



The Facts About Payday Advance Services



Community Financial Services Association of America

Overview

The Community Financial Services Association of America (CFSA) was established in 1999 to help ensure consumer confidence in, and long-term success of, the payday advance industry—one of the fastest-growing financial service industries in the United States. Today, CFSA is comprised of 164 member companies, representing more than half of the estimated 22 thousand payday advance locations nationally.

CFSA's mission is to promote laws and regulations that protect consumers, while preserving their access to credit options, and to support and encourage responsible industry practices.

CFSA works aggressively at the local, state and national levels to educate legislators and regulators about the role of payday advance in the broader financial service arena. The majority of states have considered and enacted balanced and responsible legislation, with 37 states and the District of Columbia currently regulating payday advance services.

To help self-govern the membership and encourage responsible industry practices, CFSA introduced a set of mandatory "Best Practices" in early 2000. To be a member of CFSA, a payday advance provider must abide by these practices. CFSA's Best Practices cover areas such as full disclosure of transaction terms, compliance with applicable state and federal regulations, appropriate collection practices, encouraging responsible use of the service and special protections that address the unique circumstances of military personnel who choose to use a payday advance.

CFSA is also proud to support special initiatives designed to help member companies promote their customers' financial well being. The association's *CFSAccess* program includes financial literacy initiatives such as promoting the FDIC's *Money Smart* consumer education program through a partnership with the National Urban League. The association also has a partnership with PRBC, an innovative new credit reporting agency, allowing member companies' customers to build their credit history by voluntarily having their payday advance repayments reported.

Since its founding, CFSA has and will continue to demonstrate its member companies' commitment to listening to emerging concerns of consumers and policymakers and taking action to address their needs.



Best Practices for the Payday Advance Industry

CFSA Members must abide by the following Best Practices:

- 1. Full disclosure.** A member will comply with the disclosure requirements of the state in which the payday advance office is located and with federal disclosure requirements including the Federal Truth in Lending Act. A contract between a member and the customer must fully outline the terms of the payday advance transaction. Members agree to disclose the cost of the service fee both as a dollar amount and as an annual percentage rate ("APR").
- 2. Compliance.** A member will comply with all applicable laws. A member will not charge a fee or rate for a payday advance that is not authorized by state or federal law.
- 3. Truthful advertising.** A member will not advertise the payday advance service in any false, misleading, or deceptive manner, and will promote only the responsible use of the payday advance service. (effective 5/31/2007)
- 4. Encourage consumer responsibility.** A member will implement procedures to inform consumers of the intended use of the payday advance service. These procedures will include the placement of a "Customer Notice" on all marketing materials, including all television, print, radio and on-line advertising, direct mail and in-store promotional materials. (effective 5/31/2007)
- 5. Rollovers.** Members shall not allow customers to rollover a loan (the extension of an outstanding advance by payment of only a fee) unless expressly authorized by state law, but in such cases where authorized the member will limit rollovers to four (4) or the state limit, whichever is less.
- 6. Right to rescind.** A member will give its customers the right to rescind, at no cost, a payday advance transaction on or before the close of the following business day.
- 7. Appropriate collection practices.** A member must collect past due accounts in a professional, fair and lawful manner. A member will not use unlawful threats, intimidation, or harassment to collect accounts. CFSA believes that the collection limitations contained in the Fair Debt Collection Practices Act (FDCPA) should guide a member's practice in this area.
- 8. No criminal action.** A member will not threaten or pursue criminal action against a customer as a result of the customer's check being returned unpaid or the customer's account not being paid.
- 9. Enforcement.** A member will participate in self-policing of the industry. A member will be expected to report violations of these Best Practices to CFSA, which will investigate the matter and take appropriate action. Each member company agrees to maintain and post its own toll-free consumer hotline number in each of its outlets.
- 10. Support balanced legislation.** A member will work with state legislators and regulators to support responsible legislation of the payday advance industry that incorporates these Best Practices.
- 11. Extended Payment Plan.** A member will comply with a separate code of Best Practices for Extended Payment Plans, which provides customers who are unable to repay a loan according to their original contract, the option of repaying the loan over a longer period of time at no additional charge. A customer shall be allowed to utilize an Extended Payment Plan at least once in a 12-month period. A member will adequately disclose the availability of the Extended Payment Plan to its customers. (effective 7/31/ 2007)
- 12. Military.** A member will comply with a separate code of Military Best Practices that addresses the unique circumstances of active duty military customers. These special consumer protections include, among others: a prohibition on the garnishment of military wages or salaries and on contacting the military chain of command to collect payment; and the establishment of financial literacy initiatives that will benefit service men and women.
- 13. Internet lending.** A member that offers payday advances through the Internet shall be licensed in each state where its payday advance customers reside and shall comply with the disclosure, rollover, rate, and other requirements imposed by each such state, unless such state does not require the lender to be licensed or to comply with such provisions, or the state licensing requirements and other applicable laws are preempted by federal law.
- 14. Display of the CFSA Membership Seal.** A member company shall prominently display the CFSA Membership Seal in all stores to alert customers to the store's affiliation with the association and adherence to the association's Best Practices.



