High-Cost Payday Lending Traps Arizona Borrowers

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- Over 700 payday lenders charging up to 459% annual percentage rate (APR) for a two-week loan are located throughout Arizona; with the highest concentrations per capita in Pinal, Mohave, and Maricopa Counties.

- A typical Arizona borrower pays an estimated $516 in fees for a $325 payday loan and still owes the $325 in principal. Overall, payday lending costs Arizona families nearly $149 million each year. Payday lending drains $91 million and $23 million from Maricopa and Pima County households, respectively.

- Payday lenders will no longer be able to charge triple-digit interest rates when their exemption to Arizona's 36% rate cap expires in 2010 unless Proposition 200 is approved by voters this November. This proposition only decreases the cost of a two-week payday loan from 459% to 391% APR.

We conclude that Proposition 200 will not lead to effective reform; instead, its passage would mean Arizona payday borrowers would remain mired in the debt trap.

Introduction

A payday loan is a small, short-term loan of up to $500 secured by the borrower's personal check. Marketed as a quick and easy solution to dealing with an unexpected expense, these loans are generally due in about two weeks. In Arizona, borrowers can be charged up to $17.65 per $100 borrowed, which equates to a cost of 459% APR.

Payday Loan Basics

- Loans of up to $500
- Usually due in two weeks
- Fee of $17.65 per $100 borrowed, or 459% APR
- Average borrower takes 9 loans per year

To qualify, a customer seeking a payday loan typically needs just a form of identification, a checking account, and proof of income either from a job or government benefits like Social Security. The borrower provides the lender with a personal check for the amount of cash they are receiving that day plus the fee. If the borrower does not pay back the loan when due, the lender can cash their personal check as repayment.

Because the entire loan amount, plus the fee, is due in two short weeks, borrowers typically find it hard to pay back a payday loan and also meet their regular living expenses. The result is that borrowers either have to extend their loan out another two weeks by paying an additional fee, or pay back their loan and then take out another a few days later when their money runs out. This is the start of the payday lending debt trap cycle, where a borrower intends to only take one loan, but ends up having to take another each pay period. The average payday borrower takes out 9 payday loans a year, and an industry researcher has noted that the typical borrower stays in payday loans for 18 months.[1]

Arizona's Payday Lending Experience
Until the beginning of this decade, no Arizona lender was permitted to offer a small loan product in excess of 36% APR. In 2000, however, the legislature passed a law exempting payday lenders from the 36% APR rate cap for all other small loan products. Instead, payday lenders were allowed to charge up to $17.65 per $100 borrowed for loans of up to $500 with a term of at least five days. For the typical two-week payday loan, this equates to an APR of 459%. This legislation, which was signed into law by the Governor in April 2000, includes a sunset provision, which removes this special exemption to the 36% APR rate cap on July 1, 2010. This means that payday lenders will soon no longer be able to charge triple-digit rates and instead will have to abide by the laws that apply to all of Arizona's other small loan lenders.[2]

As of August 2008, there were over 700 payday lending licensees located across Arizona. While payday lenders are distributed throughout all but two counties, the most payday lenders per capita are in Pinal, Mohave, and Maricopa Counties.

Nationally, payday borrowers take out an average loan of $325. Payday lenders tend to charge the maximum allowed by state law; not competing on price with nearby storefronts. Based on this data, we find that **payday lenders make over $841 million in loans each year, draining nearly $149 million in fees from Arizona borrowers.**

County	Payday Lenders[3]	Loan Volume[4]	Total Fees Paid[5]	Stores per 100,000 people[6]
Apache*	0	--	--	--
Cochise	14	16,639,350	2,936,845	11.9
Coconino	15	17,827,875	3,146,620	12.9
Gila*	6	7,131,150	1,258,648	11.7
Graham*	3	3,565,575	629,324	9.0
Greenlee*	0	--	--	--
La Paz*	1	1,188,525	209,775	5.1
Maricopa	434	515,819,850	91,042,204	14.1
Mohave	30	35,655,750	6,293,240	19.4
Navajo*	9	10,696,725	1,887,972	9.2
Pima	110	130,737,750	23,075,213	13.2
Pinal	31	36,844,275	6,503,015	16.7
Santa Cruz*	4	4,754,100	839,099	10.4
Yavapai	21	24,959,025	4,405,268	12.5
Yuma	16	19,016,400	3,356,395	10.0
Other licensees	14	16,639,350	2,936,845	
TOTAL	**708**	**$841,475,700**	**$148,520,461**	

*These counties have populations of less than 100,000.

The vast bulk of revenues generated by payday lenders leave Arizona, flowing to companies headquartered in other states. Each of the top ten lenders in Arizona listed below is headquartered elsewhere.

