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Payday Lending: In Search of a Local Alternative

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March 2010

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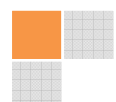
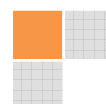


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Executive Summary

This report summarizes a small independent research study conducted to gain a deeper understanding of payday loans from multiple perspectives and to explore the need for a local alternative to payday lending. A payday loan is a small short term loan guaranteed with a post-dated cheque dated for the borrower's next payday (typically \$100-\$500 borrowed for approximately 10 days). Using Waterloo Region as a case study, the Centre for Community Based Research conducted this study, in partnership with the Wellesley Institute and with guidance from an advisory committee. Using a Participatory Action Research approach, **this study confirmed the need to develop a comprehensive local community banking project as a way to provide individuals with support and access to financial services, with broader application for other jurisdictions.**

Key Findings

Borrowers' incomes: Approximately 50% of borrowers surveyed work full-time, and almost 25% receive Ontario Disability Support Program (ODSP).

Borrowers' motivations and satisfaction: Borrowers of payday loans usually use the money for essential needs and debt; people living on lower incomes (under \$30,000) are more likely to borrow payday loans

- Borrowers are satisfied with the convenient location and hours and no minimum credit rating, as well as friendly, quick, non-judgmental services
- Borrowers are dissatisfied with the high cost of borrowing, short payback period, lack of full disclosure about that high cost, stress associated with debt, and the collection practices

Evidence of need for an alternative: payday lending is a symptom of wider social problems including chronic debt, poverty, etc.

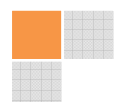
- Overwhelming majority of key informants, borrowers interviewed and survey participants indicated a need for an alternative to payday loan facilities

Viable model for a local alternative to payday lending: based on the research data, a holistic comprehensive approach to a community banking project would work best in Waterloo Region, rather than an isolated payday loan alternative service.

- A literature review of existing payday lending alternatives revealed several models in North America, Australia, and the U.K. One Canadian example, located in Winnipeg, takes a similar approach to the holistic model suggested by the data.

Recommendations for next steps

1. Disseminate final research report using web-based approaches, including social media & website
2. Create a separate practical document for sharing Waterloo Region-focused aspects
3. Explore potential next steps for developing a collaborative microfinance project in Waterloo Region.
 - a. Large community forum
 - b. Small meeting of potential collaborators
 - c. Engage with each stakeholder group: financial institutions; community organizations; potential funding sources; borrowers; governments
4. Communicate policy recommendations to appropriate bodies



Summary of Policy Recommendations

The following summarizes a number of provincial and federal policy implications that emerged from the data. These recommendations are further described in more detail in the main body of the report.

Provincial policy area recommendations

ENFORCEMENT: That the Ministry of Consumer Services demonstrate their enforcement of current regulations under the Ontario Payday Loans Act with particular attention to:

- ENSURE that only registered lenders are supplying payday loans;
- ENSURE that all payday lenders have educational materials available on-site
- IMPLEMENT the Ontario Payday Lending Education Fund

CONSUMER PROTECTION: That the Ministry of Consumer Services Consumer Protection Branch increase efforts to ensure public awareness of interest rates for payday loans:

- FEATURE educational materials regarding payday loans on their website
- PROVIDE public service announcements in mainstream media

FINANCIAL LITERACY: That financial literacy curriculum for youth and adults in Ontario include the learning goal of increased awareness of payday lending, its high interest rates and short pay-back periods.

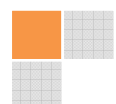
POVERTY REDUCTION STRATEGY: That the Ministry of Children and Youth Services clarify to the public how the Community Opportunities Fund is being spent. According to Ontario's Poverty Reduction Strategy, \$5 million is invested annually in a Community Opportunities Fund.

Federal policy areas

NATIONAL STRATEGY: That the Task Force on Financial Literacy explore microfinance incentives including:

- Micro-loan funding
- Asset-building programs
- Credit restoration opportunities

FINANCIAL SERVICES FOR PEOPLE WITH LOW-INCOMES: That the Financial Consumer Agency of Canada extend increased access to financial services for people with low-incomes.