Payday Advance: Market Demand

Consumer Need

- Payday advance fills a need not met by traditional financial institutions
- It's a convenient, less costly and often more desirable option for short-term, unsecured credit.

Market Alternatives

- **Bounced check and overdraft protection fees**

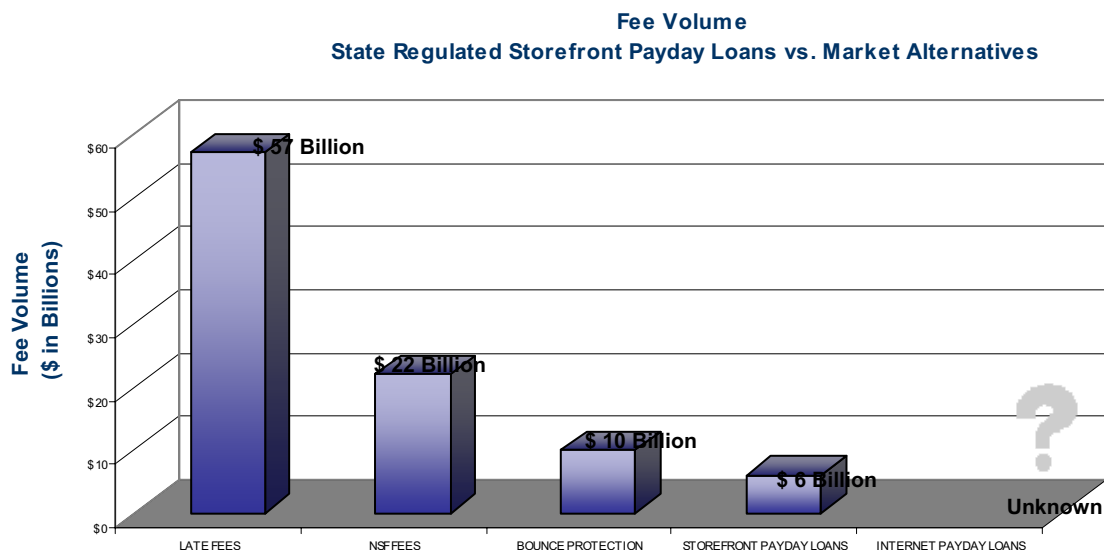
- Consumers pay an estimated \$22 billion in NSF fees to banks and credit unions (*Contrasting Payday Loans to Bounced Check Fees*, Consumer Credit Research Foundation, Thomas E. Lehman, Ph.D., 2005). Banks also collect an estimated \$10.3 billion annually for overdraft protection services (*Overdraft Fees Can Overwhelm*, Washington Post, June 26, 2005).
- **(Late payment penalties (landlords, utility companies, credit card companies, etc.)** An estimated \$57 billion in late bill payment fees were collected by businesses in 2003, more than 140 percent of the total estimated payday lending volume in the United States (*Sizing NSF-Related Fees*, BAI Banking Strategies Magazine, Bill Stoneman, January-February, 2005). Credit card late fee penalties totaled over \$11 billion in 2005 (CreditCards.com, November 2006).

- **Internet payday lending**

- With a growing but unmeasured market size, Internet payday lending is an “explosive” market that is creating increasing problems for state regulators and enforcement officials, says Bankrate.com (*Online Payday Loans: Borrower Beware*, September 12, 2005). Unregulated off-shore lenders have access to consumers’ bank accounts and charge up to \$30 per \$100 borrowed.

- **Impact of Elimination**

Removing the choice of regulated storefront payday lending, the smallest segment of the market, will only force consumers to more expensive, less desirable and unregulated alternatives.