Business Name	Number of Locations	Company Headquarters
Ace Cash Express	108	Texas
Advance America	56	South Carolina
Loan Mart/Money Mart (Dollar Financial Group)	55	Pennsylvania
Check Into Cash	47	Tennessee
Southwest Check Cashing/Check$mart (Buckeye Check Cashing)	46	Ohio
Quik Cash (Q.C. Holdings)	40	Missouri
Check 'n Go (Southwestern & Pacific Specialty Finance)	34	Ohio
Allied Cash Advance	33	Florida
Fast Payday Loans, Inc.	29	Georgia*
Checkmate Payday Loans (L.M.S.A. Financial Corporation Arizona)	27	Washington State*

*Headquarters for Fast Payday Loans and Checkmate could not be confirmed; however these companies' primary contact information lists an out-of-state address

For the average borrower taking out nine loans per year (an initial loan and then 8 subsequent consecutive transactions), this means they will pay $516 in fees for $325 in credit, and still owe $325 in principal. **In total, they pay $841 to borrow $325.** Because these nine loans are typically taken out one after the other—either as a renewal or as a back-to-back transaction—the borrower is not really extended new credit each time, but rather paying a fee to re-open the initial loan every two weeks.[7]

$325 Loan	
Fee of $17.65 per $100 borrowed	$57
Total fees paid with nine loans	$516
Total fees plus principal due to payday lender $516 (fees)+ $325 (principal)	$841

Payday Lenders Threaten to Continue the Debt Trap Cycle

The payday lending industry depends on borrowers becoming trapped in debt for the bulk of their revenues. For example, national data show that:

- 90% of payday lending business is generated by borrowers with five or more loans a year, and
- 60% of payday lending business is generated by borrowers with at least 12 loans a year.

This dependence of repeat borrowers is evident in a statement by Carol Stewart, the Vice President of Government Affairs for Advance America. When asked why her company was opposed to limiting borrowers to five loans a year (which would allow them to navigate more than one financial emergency a quarter), she stated: ""We can't live on five [loans]."[8] A remark from the CEO of Cash America is also telling: "And the theory in the business is you've got to get that customer in, work to turn him into a repetitive customer, long-term customer, because that's really where the profitability is."[9]

With the special exemption allowing payday lenders to charge triple digit rates scheduled to come to an end in Arizona in July 2010, payday lending revenues are threatened by the prospect of no longer being able to trap borrowers in debt. In response, payday lenders have put Proposition 200—which would remove the sunset provision and allow payday lenders to continue to charge triple-digit APRs—on the ballot. Called the "Payday Loan Reform Act," this ballot initiative also includes provisions such as limiting borrowers to one loan at a time and one payment plan per year that sound promising. However, in other states that have adopted these types of reforms, with much stronger enforcement that proposed in Arizona, payday borrowers continue to be trapped in long-term, high-cost debt at roughly the same levels as before this "reform" (see Appendix 1 for more details on all of Proposition 200's provisions and Appendix 2 for a summary of how these reforms have failed in other states).

Industry-Sponsored Payday Loan Reform Act

-Repeals sunset clause which would lower payday loan rates to 36% APR in 2010

-Only lowers rate charged from 459% APR to 391% APR on a two-week payday loan

Proposition 200 will not stop the payday loan debt trap

Many states and the federal government have acted to end triple-digit interest rate payday loans. Fifteen states and the District of Columbia enforce reasonable interest rate caps on all small loans (these states' rate caps are detailed in Appendix 3). [10] In addition, Congress passed and President Bush signed into law a cap of 36% APR on loans to members of the military, whose security clearances and deployment schedules were found to be threatened by payday and other high-cost lenders.[11]

In July 2010, Arizona is poised to similarly eliminate the harmful impact of this abusive product on its citizens. However, if payday lenders have their way and pass Proposition 200, Arizonans will be paying 391% APR on their payday loans (down from 459%), rather than falling back to the 36% cap in 2010. In fact, the whole point of the payday lending industry's ballot initiative is to remove the 2010 sunset date that would force them to lend at the 36% interest cap for all other small lenders in the state. This sunset date, if not removed by the payday industry's initiative, will level the playing field for all small loan lenders, by eliminating the special exemption that has allowed payday lenders to charge rate 10 times higher than other small lenders.

From our analysis, we must conclude that **Proposition 200 will not lead to effective reform; instead, Arizona payday borrowers will remain mired in the debt trap.**

APPENDIX 1: Proposition 200 provisions

The proposed changes in Proposition 200 include:

- *Removing the sunset provision in the 2000 authorization of payday lending.* Payday lenders' exemption from the 36% APR small loan rate cap is scheduled to sunset on July 1, 2010. This provision removes this sunset clause, thereby allowing payday lenders to continue charging triple-digit annual interest.

