DFC
GLOBAL CORP

May 2, 2012

The Honorable Anna-Maja Henriksson
Minister of Justice
Eteläesplanadi 10
Helsinki
FINLAND

_Re:_ Micro Loans — Proposed Amendment to Consumer Protection Act

Dear Ms. Henriksson:

DFC Global Corp. respectfully submits this letter in opposition to the working group's April 11, 2012 proposal to amend the consumer-credit provisions of the Consumer Protection Act. DFC favors responsible lending practices in general and supports fair and reasonable regulatory controls to achieve such practices; however, the working group's proposals are confiscatory and unreasonable.

DFC is a diversified financial-services company primarily serving unbanked and underbanked consumers for over 30 years. Through retail storefront locations and the internet, DFC provides a range of consumer financial products and services in eight countries (Canada, the United Kingdom, the United States, the Republic of Ireland, Sweden, Finland, Poland and Spain) to consumers who, for reasons of convenience and accessibility, purchase financial services from non-banks. DFC's services — principally short-term, small consumer ("micro") loans and pawn loans — provide customers with immediate access to cash for living expenses or other episodic needs.

DFC operates 18 pawn-loan stores in Sweden and 13 such stores in Finland, operated under the names Sefina® and Helsingin Pantti℠.

Relevant to this matter, in July 2011, DFC acquired Risicum Oyj, the leading provider of internet loans in Finland. Risicum, which was established in 2005, provides micro loans through both internet and mobile phone technology, utilizing multiple brands to appeal to specific customer demographics. Risicum also provides internet and telephony-based loans in Sweden and Poland. Risicum employs 53 employees at its offices in Helsinki and Turku.

DFC opposes the working group's April 11 proposal. If the proposal were adopted, we will be forced to discontinue Risicum's lending activities in Finland and to terminate the employment of the majority of its employees. Accordingly, for the following reasons, DFC strongly urges that the working group's proposal be rejected. We respectfully offer our detailed comments regarding the proposal and, where appropriate, suggestions for modification of the proposal.

1. *De facto* prohibition of micro loans

The working group's proposal would fix the maximum permissible finance charge for micro loans below lenders' marginal costs of marketing, originating, servicing and collecting such loans, as well as credit losses associated with such loans. The practical effect of such an interest-rate ceiling would be to ban such loans altogether.

Under today's market-based pricing, the average finance charge to a consumer for a €100 loan repayable in 30 days is €25. As we note below, this rate is comparable to the rates charged in other countries. The working group's "option 2" recommendation would reduce the maximum permissible finance charge for such a loan by 89%, to €2.55, without any concomitant reduction in lenders' costs.

These costs can be roughly divided into four categories: fixed and variable operating costs (which consist primarily of personnel and occupancy costs), cost of loan capital, and cost for bad debts. Notably, the cost of verifying the borrower's identity *alone* can amount to €2 or more per approved loan, in the form of a one-time bank charge.

If these recommendations were to be implemented, lenders like DFC's Risicum subsidiary would become unprofitable and would be forced to discontinue lending operations in Finland. Such interest-rate limitations would deny Finnish consumers access to a popular form of credit available in other Nordic countries and place Finnish consumers at a disadvantage relative to consumers elsewhere. Not a single one of the Nordic nations has such a rate cap.

The economic effects of price controls of any kind are well-known to economists. While affordability and consumer protection are generally cited as the goals of interest-rate ceilings, interest-rate controls invariably evolve in a system of implicit subsidies, under which some rates are maintained at levels that are artificially high so that others can be restrained. Interest-rate ceilings erode service quality, as lenders reduce the expenses of their operations and weed out all but the most creditworthy borrowers; pricing to the most desirable borrowers is invariably increased so that the least desirable customers can be subsidized, if they are served at all. When maximum permissible interest rates are set below lenders' direct costs, lenders exit the market altogether. The distortion of market forces that occurs with rate caps would deprive the most desperate of borrowers of the opportunity to borrow from legitimate, regulated lenders and instead compel marginal borrowers to deal with lenders who are willing to lend illegally[1] and who, more likely than not, will pursue just as illegal collection practices when the loans come due.

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[1] Rationing and under-the-table payments are common results of legal price ceilings. "Loan sharking" is the most prevalent result of artificially low usury ceilings.