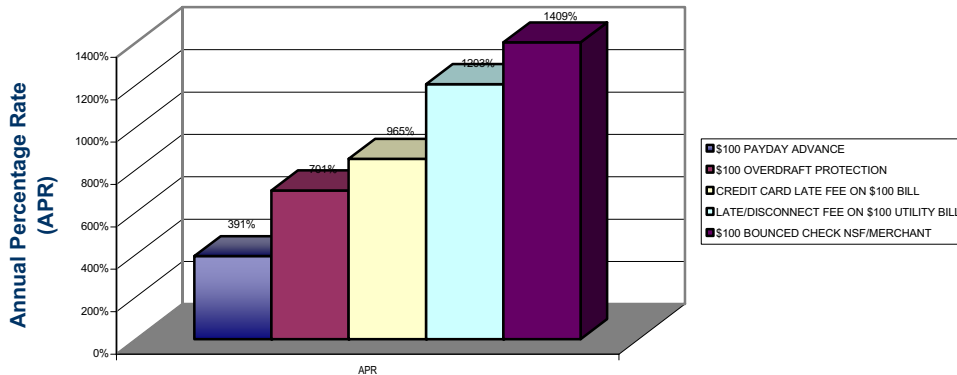




Payday Advance: A Cost Comparison

Payday advance fees are lower than many of consumers' alternatives, even when expressed as an annual percentage rate (APR).

APR Comparisons On Payday Advance Alternatives (14-Day Term)



CREDIT ALTERNATIVE	\$100 PAYDAY ADVANCE	\$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	\$26.90	\$37.00	\$46.16	\$54.04
APR	391%	701%	965%	1203%	1409%

Source: Avg. NSF fee \$27.40 (Bankrate.com, Fall 2006); Avg. merchant return check fee \$26.64 (2006 CFSA Fee Survey); Avg. utility late and reconnect fee (2006 CFSA Fee Survey); Avg. credit card late fee (Credit cards: Increased Complexity in Rates and Fees, Government Accountability Office, 2006); Avg. overdraft protection fee (Bankrate.com, 2005); Typical payday advance Fee (CFSA)

Consumer groups and academic researchers comment on the cost of payday advance versus its alternatives:

“We find that fixed operating costs and loan losses justify a large part of the high APR charged on payday advance loans...These operating costs lie in the range of [payday] advance fees, suggesting that payday loans may not necessarily yield extraordinary profits.”—Payday Lending: Do the Costs Justify the Price, Center for Financial Research, Federal Deposit Insurance Corporation, 2005

“Critics also contend that [overdraft] bounce protection fees, as high as \$37 per transaction, are little more than high-priced credit. ‘If a bank lends you \$100 and charges you a \$20 fee—and then you pay the money back in two weeks—that’s an annualized interest rate of 520%,’ notes Jean Ann Fox, director for consumer protection at the Consumer Federation of America in Washington. ‘It’s worse than a payday loan’.” –Business Week, May 2, 2005

“Unlike payday lending programs, the extraordinarily high APRs in fee-based overdraft programs are never disclosed as such, and none of the other consumer protections are provided. Moreover, fee-based overdraft programs are aimed at the very same customers that payday lenders are seeking...and the costs rival or exceed those of payday lending.”—Comment letter to Board of Governors of the Federal Reserve System from 90 consumer group organizational signators, January 27, 2003

“Interviews and industry survey indicate that payday loan customers do make a cost analysis in comparing the price of a payday loan with the alternative costs of bouncing a check and/or incurring late fees...When used on a recurring basis for small amounts, the annualized percentage rate for fee-based bounce protection far exceeds the APRs associated with payday loans.”—Low-Cost Payday Loans: Opportunities and Obstacles, Annie Casey Foundation Report, June 2005.

“Courtesy pay is not marketed as an alternative to a payday loan, but it serves a similar function when used as credit. Credit unions charge fees ranging from \$15 to \$35 to cover an overdraft.”—Credit Union Payday Loan Alternatives, National Association of Community Credit Unions, December 2005.



Why Payday Advance Is Not Predatory Lending

The term “predatory lending” has received a lot of attention recently; but often its definition is unclear and the distinction between predatory lending and subprime lending is blurred. This vagueness of the term has been used to portray certain financial services inaccurately. Payday advance has been the target of just such an attempt, and it is clearly unwarranted.

In general, predatory lending is defined as a harmful form of subprime lending in which consumers are pressured to take loans they don’t need, putting valuable assets at risk. Federal Reserve Governor Edward Gramlich said in an address to the Texas Association of Bank Counsel in South Padre Island, Texas, October 9, 2003 that predatory lending typically involves at least one, and perhaps all three, of the elements listed below. **Not one** of these elements applies to payday advance and here’s why.