- *Lowering the allowable fee from $17.65 per $100 borrowed to $15 per $100 borrowed.* This provision reduces the APR on the typical two-week payday loan from 459% to 391%, still 10 times higher than the interest rate cap for other small lenders in the state.

- *Capping the maximum loan term at 35 days.* While the provision would cap the maximum loan duration at 35 days, it fails to lengthen the minimum term of 5 days. Thus, lenders could still make two-week loans at 391% APR.

- *Limit to One Loan Outstanding with a 24 Hour Cooling Off Period.* The proposition includes no effective enforcement for this one loan at a time provision. Even if this provision were enforced, a payday lender could make as many as 24 two-week loans to a borrower in a single year. In Florida, which already has this provision and clear enforcement through a comprehensive database, the typical borrower still gets caught in the same debt trap--paying off their loan, waiting a short period of time, and then taking out another in a "back-to-back transaction."[12]

- *Debit Access to Borrower Accounts.* While characterized by the industry as offering convenience, in reality this provision would give payday lenders unfettered access to customer bank accounts and facilitate overcharging through continuous fees. In addition, this provision could open the door to other forms of payday lending, such as internet and kiosk payday lending.

- *Repayment Plan.* This provision would limit consumers' rights of renegotiation to one request of a repayment plan annually. Currently Arizona law allows borrowers and lenders to engage in unlimited renegotiation. In addition, it merely gives borrowers the right to ask for a repayment plan, rather than requiring lenders inform them of this option. States that collect data on repayment plan usage report only between 1-3% of eligible transactions employ this option.[13]

- *Borrower Database to Track Borrowers with Repayment Plans.* While other states employ databases to enforce provisions such as a one loan limit and cooling off period, the database proposed in Arizona will only be used to ensure that borrowers do not take advantage of more than one repayment plan each year.

- *Disclosures in Spanish or English.* This proposal would require that a copy of the written agreement currently required under Arizona law be made available to borrowers at their request in Spanish or English.

APPENDIX 2: Experiences of other states with payday lending "reforms"

As shown in the table below, the experience of states introducing similar payday lending "reforms" short of a rate cap at or about 36% interest are ineffective.

	Regulations	Results
Florida[14]	• $500 maximum loan amount • No more than one outstanding loan at a time • $10 per $100 (plus verification fee) maximum fee • 24 hour cooling off period after each loan • 60 day grace period available, upon declaration of inability to repay • Rollovers prohibited • Database	• 89% of loans go to borrowers with five or more transactions per year • 58% of loans go to borrowers with 12 or more transactions per year • Average of 8 loans per borrower • Less than one percent of transactions take advantage of the 60 day grace period • 45% of new loans are taken out the day after the previous loan paid off; 88% of new loans are taken out in the same two week pay period that previous loan is paid off
Michigan[15] *13 month time period as reported by regulator	• $600 maximum loan amount • No more than two loans outstanding at a time (can only have one loan outstanding per lender) • Maximum fee of 15% for 1st $100 borrowed; 14% for 2nd $100; 13% for 3rd $100; 12% for 4th $100; and 11% for 5th and 6th $100 • Payment plan option • Rollovers prohibited • Database	• 94% of loans go to borrowers with five or more transactions* • 77% of loans go to borrowers with 12 or more transactions* • Average of 8 loans per borrower • 2% of eligible transactions employ payment plan

	Regulations	Results
Oklahoma[16]	• $500 maximum loan amount • No more than two outstanding loans at a time • $15 per $100 maximum fee on loans up to $300; $10 per $100 maximum fee on loans of $301-500 • Two business day cooling off period after 5th consecutive loan • Payment plan option available after 3rd consecutive loan • Rollovers prohibited • Database	• 91% of loans go to borrowers with five or more transactions per year • 64% of loans go to borrowers with 12 or more transactions per year • Average of 9 loans per borrower • Less than 2% of eligible transactions employ payment plan • 59% of new loans are taken out the day after the previous loan paid off; 87% of new loans are taken out in the same two week pay period that previous loan is paid off
Washington[17]	• Cannot borrow more than $700 from a single lender at one time • $15 per $100 maximum fee on loans up to $500, then $10 per $100 on remaining portion of loan up to $700 • Payment plan option available after 4th consecutive loan with same company • Rollovers prohibited	• 89% of loans go to borrowers with five or more transactions per year • 56% of loans go to borrowers with 12 or more transactions per year • Average of 8 loans per borrower • 1.2% of all transactions employ the payment plan option

APPENDIX 3: States with reasonable small loan interest rate caps

State	Maximum Annual Interest Allowable[18]
Arkansas (new AG ruling that this cap applies to payday loans)	17%
District of Columbia	24%
Georgia	60%
Maine	30%
Maryland	33%
Massachusetts	23%
New Hampshire (new law, taking effect Jan 2009)	36%
New Jersey	30%
New York	25%
North Carolina	36%
Ohio (new law, being challenged by ballot referendum by payday lenders)	28%
Oregon	36%
Pennsylvania	24%
Vermont	18%
West Virginia	31%

