

BANKING
DEPARTMENT OF BANKING AND INSURANCE
DIVISION OF BANKING

Check Cashing
Deposits

Adopted Amendments: N.J.A.C. 3:24-1.3 and 5.5

Proposed: August 15, 2005 at 37 N.J.R. 2917(a).

Adopted: August 15, 2006 by Steven M. Goldman, Commissioner, Department of Banking and Insurance.

Filed: August 15, 2006 as R. 2006 d.329, **with substantive changes** not requiring additional public notice and comments (see N.J.A.C. 1:30-6.3).

Authority: N.J.S.A. 17:1-8, 17:1-15 and 17:15A-30 et seq.

Effective Date: September 18, 2006

Expiration Date: May 25, 2010

Summary of Public Comments and Agency Responses:

The Department received comments from James Silkensen, Executive Vice President of the New Jersey League of Community Bankers, and Gerald Goldman, Esq., General Counsel, New Jersey Check Cashers Association.

COMMENT: One commenter stated their group raised no objection to the proposal to allow New Jersey licensed check cashers to make their deposits at an out-of-State financial institution approved by the Commissioner.

RESPONSE: The Department appreciates the expression of non-objection for the proposal.

COMMENT: One commenter supported the main thrust of the proposed amendments.

RESPONSE: The Department appreciates the expression of support for the proposal.

COMMENT: One commenter applauded the Department for responding to the current emergency facing check cashers resulting from termination of relationships by banks and the scarce number still willing to provide banking services to check cashers.

RESPONSE: The Department appreciates the expression of support for the proposal.

COMMENT: One commenter stated that the criteria specified in proposed N.J.A.C. 3:24-5.5(a)3 should be deleted in its entirety. The commenter stated that whether an out-of-State bank makes payday loans, refund anticipation loans or title loans is completely irrelevant to that bank's financial capacity to provide commercial banking facilities to New Jersey check cashers. The commenter stated that the social policy that the Department is surreptitiously attempting to further is entirely divorced from the goals and purposes of the statute from which the Department derives its authority to promulgate these rules, citing N.J.S.A. 17:15A-52(a) and 17:15A-30 et seq. The commenter stated that, given that an out-of-State bank automatically would be disqualified from being able to provide check cashing services to New Jersey check cashers because of the making of one of the three types of specified sub-prime loans through any means, the criteria is unrelated to the statutory prohibition on non-pawnbroker lending by licensed check cashers, citing N.J.S.A. 17:15A-47(e).

RESPONSE: The Department disagrees with the commenter that proposed N.J.A.C. 3:24-5.5(a)3 should be deleted. The Legislature has declared that usurious loans are violative of the public policy of New Jersey. The Department believes the application process is an appropriate means by which to support New Jersey public policy objectives. For example, in N.J.S.A 17:9A-20 et seq. and N.J.A.C. 3:1-2, compliance with community reinvestment obligations is required for approval to branch.

The Department strongly disagrees with the commenter's position that the Department is attempting surreptitiously to further a social policy by the proposal. The Summary and Economic Impact in the proposal clearly give notice that only those out-of-State institutions that do not engage in payday, title or refund anticipation loans would qualify for the privilege of being permitted to house the business accounts of a New Jersey licensed check casher. There is nothing secretive about it.

Further, the Department believes that the statute gives the Department broad authority in licensing and regulating check cashers. Among other things, it must determine the financial responsibility and general fitness of the applicant. This includes ensuring that licensees only use out-of-State institutions that comply with New Jersey's public policy on non-usurious lending.

COMMENT: One commenter stated that if an out-of-State bank is making illegal sub-prime loans in New Jersey, then it can be prosecuted and enjoined from violating N.J.S.A 2C:21-19 in proceedings commenced by New Jersey Division of Criminal Justice or the appropriate county prosecutor. The commenter stated that the proposed amendments have nothing to do with that issue and if the out-of-State bank acts lawfully in making sub-prime loans in New Jersey then the Department has no legitimate interest in preventing that conduct.