Three Elements of Predatory Lending, according to Federal Reserve Governor Gramlich

- Making unaffordable loans based on the **assets** of the borrower rather than on the borrower’s ability to repay an obligation.
- Inducing a borrower to refinance a loan repeatedly in order to charge high points and fees each time the loan is refinanced (“loan flipping”).
- Engaging in fraud or deception to conceal the true nature of the loan obligation from an unsuspecting or unsophisticated borrower.

Why Payday Advance is NOT Predatory Lending

- Payday advance is a small denomination, un-collateralized, unsecured short-term financial transaction based on the borrower’s steady income.
- Most state laws prohibit the extension of a payday advance by paying an additional fee (rollover). CFSA members do not encourage rollovers and, in states where rollovers are permitted, limit them to 4 or the state limit, whichever is less.
- The cost of a payday advance is fully disclosed to customers on signage and in disclosure agreements. It is a one-time, flat fee and there are no hidden charges, balloon payments or accruing interest. CFSA members also provide an educational brochure emphasizing responsible use of the product and offer a free right of rescission should the customer change his mind.

Payday advances are small, short-term cash advances with simple terms and fees. Thirty-seven states and the District of Columbia have laws and/or regulations governing this product. The industry is dedicated to working with interested parties to ensure that consumers use the service appropriately. Members of the Community Financial Services Association of America (CFSA), the national trade association of payday advance, believe that payday lending should be conducted in a safe and responsible manner and with appropriate disclosures and strong consumer protections. CFSA’s Best Practices, which apply to all CFSA members, are intended to ensure such conduct. CFSA members must abide by the following Best Practices:

- A 24-hour, cost-free customer right to rescind any transaction.
- Prohibition of or limitation on rollovers.
- Full disclosure of transaction terms.
- Encourage responsible use of the service.
- Appropriate collection practices.
- No criminal action against customers.
- Compliance with state and federal regulations.
- Truthful advertising.
- Enforcement of Best Practices.



Payday Advance State Legislation

A Regulated Alternative to Unregulated Internet Lenders

While there is nothing inherently illegal or unethical about Internet payday lending, without a doubt, there is tremendous room for consumer abuse. Following applicable law, Internet lenders can deliver convenient and responsible payday loans. But all too often, unscrupulous lenders hide behind sophisticated Web sites, delivering nothing but trouble to unsuspecting consumers.

More and more consumers are getting payday loans over the Internet.

Consumer demand for small denomination, short-term credit is growing.

- Industry analysts estimate \$40 billion in payday loan volume nationally, from traditional storefront locations.
- Internet search engines identify about 3,000 Web sites delivering payday loans online, either directly to the consumer or by generating leads for Internet lenders.

Responsible and balanced state payday loan laws is the strongest deterrent against unregulated Internet lending.

One national Internet lender has revealed that the company receives five to ten times as many payday loan applications from unregulated states versus those with state regulation.

- *With access to a local payday lender, consumers appear to be less likely to take risks with faceless strangers for their short-term financial needs.*

State regulation that strikes a balance between providing strong protections for consumers and enabling reputable lenders to profitably set up local storefronts may reduce consumer dependence on unregulated cyberspace lenders.

- A majority of the 37 states that regulate payday lending cap the service fee below that of the typical Internet payday loan.
- Regulated payday lenders must comply with the Truth in Lending law and provide full and clear disclosure of loan terms and cost.
- Most state laws prohibit rollovers and none make the renewals automatic, as many online lenders do.
- Traditional storefront payday lenders are established businesses with personal contact between them and their customers, while Internet lenders are more often unknown entities, with the only contact being direct access to customers' bank accounts.
- Regulated payday lenders have privacy policies, which are disclosed to consumers.
- State-regulated payday lenders are licensed by the state and easily accessible to customers for personal service, as well as for dispute resolution.

Evidence mounts that consumers are susceptible to unscrupulous and illegal practices of many Internet lenders who do not comply with applicable laws.

A consumer advocate's survey of online payday lenders, media reports and information from some state regulators reveal substantial problems with Internet payday lending.