Introduction

This report summarizes the findings of a research study conducted in Waterloo Region, Ontario by the Centre for Community Based Research (CCBR). The purpose of this research study was to look at the nature of existing payday lending services from multiple perspectives and to explore the need for and possibility of a 'made-in-Waterloo Region' alternative to payday lending. The project idea was initiated by staff at CCBR in consultation with community partners. Wellesley Institute (www.wellesleyinstitute.com) joined this partnership, carried out an environmental scan of national and international literature on payday lending (see Appendix), initiated connections with a local bank (Goodwill Industries, London, Ontario) and provided the funds to carry out the research.

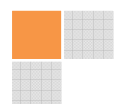
The report is intended for a diverse audience of individuals and organizations interested in the topic of payday lending and the potential to develop alternatives. It is meant to be a source of information in general, and more specifically, it can be a launching pad for forming a local alternative community banking project. It is relevant to the financial sector, social services sector, public sector, as well as borrowers of payday loans, academics, activists, and educators. The report is structured so that it begins with an overview of the payday lending industry, a description of the research study, and then a report of the findings, which are organized according to the main research questions. The final section of the report is recommendations for next steps.

Payday lending 101

A payday loan, also called a payday advance or pay cheque advance, is a small, short term unsecured loan to meet the borrower's expenses until his or her next payday. The borrower guarantees repayment with a post-dated cheque or pre-authorized debit. Typically, the loan amount ranges from \$100 to \$400 and it is usually due 10 to 14 days later. The average loan amount is \$280 borrowed for a period of 10 days (Canadian Payday Loan Association, 2009). Lenders typically require borrowers to prove three months of continuous employment, produce proof of address, and have an active chequing account. No credit cheque is performed. The interest rate charged is much higher than those charged by banks or credit cards. The average loan interest rate can range from 390% – 780% APR (annual percentage of rate) (Americans for Fairness in Lending, 2010), exorbitantly higher than the 60% anti-usury clause in the Criminal Code of Canada.

The proponents of payday lending, such as the Canadian Payday Loan Association, argue that payday loan stores provide a service which is not available from other sources. They establish that many credit unions have attempted to offer similar products, with lower interest rates, but have been unable to do so without government grants or subsidies. A staff report released by the Federal Reserve Bank of New York concluded that payday loans should not be categorized as 'predatory' since they may improve household welfare. Moreover, they further assert, that payday stores extend credit to 'risky' customers with high chances of default.

However, the critics, including the Public Interest Advocacy Centre, term this practice as exploitative, taking advantage of people's financial hardships. They say that low-income borrowers are more likely to be trapped in a 'debt cycle' because the short pay-back period makes it difficult to pay back the entire amount owing. Statistics compiled by the Centre for Responsible Lending (2009) show that the majority of the industry's profit comes from repeat borrowers who are unable to repay loans on the due date and instead repeatedly borrow, paying fees each time.



Payday lending in Canada

Starting in the 1990s, payday loans became increasingly popular in Canada. In the same time period, traditional banks had begun tightening restrictions on lending small amounts of money (under \$5000). Approximately 1,350 stores operate in Canada, with over 700 in Ontario (Robinson, 2006, p. 11). Over 40 storefronts operate in Waterloo Region (population 533 700).

The payday lending industry supplies short-term credit in small amounts to meet the demand of people who are not served by traditional banks. Ultimately, this trend in the financial sector encourages and fosters a two-tiered banking system: at one level, we have a highly regulated service, strictly monitored by the Financial Consumer Agency of Canada (Financial Consumer Agency, 2010) for the majority of residents, and at another level, we have a loosely (and very recently) regulated service, with unspecified monitoring by provincial ministries offered at a vastly higher cost for those with limited resources or who have a poor credit history.

Up until 2007, payday lending was technically not legal in Canada, because fees exceeded anti-usury law, but the industry flourished nevertheless. The government was aware of the issue and deliberated how to respond to this dilemma. Before any legislative changes, a class-action law suit against one of the largest providers of payday lenders was launched and settled out of court. In the spring of 2007, the Canadian government amended the anti-usury section of the Criminal Code of Canada, section 347, to exempt payday lenders from the maximum 60 % Annual Percentage Rate and to give provinces and territories the authority to implement regulations independently (Ministry of Government Services, 2009). Since that time, Ontario's Payday Loan Act was passed in 2008 and most elements were implemented during 2009 (Ministry of Consumer Services, 2010). The main elements of this Act are as follows:

- Payday lenders and loan brokers are required to be licensed.
- "Rollover" loans are prohibited.
- Payday loan borrowers have a two-day "cooling off" period to cancel a loan with no reason without incurring a penalty.
- An Ontario Payday Lending Education Fund will be established, paid for by licensees.
- Maximum total cost for borrowing a payday loan in Ontario is \$21 per \$100 borrowed.