[1]Summarizing all available state regulator data, the Center for Responsible Lending reports a national average of 8.7 loans per borrower per year. See Uriah King and Leslie Parrish, *Springing the Debt Trap*, Center for Responsible Lending (December 13, 2007). Pat Cirillo of Cypress Research Group, in testimony to the Ohio House Committee on Financial Institutions, Real Estate and Securities, January 31, 2008 noted that "…if you look at the cycle, the amount of time that folks tend to use this product, they are in and out of it really for about 18 months." Transcript on file with the Center for Responsible Lending.

[2]For more details, see Ariz. Rev. Stat. § 6-1251 et seq.

[3]Arizona Department of Financial Institutions, Deferred Presentment licensees as of August 27, 2008.

[4]The Center for Responsible Lending finds that, nationally, the average payday lending store makes 3,657 loans per year and the average payday loan size is $325. To estimate loan volume for Arizona counties, we multiply the number of stores by 3,657 loans. Then we take the total loans and multiply by $325. For more information on the Center for Responsible Lending's estimates, see Uriah King, Leslie Parrish, and Ozlem Tanik, *Financial Quicksand*, Center for Responsible Lending (November 2006).

[5] Payday lenders generally charge the maximum amount permitted by law. In Arizona, payday lenders can charge up to $17.65 per $100 borrowed.

[6]Arizona population by county from U.S. Census (2000).

[7]Regulator data from Florida and Oklahoma (the only states with this level of detailed data available) shows that 45% and 59% of repeat payday transactions, respectively, are opened at the borrower's first opportunity. In addition, 88% and 87% of new loans are originated before the borrower receives their next paycheck. Data on file with the Center for Responsible Lending.

[8]Jeff Shapiro, "Payday-loan fights loom." *The Richmond Times-Dispatch* (February 29, 2008).

[9]Dan Feehan, CEO of Cash America, remarks made at Jefferies Financial Services Conference (June 20, 2007). Transcript on file with the Center for Responsible Lending.

[10]High-cost payday loans are not available in the following states/jurisdictions: Arkansas, Connecticut, the District of Columbia, Georgia, Maine, Maryland, Massachusetts, New Jersey, New York, North Carolina, Pennsylvania, Vermont, and West Virginia. In addition, Oregon's small loan law allows small loans of 36% plus a $10 per $100 fee for a 31 day or longer loan term. Ohio's new 28% APR rate cap was to take effect in September 2008 but is currently being challenged by a payday lending industry-sponsored ballot initiative and New Hampshire's 36% APR rate cap will take effect January 1, 2009.

[11] The Military Lending Act, which caps interest rates on small loans of 91 days or less to active duty military and their dependents was part of the John Warner National Defense Authorization Act for Fiscal Year 2007, signed into law in October 2006. The interest rate cap took effect October 1, 2007.

[12]According to the state regulator, nearly half (45%) of repeat payday transactions happen as soon as the 24 hour cooling-off period expires and 88% of transactions are originated before the borrower receives their next paycheck. Data on file with the Center for Responsible Lending and summarized in Uriah King and Leslie Parrish, *Springing the Debt Trap*, Center for Responsible Lending (December 13, 2007).

[13]According to regulator data, 0.42 percent of eligible transactions have employed a grace period in Florida; 2.4 percent of eligible transactions have gone into a payment plan in Michigan, and 1.8 percent of eligible transactions have gone into a payment plan in Oklahoma. See Uriah King and Leslie Parrish, *Springing the Debt Trap*, Center for Responsible Lending (December 13, 2007).

[14] *Florida Trends in Deferred Presentment*, Prepared by Veritec Solutions LLC for the Florida Department of Banking and Finance (August 2007). Summary calculations by the Center for Responsible Lending.

[15] *Michigan Trends in Deferred Presentment*, Prepared by Veritec Solutions LLC for the Michigan Office of Financial and Insurance Services (July 31, 2007). Summary calculations by the Center for Responsible Lending.

[16] *Oklahoma Trends in Deferred Deposit Lending*, prepared by Veritec Solutions LLC for the Oklahoma Department of Consumer Credit (May 2007). Summary calculations by the Center for Responsible Lending.

[17] Data is based on reporting from 92% of the industry. See *2006 Payday Lending Report*. Washington State Department of Financial Institutions (2007).). Summary calculations by the Center for Responsible Lending.

[18] For more information on interest rate caps on small loans by state, see www.paydayloaninfo.org, maintained by the Consumer Federation of America.