- **Fees are high and disclosures inadequate.**
 - The most frequently posted finance charge of surveyed lenders was \$25 per \$100 borrowed, the next most frequent was \$30 per hundred.
 - Only 57% posted the finance charge and almost never in a conspicuous place.
 - Just over a third (38%) disclosed annual percentage rates (APR) before customers had to complete the application process.
 - Many lenders automatically renew the payday loans, a practice typically hidden in the small print.
- **Consumers are exposed to privacy and security risks.**
 - Internet payday lenders require a tremendous amount of personal information, including bank account numbers, Social Security number, driver's license number, and even mother's maiden name, along with customer's name, address and employment information.
 - Personal data are transmitted to lenders over web links, many of which may be unsecure.
 - Lenders have access to consumers' bank accounts, so they can electronically deposit loan proceeds and withdraw loan payments, with no personal contact between the two parties.
 - Some regulators say consumers can have a difficult time stopping lenders from taking money out of their bank accounts.
- **Online lenders are unknown, faceless entities, often leaving consumers with no recourse.**
 - Difficulties in identifying, locating or communicating with lenders make it difficult to resolve disputes.
 - Some lenders are licensed in their home states, others hide behind anonymous domain registrations or are located outside of the U.S.
 - There is no national association representing online payday lenders.
- **There are questions concerning applicable law and regulatory jurisdiction for online payday lenders.**
 - Many state officials are trying to take action, but are having problems locating lenders.
 - A large number of lenders are located offshore and out of reach of American laws.



Payday Advance and the Military

The facts do not support the claim that payday advance companies target the military

Research confirms that military personnel represent a small percentage of payday advance customers nationally

- A 2005 poll conducted by one of the nation's leading pollsters, Penn, Schoen & Berland Associates, found that only 3.69% of active-duty military personnel have used a payday advance in the last five years, only 1.18% had an advance outstanding
 - The nationally representative sample interviewed 1,002 members of the U.S. Armed Forces, across all branches of service
 - With an active duty military population of 1.4 million, this incidence rate translates into 51,660 military personnel who have used a payday advance in the last five years and 16,520 with an advance outstanding
- New poll results discredit widely publicized and unsubstantiated claims that military personnel are heavy users of the payday advance service
 - Poll also confirms previous findings of payday advance customer surveys and individual company records that reported a small percentage of the industry's customer base as military

The payday advance customer demographic is extremely broad— not dominated by any population segment

- The service offers a small, unsecured cash advance to those needing help between paydays
- Research consistently confirms that customers are middle-income, educated young families, many of whom have not accumulated assets or a credit history—a large and diverse audience

The misperception that military are heavy consumers of payday advance is rooted in confusion among product offerings in the fringe financial services market

- Many people confuse payday advance stores with check cashing stores
 - When check cashers locate near military bases, it's primarily because they cash government checks, sell money orders, wire money and exchange currency—services often used by military personnel
- Mono-line payday advance stores (those businesses offering only payday advance)
 - Are typically located in suburban shopping centers anchored by national/regional retailers—not usually near the base gates—and serve the credit needs of entire surrounding communities

Even though the military represent a small percentage of CFSA member companies' customers, the association has responded to their needs with special programs and practices

- In March '03 CFSA adopted a resolution urging members to consider actions addressing the special needs of military customers during war
 - Companies responded in 5,000+ locations, with programs going beyond those required by the *Soldiers' and Sailors' Civil Relief Act*, to provide additional accommodations for our troops
 - National program recognition was awarded to First American Cash Advance, which received a bronze eagle during the American Legion's 85th National Convention, and to Check Into Cash, which received a National Corporate Award from the Veterans of Foreign Wars

- CFSA also established a toll-free hotline to help military customers get questions resolved quickly
In 2004 CFSA enhanced its mandatory *Best Practices* member standards to include special provisions for active duty military payday advance customers
- Under advisement of its Advisory Council on Military Affairs, a panel of retired military officers and senior noncommissioned officers, CFSA adopted *Military Best Practices*, establishing protections and information resources specific to the military
 - Provisions include: prohibition on the garnishment of military wages or salaries and on contacting the military chain of command to collect payment; deferral of collection activity against a military customer deployed to combat or national guardsman or reservist called to active duty; and efforts to strengthen the financial knowledge of military members

Federal Reserve Bank of New York Staff Report: Payday loans do not fit our definition of “predatory”.

A new study, “*Defining and Detecting Predatory Lending*,” by Donald P. Morgan, Research Officer, Federal Reserve Bank of New York, concludes that payday loans are not a “welfare reducing” form of credit. To the contrary, the author suggests that payday lenders enhance the welfare of households by increasing the supply of credit.