It is early yet to know how these regulations will affect the industry, but already these regulations are seen by critics as quite lenient. Some have speculated that increased, even stricter regulations will be needed, since the industry representatives themselves are pleased with the current rules. The Canadian Payday Loan Association, a national body representing most of the established lenders in the industry, has been advocating for regulation of payday lending since they started.

Overview of the study

Payday lending has been vastly under-studied in Canada, with the exception of the area of fee structures (Robinson, 2007). The first national Statistics Canada study on the issue was the Survey of Financial Security. It showed that "young families were three times more likely to have used payday loans" and that "low-income families (after tax) were fully twice as likely as those not in a low income bracket to have used payday loans-4.6% compared with 2.3%" (Pyper, 2007). This study is a start in understanding the demographic information for who uses payday loans, but a gap remains in understanding why they use them, and what alternative would work for them.



Purpose and research questions

The overall purpose of this research study was to look at the existing practice of payday lending and to explore the need for a local solution as an alternative. Using Waterloo Region as a case study, six main research questions were addressed by the study:

1. What is the nature of borrowers' experiences with payday lending?
2. What are the motivations and levels of satisfaction of payday loan borrowers in the Waterloo Region?
3. Is there a need for an alternative to payday lending for low income people in Waterloo Region?
4. What are existing alternatives to payday lending across North America and globally?
5. Are there potential partner(s) interested to explore implementing a viable social enterprise venture based on needs assessment?
6. What are the policy implications of this study?

About the research partners

To understand the context of this research project, it is important to know a little bit about the organizations behind it.

Research team

The Centre for Community Based Research (CCBR) is an independent, non-profit organization focused on strengthening communities through social research. CCBR believes in the power of knowledge to impact positive social change. We are passionate about bringing people together to use knowledge to provide real and innovative solutions to community needs. Our approach to research is participatory and action-oriented in a way that mobilizes people to participate as full and equal members of society. It is in the spirit of our beliefs and passion that we conducted this research in partnership with the Wellesley Institute. Project researchers were Sarah Marsh, Yasir Dildar, Rich Janzen, and Brian Barlett.

Research partner and funder

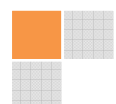
Wellesley Institute (WI) is a Toronto-based non-profit and non-partisan research and policy institute focused on developing research and community-based policy solutions to the problems of urban health and health disparities. WI works in collaborations and partnerships locally, nationally and internationally to support social and policy change to address the impact of the social determinants of health. Project contact and collaborators were Nimira Lalani and Michael Shapcott.

Advisory Committee

A six member advisory committee guided the research process. Committee members gave input into all data collection tools, sampling criteria, participant recruitment, analysis interpretation, and the dissemination of findings. Members reflected diverse stakeholder groups including: social service agencies, an anti-poverty initiative, a financial institution, and the partner organization: Wellesley Institute.

Research approach and methods

Consistent with other CCBR-led studies, this research used a mixed-methods participatory action research (PAR) approach. The study was conducted by a four member research team, including an advisor, two researchers, and a community researcher. Combined, these members bring content expertise (i.e. economic security), research expertise, and awareness of the local community context.



The project utilized several ways of gathering information involving different stakeholder perspectives. Use of a series of methods enhances triangulation of evaluation results and increases the rigour of the findings. Main methods included:

Payday Loan Borrowers Interviews: The research study explored the diverse motivations or reasons for using payday loan facilities by conducting 11 individual interviews with selected loan borrowers. The loan borrowers also provided their feedback about their level of satisfaction with existing services and suggested key features of an alternative. Participants were recruited with posters located in community locations throughout the region, and selection was based on ensuring representation from Kitchener, Waterloo, and Cambridge, as well as gender and income source. All of the interviews were audio-recorded and transcribed with participants' permission.