The working group proposal assumes, without any theoretical or practical evidentiary foundation, that: (a) micro loans will continue to be available in a legitimate market, even if maximum permissible rates are fixed below lenders' costs; or (b) if such loans become unavailable, borrowers will behave in a manner deemed more responsible financially. Yet history teaches that governments cannot suspend the laws of economics; needy borrowers will obtain the credit that they need, even if they can only do so illegally.

At current market pricing, there is no evidence of excess, or "economic," profits among lenders. Barriers to entry are low. The market is highly – nearly perfectly – competitive, with over 80 lenders engaged in such lending in Finland, all offering very similar and nearly commoditized loan services. Market pricing of micro loans in Finland is similar to the pricing of such loans in other countries. The evidentiary and conceptual basis for usury strictures is thus, at best, weak.

While well-intentioned, the working group's adherence to the concept of annualized interest costs is based on a misunderstanding of the nature and use of these micro loans. For Risicum's loans, fixed costs of personnel and occupancy figure disproportionately high, and the actual cost of money disproportionately low, relative to lending in long-term markets such as the residential mortgage loan business. Rather, the cost of the "service" aspect of the transaction is primarily being passed along to the borrower in pricing of Risicum's loan products. Nor is interest being compounded in this market. Standard notions of long-term measures of the cost of credit are simply inappropriate. Accordingly, because such loans are made for a short-term only, an annual percentage rate is not an appropriate method of cost comparison, and the fee expressed in euros is generally far more informative to the borrower.

2. The working group´s underlying assumptions are erroneous

a) Micro loans constitute a tiny component of the consumer credit market in Finland.

Micro loans are not a central or even a significant factor in household finance in Finland. Such loans constitute a mere 0.5% of all household indebtedness; of all credit extended to homeowners, micro loans account for less than 0.1%.[2]

While the potential for consumer detriment from the use of small loans is narrowly limited – necessarily so because of the small euro value of such loans and the non-compounding nature of interest charges – there are no comparable limits to the amount of mischief a consumer can commit, with a credit card, through behavior-related charges. The working group did not attempt to compare and apportion problems caused by micro loans against those caused by other

[2] Statistics Finland.

forms of consumer credit. If there is a problem, micro loans are an insignificant part of it.

b) Payment defaults

Of all legal payment defaults by Finnish consumers, only 1% are related to micro loans[3]. Approximately 72% of all micro loans are initially paid on time, and a significant portion of the remaining late payments are ultimately collected. Serious payment defaults are uncommon because the loan size is small and lateness is relatively easy to remedy.

Flaws with regard to other credit products are not discussed at all in the report. For example, credit cards result in tens of thousands of payment defaults per annum.[4] The underlying causes of increasing indebtedness in Finland are not addressed by the working group, and such causes are connected excessive spending, not terms of consumer credit.[5]

c) Alternative measures

Consumer credit experts recognize the bluntness of interest-rate ceilings as a weapon for regulating consumer credit policy.[6] Other tools, while less direct, may have more consumer-friendly effects while allowing the market itself to create the proper pricing and maximizing the supply of lawful credit to constrained borrowers. For example, liberalized bankruptcy exemptions and restrictions on creditor collection remedies force lenders to internalize the costs of poor credit decisions while not restraining prices artificially. Likewise, enhanced disclosures may be useful to promote informed shopping and to eliminate the effects of unintended transactions. Finally, there are a variety of approaches that are gaining popularity but have not been attempted in the Finnish small-loan market, such as requiring lenders to give advice regarding appropriate forms of credit and so-called "responsible lending" rules. In its haste to publish its recommendation, the working group does not appear to have considered any of these alternatives.

Some of the issues associated with micro loans in Finland could well be alleviated by other, less draconian, measures than interest ceilings, For example,

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[3]Suomen Asiakastieto Oy.

[4]*Id.*

[5]*Id.*

[6]See, Steven M. Crafton, *An Empirical Test of the Effect of Usury Laws*, 23 J. L. & Econ. 135, 145 (1980); James E. McNulty, *A Reexamination of the Problem of State Usury Ceilings: The Impact in the Mortgage Market*, 20 Q. Rev. Econ. & Bus. 16, 26-27 (1980); Loretta J. Mester, *Why Are Credit Card Rates Sticky?*, 4 Econ. Theory 505, 505, 521 (1994); *Usury Laws: The Bad Side of Town*, Economist, Nov. 28, 1998, at 30.

a positive credit data registry, higher supervision fees and direct debt recovery capacity for small receivables, among other measures, could be attempted.

