



FINANCIAL SERVICE CENTERS OF AMERICA

Fact Sheet: Payday Advances

Payday Advances Offer Consumers A More Desirable Alternative To Other Credit Options

Payday advances (PDAs) are small, short-term cash advances, typically of \$500 or less. In recent years, PDAs have become an increasingly popular choice for American consumers in need of small dollar, short-term credit and 35 states have laws permitting these loans. Today industry analysts estimate that there are more than 22,000 locations that offer PDAs nationwide, extending nearly \$50 billion annually in short-term credit to between 15 and 17 million American households. Transparency is a key element of the PDA product. All terms and fees are clearly posted in every store and included in every contract. Members offering short term loans also adhere to a rigorous code of conduct. FiSCA's Code of Conduct can be found by visiting www.fisca.org.

What is the current situation on Capitol Hill?

Several members in both houses of Congress have introduced legislation that would impact the ability of industry to offer small dollar credit by imposing artificially low interest rate caps on these products. Certain bills in Congress, such as Senator Durbin's S. 500, would cap the annual interest rate at 36%.

Why the 36% APR cap on PDA loans will ruin the industry

There are many critics of short-term, small dollar loans, or payday advances, who claim that capping at 36% the Annual Percentage Rate that can be charged on these products will help consumers while allowing the industry to continue offering the product. Nothing could be further from the truth. The reality is that a 36% cap will put much of the industry out of business. Why?

Discussing the fees associated with these products in terms of APR is very misleading. These products are typically offered over a two-week period, not over a year. A 36% APR means lenders only will be able to charge \$1.38 per \$100 loaned for two weeks. Such a rate of return will result in the industry losing money ... for two reasons.

First, operating costs are high, given the related overhead, labor, infrastructure and administrative costs associated with operating storefronts. Second, the rate of default on payday advances is higher than with other credit products. Remember, these are non-collateralized, personal loans. For these reasons, with a 36% APR companies will lose money and will stop offering the product.

While a 391% for a PDA (\$15 per \$100 loaned) may sound excessively profitable, it is not. This conclusion is shared by independent experts. For example, in "Payday Lending: Do Outrageous Prices Necessarily Mean Outrageous Profits?" Aaron Huckstep, a professor at the Fordham University School of Law concluded: "This study finds that **the industry's proffered justifications for high service fees, and by extension high APRs, may be justified by both**

high store expenses and high loan losses. In addition, this study finds that payday lender profit margins are less than half that of their mainstream lending counterparts.”

(If possible, replace and/or include the E&Y report)

Who uses payday advances?

- Working consumers who timely repay them when due more than 90% of the time, according to numerous state regulatory reports.
- They are typically between the ages of 25-44 years old.
- They have an average household income of more than \$40,000 a year.
- The majority of are high school graduates with some college education or a degree.
- All have a steady source of income and maintain active checking accounts.

Why do people take out payday advances?

- PDAs help customers bridge the unexpected need for short-term credit when other options are not available.
- Very often a PDA is less costly to the consumer than the other available options, such as incurring late fees, bouncing a check, utilizing overdraft protection or obtaining a credit card advance.
- Recent studies have proven that consumers who use PDAs as a tool to help meet their monetary obligations fare better financially than consumers who do not have PDAs as an option.

Payday advances are typically cheaper than other short-term credit options

Credit Option	\$100 Payday Advance (2 wk loan)	\$100 Overdraft Protection	Credit Card Late Fee on \$100 Bill	Late/Disconnect Fee on \$100 Utility Bill	\$100 Bounced Check NSF/Merchant
Fee	\$15.00	\$29.00 ¹	\$34.42 ²	\$46.16 ³	\$54.87 ⁴
APR	391%	756%	897.71%	1,203%	1,431%

How does a payday advance work?

- A borrower completes a simple application for a loan and typically is required to provide supporting documentation, including proof of regular income, a personal checking account and identification.
- If approved, a borrower reads and signs an agreement containing disclosures, including those required by the Truth in Lending Act, and writes a post-dated personal check, usually coinciding with the borrower’ next payday, for the amount of the advance plus a fee.
- The lender immediately advances the borrower funds, but holds the check until the agreed upon date.
- For example, a customer seeking to obtain a \$300 payday advance will write a check for \$345 that will be deposited by the PDA provider on a future agreed upon date. That check amount represents the \$300 principal plus the \$45 in fees associated with the PDA.
- The customer receives \$300 as an advance on the post-dated check.

¹ Bankrate.com, 2007 Courtesy Overdraft Study – based on average first overdraft charge

² “Credit Cards: Increased Complexity in Rates and Fees,” General Accountability Office, 2006.

³ 2006 CFSA Fee Survey.

⁴ Average NSF fee \$28.23 (Bankrate.com, 2007 Checking Study), based on average first NSF charge. Average merchant return check fee \$26.64 (2006 CFSA Fee survey.)