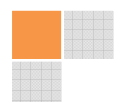
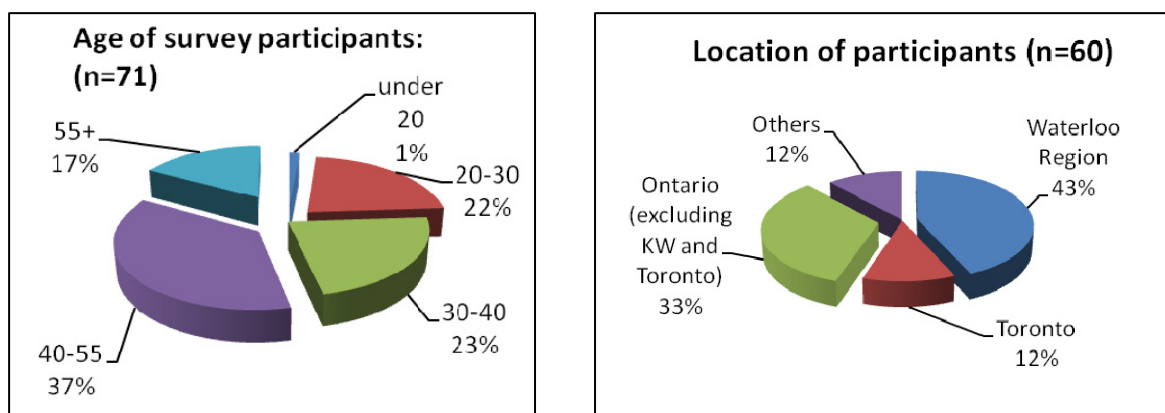
Interviewees represented three main urban areas of Waterloo Region: Kitchener, Waterloo, & Cambridge; both genders were represented (5 men; 6 women); the ages ranged from 20-55+; and sources of income included ODSP; full-time work; and social assistance.

Payday Loan Borrower Web Survey: A web-based survey was conducted to capture a wider range of borrower responses than could be gained through qualitative interviews regarding their motivations and levels of satisfaction in borrowing payday loans and to learn about their perspectives on a potential alternative. The survey was widely promoted to the public using web-based social media, emails, posters, and a website with a view to reaching borrowers of payday loans in Waterloo Region, Toronto, and other parts of Ontario and Canada. Targeted groups included the advisory committee, partner contacts at Wellesley Institute and CCBR, and service users at several community locations throughout Waterloo Region.

119 people started the survey and 76 completed it. All survey participants provided informed consent and no questions were mandatory, so some participants skipped a number of questions.

Certain demographic information was gathered from respondents, including their age ranges and place of residence. A broad range of ages was reported in the survey, the largest percentage being from the 40-55 years of age range. The percentage of borrowers in the 55+ age group (17%) responding to the survey is considerably lower than the percentage of adults in that age group in Ontario (30%) (Statistics Canada, 2006). The percentage of borrowers 40-55 years old is somewhat higher than the general population, and the percentage of borrowers aged 20-30 and 30-40 are, to a small degree, higher than the general Ontario population of adults (Statistics Canada, 2006).

43% of participants were from the Waterloo Region, 12% from Toronto, 33 % from other Ontario areas, and 12% of people either chose not to respond or they were from outside of the province.



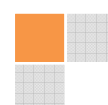
Key informant interviews: Key informant interviews were conducted to learn if there is a need for a local alternative, and to explore with potential partners the level of interest in the possibility of implementing a local initiative. A total of 10 key informants were identified in consultation with the Advisory Committee to be interviewed. Selection criteria required that all participants be familiar with payday lending and its impact in the community. Participants were selected to ensure a range of involvement with this issue, a mix of individuals from within and outside of Waterloo Region, and representatives from the following areas of expertise: financial services (n=3), human services, especially those dealing with economic security (n=4), academic or content experts (n=3), and funders with potential interest in economic security (n=1). All of the interviews were audio-recorded and transcribed with participants' permission.

Literature Review: The first phase of the study included a comprehensive national and international review of recent literature on payday lending. The focus was primarily on finding existing practices and alternatives to payday loans. Wellesley Institute also completed an Environmental Scan. Both the summary of literature findings and the environmental scan are attached in the Appendix.

Community Meeting: Toward the end of the study, diverse community stakeholders were invited to a meeting where they had opportunities to respond to and verify or clarify preliminary results, and to provide insights to add to the study findings.

