A 36% APR cap on high-cost loans promotes financial recovery

Loans at 400% annual interest wreck family finances

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QUICK REFORM COULD PLUG $5 BILLION HOLE IN WORKER WALLETS

Urgent need to stimulate economy makes reforming predatory lending a priority

Former President George W. Bush's 2008 tax rebate was designed to stimulate the economy by putting dollars back into the hands of working people. In May of 2008, the IRS sent $600 checks to households making less than $75,000 per individual and $100,000 per couple, with an additional $300 for each qualified child. President Barack Obama has also proposed a combination of cutting taxes and encouraging spending to aid in economic recovery.

A 36% cap costs taxpayers nothing and protects worker earnings and benefits

- Nearly 12 million Americans are caught in a cycle of five or more high-cost payday loans per year.
- Nationally, nearly $5 billion per year is stripped from the earnings of working people and transferred to predatory lenders through practices like payday lending.
- Congress protected military personnel from predatory payday lenders by passing a 36% cap on annual interest in 2006.
- States that enforce two-digit interest rate caps save their citizens nearly $2 billion per year collectively.

But in the meantime, predatory lenders are stripping cash from the earnings of working people who fall into this same demographic—at astounding rates. Payday loans carry annual interest rates of around 400 percent. They trap people in debt to the extent that the average borrower has nine payday transactions a year. Payday lending alone costs American families $4.2 billion in predatory fees, while other types of high-cost lending such as car title loans and refund anticipation loans strip additional earnings and benefits. (See "Financial Quicksand," www.responsiblelending.org)

For every payday lending staff position, 179 Americans are caught in the cycle of high-cost payday debt

We estimate that, of the 19 million borrowers taking out payday loans, 62 percent, almost 12 million, are caught in a cycle of five or more high-cost payday loan transactions a year.[1]

Nationally, the payday lending industry employs approximately 66,000 people in relatively low-paying jobs with very high turnover rates.[2] That figure includes employees of stores that offer other services like pawn, check-cashing and bill paying services.

Based on this calculation, for every employee of this industry, there are 179 working Americans, or others who have a steady source of income such as retirement or disability benefits, who end up paying at least $250 in interest for a $300, a loan that is designed so that they cannot afford to pay it off and walk away after paying the first $50 fee. The average borrower pays even more, about $450 in interest for nine transactions, plus the $300 principal.

Quick cash scams contribute to bankruptcies and the unbanking of Americans

No one plans to be trapped in high-cost debt for weeks or months, but that is in fact what typically happens with payday loans. Salary cuts, job losses, and higher prices for gas, food and housing can quickly cut into a family's budget, making cash shortfalls more likely—and payday loans more dangerous.

One recent study found that bankruptcy is more likely for payday borrowers as compared to similarly situated applicants who could not qualify for a payday loan: the applicants approved for payday loans were twice as likely to end up in bankruptcy.[3] And a recent report from Harvard Business School found that payday lending puts families' ability to have a bank account at risk. The study found that payday loans are associated with more closed bank accounts due to multiple overdrafts.[4]

A 36% interest rate cap costs taxpayers $0, potentially saves $5 billion nationally

A 36 percent interest rate cap for high-cost loans eliminates the predatory practice of charging 400 percent annual interest, and effectively springs the debt trap that payday lenders have set for their customers. A two-digit interest rate cap is already saving the 15 states and the District of Columbia which enforce such a cap nearly $2 billion. In addition, a federal 36 percent cap on loans to military personnel and their families has stopped the worst payday lender abuses of those serving our country. Our civilian working families are in dire need of the same protections.

Payday lending industry representatives have lobbied for other reforms, such as payment plans and limits on loan amounts, because they understand that these measures have done nothing to slow the rate at which they can flip loans to the same borrowers. But an interest rate cap is the only measure that has proven effective in putting an end to the cycle of debt caused by these loans. (See "Springing the Debt Trap," www.responsiblelending.org)

A cap for economic recovery

Congress should enact an interest rate cap for high-cost lenders in the range of 36 percent, as a quick and essential step toward economic recovery. Such a cap will cost taxpayers nothing and protect the earnings and government benefits of American households, thereby allowing these families to save, spend, and recover from their financial shortfalls in the long term.

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[1] The FDIC reports that young payday stores have a median 693 borrowers per store, and mature stores have a median 1,037 borrowers per store. This averages 865 borrowers per store. FDIC Center for Financial Research Working Paper No. 2005-09, "Payday Lending: Do the Costs Justify the Price?", Mark Flannery, Katherine Samolyk, June 2005. Stephens Inc. reports that at the end of 2007, there were an estimated 23,586 stores offering payday loans nationwide. Stephens Inc., Investment Bankers Industry Report, April 17, 2008. Subtracting the stores from Ohio, Arkansas, and New Hampshire, which have recently passed payday lending reforms, a more conservative number would be 21,999. 21,999 stores * 865 borrowers = 19,029,135 borrowers.
[2] The FDIC reports that the median number of full-time employees per store is 2 for a young store and 3 for a mature store. For our conservative estimate of how many Americans are caught in a cycle of debt per payday employee, we calculate 3 employees per store (about 22,000). (See *Flannery*, endnote 1.) "As of December 31, 2007, the annual turnover among our center managers was approximately 58% and among our other center employees was approximately 120%. Approximately 50% of the turnover

has traditionally occurred in the first six months following the hire date of our center managers and employees." ADVANCE AMERICA, CASH ADVANCE CENTERS, INC., 2007 Form 10-K report to U.S. Securities and Exchange Commission.

[3] Paige Marta Skiba (Vanderbilt) and Jeremy Tobacman (U. Pennsylvania). *Do Payday Loans Cause Bankruptcy?* October 10, 2008. Available at: http://www.law.vanderbilt.edu/faculty/faculty-personal-sites/paige-skiba/publication/download.aspx?id=2221

[4] Specifically, an increase in the number of payday lending locations in a particular county is associated with an 11 percent increase of involuntary bank account closures, even after accounting for county per capita income, poverty rate, educational attainment, and a host of other variables. Dennis Campbell, Asis Martinez Jerez, and Peter Tufano (Harvard Business School). *Bouncing Out of the Banking System: An Empirical Analysis of Involuntary Bank Account Closures*. June 6, 2008. Available at: http://www.bos.frb.org/economic/eprg/conferences/payments2008/campbell_jerez_tufano.pdf