A positive credit register has been adopted in many other countries, and the experiences have been universally positive. Such a registry enables creditors to assess the creditworthiness of credit applicants more accurately. With the adoption of such a registry in Finland, the number of payment defaults would be expected to decrease significantly. Also, such a register would increase competition among lenders for all categories of credit, which, consequently, would result in lower costs of credit for consumers.

In other countries, consumers are protected through substantive non-interest-rate regulation of consumer credit. For example, the leading trade association of micro lenders in the United States has adopted a code of "best practices" to protect consumers and assure fair treatment.[7] A similar code is being developed in the United Kingdom and will go into effect in the fourth quarter of this year. Various states in the United States and provinces in Canada regulate (at or near market rates) the interest rates on such credit, as well as the minimum and maximum terms of such loans, required disclosures, underwriting criteria, collection fees and methods, extended interest-free repayment plans for troubled borrowers, and other aspects of micro credit. Some jurisdictions even limit the total amount of such credit a borrower may undertake from all sources and require a borrower to undergo a debt moratorium after repaying the loan and before incurring additional credit.[8]

Interest-rate ceilings are often promoted as protecting consumers by ensuring lower credit prices. Exactly why consumers require price protection from the forces of supply and demand in loan markets, but not in other markets, has never been clear and is difficult for regulators to explain. Yet the evidence is overwhelming that such price controls are detrimental to consumers by eliminating the legitimate supply of credit and forcing consumers to deal with illegal or unregulated lenders.[9] Manifold other, better ways of regulating consumer credit exist. Some of the non-interest-rate restrictions suggested in the preceding paragraph may be appropriate in Finland and should be attempted prior to setting maximum permissible interest rates below lenders' costs.

d) Access to credit

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[7]Consumer Financial Services Association of America, Ltd. Member Best Practices, *available at* http://cfsaa.com/cfsa-member-best-practices.aspx (last visited May 2, 2012).

[8]See, *e.g.*, Florida Money Transmitters' Code, Fla. Stat. § 560.103 *et seq*.

[9]Duesenberry, James. S. *et al.*, 1969. Report of the commission on Mortgage Interest Rates to the President of the United States, (Washington, U.S. Government Printing Office).

There do not seem to be any market alternatives in Finland to micro loans. Banks do not currently extend any form of consumer credit equivalent to micro loans. Credit cards either are not available or financially viable or because of their terms are not attractive to the majority of users of micro loans. Social credit has no significance to the great majority of users of micro loans, since they do not qualify for such credit. In any event, social credit does not seem to have any meaning to anyone who needs a loan quickly.

By prohibiting micro loans, the proposal would force consumers to other forms of credit that would result in larger loan amounts, or, to illegal markets. In either case, consumer detriments related to payment defaults, collection and overindebtedness would increase.

Substantial evidence exists in other jurisdictions that borrowing shifts to the black market when interest-rate regulation is too restrictive. As only one minor example, in the United States, nearly all internet advertising for unregulated offshore or native American lending is targeted at consumers in states with highly restrictive interest-rate ceilings.

e) Investment environment and the Finnish Constitution

There is a complete absence of evidence that could lead to the conclusion that consumer indebtedness problems are caused primarily by micro loans. Since the few issues associated with micro loans could, as discussed above, be ameliorated through materially less onerous remedies, the outright prohibition of micro loans implicit in the working group's proposal offends basic rights, especially protection of property and freedom of trade. The working group's effort to address micro loans separately from other forms of consumer credit — forms that demonstrably cause much greater consumer detriment — is legally problematic.

The lack of a positive credit register will hinder foreign consumer lenders from entering the Finnish market. The absence of the positive credit register will create a competitive advantage to large Finnish banks based on their existing customer portfolios. As discussed above, the creation of a mandatory positive credit register would significantly enhance the competitive environment in Finland.

Also, financial markets in the Nordic countries have been largely integrated. Introducing a set of rules applicable to micro loans in Finland different from those of the other Nordic countries would be likely to have an adverse effect on the development of regional financial markets. Such a result would also be contrary to the long tradition of Nordic cooperation with regard to consumer protection laws.

Consequently, the competitive implications of the recommendations of the working group of the Ministry of Justice should also be assessed by the Finnish Competition Authority.

We request that the Ministry of Justice thoroughly consider the arguments set out in this letter. We will be pleased to submit international research materials on the subject matter upon your request and to discuss the matter further. Thank you for your consideration in this matter, Ms. Henriksson.

Yours sincerely,

DFC GLOBAL CORP.

By:
Kenneth W. Schwenke
President

BY HAND DELIVERY