Table : Research Methods

Method	Description	Involvement
<i>Individual Interviews with Borrowers</i>	11 individual interviews were held with selected loan borrowers. Borrower motivations, satisfactions, and opinions about alternatives were addressed in this method.	Payday loan borrowers (n=11)
<i>Borrower Web Survey</i>	A web survey was open to the public during January 2010. This method addressed the research questions about borrower motivations, satisfactions, and opinions about alternatives.	Individuals who had borrowing experience and/or knowledge of payday lending (n=76)
<i>Key Informant interviews</i>	Face-to-face and telephone interviews were held with key informants using a semi-structured interview protocol. The primary research questions addressed were about alternatives and potential partners for a payday lending alternative and policy implications.	Individuals from a range of settings, including: financial institutions; community non-profits; government; academic (n=10)
<i>Literature Review</i>	A national and international recent literature on payday lending was reviewed. The focus was primarily on finding documentation of existing practices and alternatives to payday loans as well as policy implications.	Wellesley Institute literature review contributions; academic articles; reports; contributions to payday lending listserv.
<i>Community meeting</i>	Preliminary results were shared at a meeting of 30 diverse community stakeholders. Through small and large group discussions, meeting participants contributed verification of preliminary findings and additional valuable insights to the study.	30 interested community members, including outreach workers, business owners, individuals from community non-profit organizations, foundations, and financial institutions, among others.



Data analysis

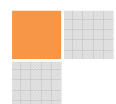
Data analysis was carried out collaboratively by the research team to ensure that study themes were identified and confirmed by multiple team members. Furthermore, research findings were presented to the advisory committee for further verification. The web survey data was analyzed through graphs (using MS Excel) while the qualitative data from key informant interviews and individual interviews was transcribed and analyzed using content analysis based on five main research questions.

Limitations

It is important to highlight the fact that the web survey results are not representative of all payday loan borrowers. The survey was not based on a random sample and the sample size was relatively small, so we cannot generalize the study findings for mainstream payday loan borrowers.

Study scope

The focus of this study is on existing payday lending practices and the potential for an alternative, which are particular aspects of the wider dilemma of lack of access to financial services for vulnerable and low-income populations. While the scope of our inquiry did not extend to most aspects of financial exclusion for low income and marginalized people (for example the unbanked), all data sources (interviewees, survey participants, documents, community meeting participants) were interested in payday lending as just one piece of a larger puzzle including the lack of access to financial services for many in Canada and the need for increased knowledge and skills in managing personal finances.

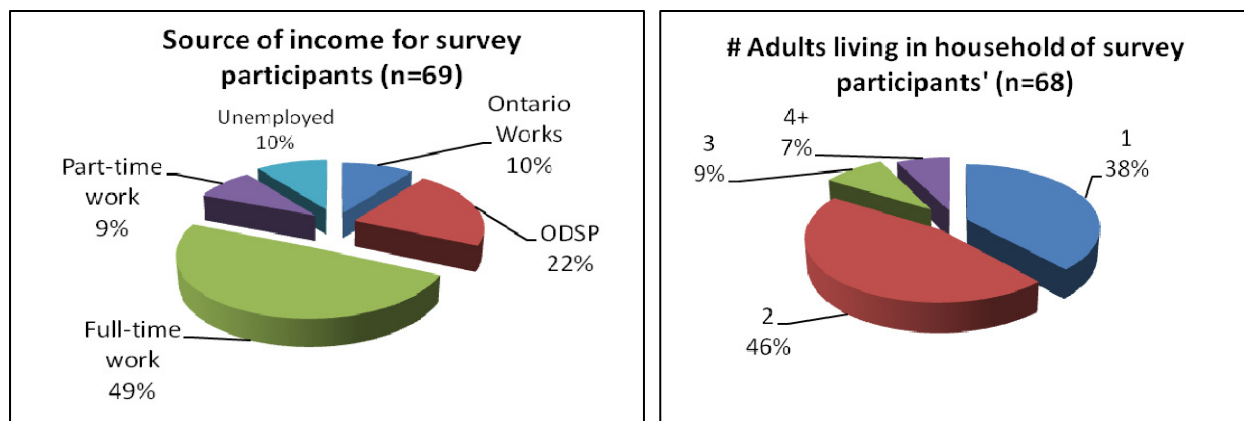


Study Findings

The study findings are summarized in six sections. The first is a brief look at the nature of borrowers' incomes. The rest of the five sections mirror the main research questions: existing practices; borrowers' motivations and satisfaction; the need for an alternative; existing alternatives; developing a local approach to alternatives; and policy recommendations.

