subsection 6: "Regulatory sandbox" means the program established by this chapter that allows a person to temporarily test innovative financial products or services on a limited basis without otherwise being licensed or authorized to act under the laws of this state."