Noting the difficulty in defining “predatory,” the author sets out to distinguish predatory lending from “the kind that helps households maintain consumption even as their incomes fluctuate.” He examined differences in household debt and delinquency across states that allow payday lending and those that do not and compared the change in those differences before and after the advent of payday lending. Particular attention was paid to households that are generally perceived as more vulnerable to predation (those with income uncertainty or less education).

Noted in the report:

Payday loans are not welfare reducing, or “predatory”

“We define predatory lending as a welfare reducing provision of credit.”

“Our findings seem mostly inconsistent with the hypothesis that payday lenders prey on, i.e., lower the welfare of, households with uncertain income or households with less education.”

“On the whole, our results seem consistent with the hypothesis that payday lending represents a legitimate increase in the supply of credit, not a contrived increase in credit demand.”

Payday loans may enhance the welfare of households

“...[credit]delinquency rates were marginally lower for risky households in states with unlimited payday loans.”

“Households with uncertain income who live in states with unlimited payday loans are less likely to have missed a debt payment over the previous year...consistent with claims by defenders of payday lending that some households borrow from payday lenders to avoid missing other payments on debt.”

“Those types of households who happen to live in states that allow unlimited payday loans are less likely to report being turned down for credit, but are not more likely, by and large, to report higher debt levels...”

Price does not make payday loans “predatory”; limiting access raises prices

“Higher prices are neither necessary nor sufficient to conclude that a certain class of credit is predatory.”

“We find somewhat lower payday prices in cities with more payday stores per capita, consistent with the hypothesis that competition limits payday loan prices.”

“The problem of high prices may reflect too few payday lenders, rather than too many.”

“Before payday lending...very small, short-term loans may not have been worthwhile for banks. Payday lending technology may have lowered those fixed costs, thus increasing the supply of credit...That version of the genesis of payday lending suggests the payday innovation was welfare improving, not predatory.”



Payday Advance: Fact vs. Fiction

Fiction: They prey on poor, uneducated and older consumers

Fact: Payday advance customers represent the heart of the working middle class

- Majority have incomes between \$25,000 and \$50,000
- 68% are under 45 years old; only 3.5% are 65 or older
- 94% have a high school diploma or better; 56% have some college or a degree
- 42% own their own homes
- 57% have major credit cards; 49% are credit union members
- 100% have a steady income and an active checking account, both required for an advance

Fiction: They target military personnel

Fact: The military represent a small percentage of payday advance customers

- A 2005 poll conducted by one of the nation's leading pollsters (Penn, Schoen & Berland Associates) found that only 3.69% of active duty military personnel have used a payday advance in the last five years, only 1.18% had an advance outstanding
 - With an active duty military population of 1.4 million, this incidence rate translates into 51,660 military personnel who have used a payday advance in the last five years and 16,520 with an advance outstanding

Fiction: They charge outrageous rates

Fact: Payday advance fees typically cost less than customers' alternatives

- Bank/merchant fees on one bounced check can cost three times that of a \$100 advance
- Payday advance APRs are often lower than customers' alternatives, even on same 2-week term
 - \$100 payday advance with \$15 fee = 391% APR
 - \$100 bounced check with \$54 NSF & merchant fees = 1,409% APR
 - \$100 credit card balance with \$37 late fee = 965% APR
 - \$100 check with \$27 overdraft privilege fee = 701% APR
 - \$100 utility bill with \$46 late/reconnect fee = 1,203% APR
- 96% of customers are aware of the finance charge; 78% recalled it being disclosed as an APR

Fiction: They put customers into a cycle of debt

Fact: Most customers use payday advance responsibly

- 66% use payday advance to cover unexpected expenses or temporary income reduction
- Research & regulators confirm that most use payday advance moderately
 - The Credit Research Center at Georgetown University reported more than half use payday advance 6 or fewer times annually; 78% use it between once a year and about once a month
 - A 2005 study by the FDIC's Center for Financial Research found that 72% of customers took out less than 12 advances per year, and the average was 7
 - State regulators consistently report 70-80% use the service between once a year and about once a month

Fiction: They take advantage of unsuspecting customers

Fact: Across the country customers overwhelmingly appreciate the service

- Millions choose payday advance as a dignified, discreet, and often less costly solution for cash flow problems, without asking family for money or risking personal items as collateral
- 70% choose payday advance for convenience; only 6% because there was no alternative
- 92% of customers say payday advance is a useful service; only 12% were dissatisfied
- State regulators report very few complaints out of millions of transactions