RESPONSE: The Department strongly disagrees with the commenter that the Department has no legitimate interest in preventing out-of-State banks from making usurious sub-prime loans in New Jersey. The public policy of New Jersey clearly reflects that usurious loans are a concern in this state. In passing the Home Ownership Security Act (HOSA), N.J.S.A. 46:10B-23 et seq., the Legislature noted that high cost lending threatens the viability of communities and that many

residents find themselves victims of overreaching lenders and that competition and self regulation have not eliminated abusive loan terms.

The Department recently adopted amendments to N.J.A.C. 3:4-4 regarding agents of foreign banks. The amendments prohibited foreign banks seeking to use the agent exemption from making payday, title or refund anticipation loans in New Jersey. The Department has and will continue to be vigilant in rooting out usurious lending, whether it be through the adoption of regulations, the issuance of bulletins, education outreach to consumers and communities or enforcement actions.

COMMENT: The commenter stated that legal sub-prime lending in New Jersey in excess of criminal usury as set forth at N.J.S.A. 2C:21-19 would have to be made through a process known as “rate exportation.” The commenter stated that this has been held to be a valid exercise of banking prerogatives conferred by Section 85 of the National Bank Act and that Federal and state courts have consistently upheld rate exportation against the efforts of states to curtail it.

RESPONSE: The Department does not fully agree with the commenter’s arguments regarding rate exportation. Moreover, they are not relevant to this rulemaking concerning New Jersey licensed check cashers. The Department has the authority to establish reasonable standards for out-of-State institutions in which New Jersey licensed check cashers may maintain their business accounts. The rule proposal does not interfere with the banking powers of national banks under Section 85 of the National Banking Act, or with the banking powers of out-of-State, state-chartered FDIC insured banks under section 27 of the FDI Act, 12 U.S.C. § 1831d. The rule governs which out-of-State institutions the Department will approve for use by New Jersey check casher licensees.

COMMENT: One commenter stated that it is virtually certain that proposed N.J.A.C. 3:24-5.5(a)3 is invalid and preempted by Federal banking law under the supremacy clause of the United States Constitution.

RESPONSE: The Department disagrees. Proposed N.J.A.C. 3:24-5.5(a)3 does not regulate the activities of any bank. It establishes criteria to be used by the Commissioner to approve out-of-State banks for use by New Jersey check cashers. The establishment of those criteria is not an infringement upon the exercise of a banking power, as under the current rules check cashers may not maintain their business account in any out-of-State bank. The commenter's contention that such a rulemaking is preempted by the United States Constitution is incorrect.

COMMENT: One commenter stated that all "payday loan" rate exportation is conducted by State-chartered banks under the supervision of the Federal Deposit Insurance Corporation (FDIC) and that the FDIC has issued explicit guidelines for banks making "payday loans" through rate exportation programs. The commenter stated that if a rate exporting bank complies with the FDIC guidelines, it has an absolute right to conduct payday lending in New Jersey no matter how negatively the Department views those transactions and irrespective of the criminal usury statute at N.J.S.A. 2C:21-19.

RESPONSE: The Department disagrees with the comment. The proposal addresses which out-of-State banks may be used by New Jersey check cashers, not the exportation of interest rates.

COMMENT: One commenter stated that whether an out-of-State bank is, or later commences, making payday loans, refund anticipation loans, or title loans has nothing to do with its ability to

provide proper commercial banking facilities to New Jersey check cashers. Further, the check casher account holders have no power to control or meaningfully influence whether the out-of-State bank engages in improper forms of sub-prime lending. The commenter stated that the check cashing industry needs the broadest possible range of available banks with which to conduct business and that the Department should abandon its use of a subterfuge to regulate the lawful conduct of out-of-State banks.

RESPONSE: The Department disagrees. The regulation in question does not have as its intent the exercise of control over out-of-State banks. The Department further disagrees with the commenter's statement that whether a bank makes criminally usurious loans has nothing to do with that bank's ability to provide proper commercial banking facilities to New Jersey check cashers. The New Jersey Legislature has through usury laws, banking laws, HOSA and other consumer-protective laws, provided guidance regarding what it regards as "proper banking facilities." (Similarly, various licensing laws provide standards for the appropriate conduct of licensed activities.) In exercising its authority with respect to specifying those depositories in which New Jersey licensed check cashers may maintain their business accounts, the Department follows this legislative guidance. It has determined that out-of-State banks that make loans that violate New Jersey public policy, as expressed by the Legislature, will not be considered qualified for use by New Jersey check casher licensees.

COMMENT: One commenter stated that proposed N.J.A.C. 3:24-5.5(a)3 is so unrelated to reality and any valid State concern that it constitutes a violation of the Federal Commerce Clause. The commenter stated that it is well known that many banks with branches in New Jersey have made and continue to make various forms of criminally usurious loans, especially

refund anticipation loans. The commenter argues that the regulation proposed only precludes out-of-State banks which offer such loans from servicing licensed check cashers, while all banks with branches in New Jersey can make as many criminally usurious loans as they like, both directly and indirectly in this State, yet still provide check cashers with commercial banking services.

RESPONSE: The position of the Department, based on clear statutory language, is that criminally usurious loans are illegal and unenforceable. The Department disagrees that proposed N.J.A.C. 3:24-5.5(a)3 is violative of the Federal Commerce Clause. The Department has noted the position articulated in the comment regarding the explicit reference in the rule to out-of-State institutions and the absence of any corresponding reference to in-state institutions. The Department will consider proposing appropriate amendments in the future to address this issue.

COMMENT: One commenter stated that if the Department wants to mount an assault on rate exportation sub-prime lending, it should do so openly in the Legislative arena, noting that was the holding in the Appellate Division's recent *Muhammed* [sic] opinion.

RESPONSE: The Department is aware of the Appellate Division decision in *Muhammad v. County Bank of Rehoboth Beach Delaware, et al*, 339 N.J. Super. 222 (App. Div. 2005). The Muhammad case involved a series of three payday loans to college student Jaliyah Muhammad. The first one had an annual percentage rate of 644.1 percent, the second one had an annual percentage rate of 608.33 percent and the third with an annual percentage rate of 782.44 percent. Muhammad filed a class action complaint challenging the scheme whereby County Bank lent its charter to Main Street Bank to attempt to enable them to charge usurious loan rates to New Jersey citizens based upon principles of Federal preemption of New Jersey law. Muhammad

asserted violations of the New Jersey Consumer Fraud Act, civil usury and racketeering. The matter reached the Appellate Division through an interlocutory appeal on the issues of whether the arbitration clause in the loan agreement it was unconscionable, and whether plaintiff was entitled to discovery before the court decided if the arbitration clause was enforceable. The holding of the case addressed those two issues, not legislative action on rate exportation as asserted by the commenter.

The Department further notes that in the *Muhammad* case, although it was a unanimous Appellate Division opinion, the New Jersey Supreme Court granted the plaintiff leave to appeal on September 19, 2005, and heard oral argument on the appeal on February 14, 2006. The opinion on the interlocutory aspects of the case has not been issued as of the filing of this Notice of Adoption.

Regardless, the current rulemaking is not an assault on rate exportation. It concerns which out-of-State institutions will qualify for approval to house the business accounts of New Jersey licensed check cashers. Moreover, such approval does not mandate that, among various available institutions, a check casher use any particular approved institution. Market forces will control.

COMMENT: The commenter stated that the survival of the check cashing industry should not be mixed up with the Department's antipathy to criminally usurious lending.

RESPONSE: The proposal is designed to enhance the survival of the check cashing industry. An expansion of the pool of qualified depositories is achieved without condoning the use of the few institutions that engage in activities that would be criminally-usurious by New Jersey standards.

COMMENT: One commenter stated that even if the Department retains N.J.A.C. 3:24-5.5(a)3 upon adoption, there needs to be clarification of exactly what constitutes making such loans “in this State.” The commenter stated that the broad definitions in N.J.A.C. 3:24-1.3 and each definition at section 4 could be construed to mean a loan is made in New Jersey if a consumer domiciled here learns of the opportunity to obtain the loan through mass media disseminated across state lines. The commenter stated that the Department is aware that all forms of taboo loans are countenanced under Delaware law and that there are many payday loan stores in Pennsylvania that conduct their transactions through rate exportation. The commenter wondered whether, if a New Jersey resident learns from mass media in the Philadelphia area that he or she can obtain a payday loan in Pennsylvania or Delaware and takes out that loan by traveling to that state, the transaction would be deemed to be “in this State” because the newspaper was circulated in or the radio/television commercial was broadcast into New Jersey. The commenter stated that if it were, apart from Federal preemptions, the application of the regulations would constitute a violation of the Federal Commerce Clause and also violate a number of interstate compacts and uniform state laws.

RESPONSE: The definition of “in this State” is determined largely by case law interpreting the Commerce Clause of the U.S. Constitution. The Department recognizes the holdings in such cases regarding the dissemination of advertising across state lines. However, the Department also notes principles of judicial enforcement whereby courts may refuse to enforce contracts entered into in another state that violate the public policy (such as criminal law) of the forum’s state.

COMMENT: One commenter suggested that there be a slight modification in the second sentence of proposed N.J.A.C. 3:24-5.5(e). That part of the proposal requires a check casher to “submit and comply with a plan” to move its business accounts “within a short timeframe” when an out-of-State bank no longer satisfies the prerequisites in proposed N.J.A.C.3:24-5.5(a). The commenter urges that the phrase “short timeframe” be modified to “reasonable timeframe.” The commenter explained that they believed that “short” is an inappropriate stricture to impose on a check casher that needs to form a new banking relationship. The commenter states that a “reasonable timeframe” should be permitted, especially when the proposed amendments are necessitated by the scarcity of banks willing to provide commercial banking facilities to check cashers. The commenter notes that if the word is changed, the Department will be able to assess what constitutes a “reasonable timeframe” given all pertinent factors, which factors differ greatly from business to business based on the volume of transactions, location, the types of transactions and a number of other variables.

RESPONSE: The Department agrees. Upon adoption, the word “reasonable” is being substituted for the word “short” in N.J.A.C. 3:24-5.5(e) to modify the description of the length of the timeframe that a check casher would have to move its business accounts to a different institution should that become necessary. The word “short” was never intended to mean a timeframe that was unreasonable. Therefore, the change better states the Department’s original intent. This change may be made upon adoption without additional public notice and comment because there is no substantive change to the underlying concept that, when required, the movement of accounts from one institution to another should be accomplished without undue delay, but also without needing to conform to an overly burdensome time schedule.

COMMENT: One commenter urged that the third and final sentence of proposed N.J.A.C. 3:24-5.5(e) be modified. That part of the proposal reads "...or fails to comply with a plan submitted..." The commenter urged that additional language be added so that it would read "...or fails to comply with a plan submitted and accepted by the Department..." The commenter suggests that the plan by the check casher to obtain new banking facilities should be accepted by the Department before the failure to comply with it permits the Department to take action against a check casher. The commenter makes it clear that it is not urging that the Department be required to "approve a plan" only that the plan be "accepted," as the latter entails a considerably lesser exercise of substantive judgment.

RESPONSE: The Department does not believe the change suggested by the commenter is necessary. If a change in institution is necessary, the Commissioner will notify the check casher to submit a plan and comply with it in a reasonable timeframe. The timeframe will be established by the Commissioner. The check casher will then have the reasonable period of time to implement the change and will be well aware of what is required. Only after the expiration of this reasonable period of time would there be the need for enforcement. The plan required is not anticipated to be overly complicated so as to require the step of submission and acceptance by the Department. The plan would be to choose a different financial institution. The Department will monitor such situations and, if it is determined that there is a need for a submission and acceptance procedure, will propose amendments to the rules similar to the suggestion in the comment.

COMMENT: One commenter noted that new definitions are proposed to be included in N.J.A.C. 3:24-1.5 which are "payday loan," "refund anticipation loan," and "title loan." The

commenter noted that each definition attempts to incorporate the limitations on lawful loans set forth at N.J.S.A. 2C:21-19(a), New Jersey's criminal usury statute. The commenter states that each new definition refers to a "...rate... that exceeds the limitation on usury..." The commenter states that this language is technically inaccurate and confusing. They stated that criminal law establishes that a rate exceeding the statutory limit is "...not... a rate authorized or permitted by law..." They stated that the statute does not create a "limitation on usury," and the definitions proposed should be clarified. The commenter suggests striking the term "...limitation on usury set forth at..." and inserting in its place "...limits on lawful interest rates set forth in..."

RESPONSE: The Department agrees and will make changes to the three definitions in N.J.A.C. 3:24-1.3 upon adoption. As proposed, these three definitions reference "the limitation on usury set forth at N.J.S.A. 2C:21-19." In its definition of "usury," N.J.S.A. 2C:21-19 uses the term "maximum rate permitted by law" and goes on to define that rate. The changes being made upon adoption will incorporate into the rule the same statutory language, "maximum rate permitted by law," and referring to that rate as it is used in the statute. These changes are being made to have the text of the rule more closely track the language in N.J.S.A. 2C:21-19. This change may be made upon adoption without additional public notice and comment because no substantive change is being made to the concept reflected in the proposal that the prohibited payday, refund anticipation and title loans are those that exceed the rate limitation established by N.J.S.A. 2C:21-19, the criminal usury statute.

COMMENT: One commenter suggested that proposed N.J.S.A. 3:24-5.5(a), line 4, which states in part "...by the Commissioner as set forth in section..." should be modified to reflect that in determining whether to approve the use of an out-of-State bank, the Commissioner will apply the specific substantive standards in the amendment. The commenter believes that the phrase "as set

forth” can be construed as denoting a procedure incorporating standards and that the clear intent of the proposed amendments is to incorporate the criteria immediately below it. Therefore, the commenter urges the deletion of the word “as” in the phrase “as set forth” and replacing it with the words “applying the criteria,” so that it will read “applying the criteria set forth” in place of what was proposed.

RESPONSE: The Department disagrees because it thinks that the language is clear that the Department will rely on the three requirements specified in that subsection when determining whether an out-of-State institution would qualify for approval by the Department. The Department declines to make the change requested by the commenter because it is unnecessary.

Federal Standards Statement

The adopted amendments are not subject to any Federal standards or requirements. Therefore, a Federal standards analysis is not required.

Full text of the adopted amendments follow: (additions to proposal indicated in boldface with asterisks***thus***; deletions from proposal indicated in brackets with asterisks*[thus]*):

3:24-1.3 Definitions

Words and terms, when used in this chapter, shall have the meanings as defined below, unless the context clearly indicates otherwise.

...

"Payday loan" means an agreement to defer the presentment of a negotiable item, or defer the deposit of an item for collection, or defer debiting the borrower's account electronically or by any other means, in return for a consideration or other thing of value where the rate, fee or other consideration charged for such forbearance exceeds the *[limitation on usury set forth at]* ***"maximum rate permitted by law" as that phrase is used in*** N.J.S.A. 2C:21-19. "Payday loan" shall include, but not be limited to, such loans made.

1. - 4. (No change from proposal.)

...

"Refund anticipation loan" means an agreement to lend a borrower funds, or to extend any other consideration to a borrower, in return for a promise by the borrower to repay the loan or other consideration that includes an assignment of the borrower's Federal and/or state tax refund, where the rate, fee or other consideration charged for such forbearance exceeds the *[limitation on usury set forth at]* ***"maximum rate permitted by law" as that phrase is used in*** N.J.S.A. 2C:21-19. "Refund anticipation loan" includes, but is not limited to, such loans made:

1. - 4. (No change from proposal.)

...

"Title loan" means an agreement to lend a borrower funds, secured by a title to a motor vehicle, which loan is in return for a consideration or other thing of value where the rate, fee or other consideration for such forbearance exceeds the *[limitation on usury set forth at]* ***"maximum rate permitted by law" as that phrase is used in*** N.J.S.A. 2C:21-19. "Title loan" shall include, but not be limited to, such loans made:

1. - 4. (No change from proposal.)

3:24-5.5 Deposits

(a) - (d) (No change from proposal.)

(e) If an out-of-State financial institution approved by the Commissioner fails to maintain the standards specified in (a) above or if the institution is placed under a supervisory order from its primary regulator or operates in a manner inconsistent with safe and sound financial practices, the Commissioner may take such action as he or she deems appropriate and necessary to protect the licensee and the public. The action may include revoking the approval conferred by the Commissioner on the institution pursuant to (a) above and requiring any check casher utilizing that institution to submit and comply with a plan for moving its business account(s) to a different institution within a *[short]* **reasonable*** timeframe established by the Department. If a check casher utilizing such an institution fails to supply such a plan or fails to comply with a plan submitted, the Department may suspend, revoke or refuse to renew the license of the check casher pursuant to N.J.S.A. 17:15A-48(a)1.

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