Income sources and income levels of payday loan borrowers

Insights about the income sources of people who borrow payday loans were gained through all data sources, including the anonymous online survey for borrowers. Survey respondents varied in source of income; approximately half (49%) work full time and almost a quarter (22%) receive Ontario Disability Support Program (ODSP). Canadian citizens make up 89% of survey participants, while the other 11% are permanent residents. The majority of participants are living in single adult or two-adult households.



According to Stegman and Faris (2003), households with annual incomes under \$50,000 make up the 'core market' for payday loans. Results from the Canadian Ipsos-Reid Express (Ipsos-Reid, 2005) – a national omnibus poll of Canadian adults indicated that households with incomes less than \$30,000 per year were more likely to have borrowed a payday loan (2005).

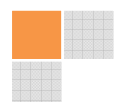
While the typical income levels of payday loan borrowers are modest to low, some borrowers are homeowners and people with high-income levels.

"I belong to a credit union. I have a lot of equity in my house. I needed a small amount of money but they would not comply because of my poor credit rating. As such, I got the money from payday loan." (Borrower interviewee)

"I have excellent credit rating but RBC [Royal Bank of Canada] treats me like I'm a risk because I'm single." (Borrower interviewee)

Borrowers' motivations & satisfaction

This study attempts to better understand the reasons why people borrow, what makes them repeat customers, and what their levels of satisfaction are regarding the service.



Why do people borrow payday loans?

Many factors contribute to the prevalence of payday loans, by far the most prevalent being the need to pay for basic needs on low incomes. Other factors include a lack of other options for small loans, addictions for some people, and for many, the context of a consumer culture driven by credit.

All of the borrowers interviewed and most survey respondents borrowed their first payday loan to pay for basic expenses. This data is consistent with other studies, including a California-based survey (Taking the Pay, 2007). Borrower interviewees named specific expenses including: paying rent, groceries, medication, and car repair. One participant first borrowed when she was not working: *“The first was because I had no job, and I was really broke and the kids needed some medication and there were no groceries in the house so I just went”* (Borrower interviewee).

Two interviewees mentioned that addictions also played a role for them to borrow money: *“Alcohol plays a definite key in it, a definite factor.”* (Borrower interviewee)

Another research participant borrowed to pay for essential needs during a time of family crisis: *“Basic needs, my daughter was going through a very abusive relationship, and I raised my first grandson, and I was getting no financial help for that, that’s when a lot of this started”* (Borrower interviewee).

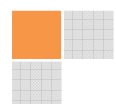
From the wider lens of current societal norms, key informants shared the opinion that household debt and a consumerist mentality of ‘buy now, pay later’ are at all-time highs, and that both contribute to ripe conditions for the payday lending industry. One interviewee from the financial sector indicated the wide-spread nature of this phenomenon:

“A lot of people live off of their overdrafts with credit unions and banks too and never seem to get out from under their overdraft. Cheque cashing is sort of the lender of last resort if I can call them that, but there are a lot of others that live month to month on their overdraft that probably would benefit from some of these counselling services and more debt management programs too... at all income levels.” (Key informant)

Such views expressed by key informants are confirmed by reported consumer debt trends. A study released by the Certified General Accountants of Canada (2009) revealed that household debt is at an all-time high, having reached \$1.3 trillion in 2008. The study suggests that the escalation of debt is primarily caused by consumption motives rather than asset accumulation.

The trend toward an increasingly credit-based economy married with the economic downturn starting in late 2008 contributes to more individuals finding difficulty managing their finances. *“Salaries aren’t increasing, they really aren’t. People aren’t getting their annual increases due to challenges right now, but everything else is going up so everybody’s paying more for their basics”* (Key informant).

Aside from the need to find a source of short-term credit, borrowers are satisfied with certain aspects of the payday lending services.



What do borrowers appreciate about payday loans?

There are a number of factors borrowers appreciate about payday loans, but the most important are the convenient location and hours and the fact that there is no minimum credit rating. These elements surfaced using all data sources, and they are demonstrated by the bar chart below. Borrowers also noted the friendly, non-judgmental services and the quick, no-questions-asked service.

Borrowers of payday loans commented about the convenience and ease with which they were able to borrow money. These hours tend to be seven days/week, between 8 and 13 hours/day (5 or 6 hours on Sunday), and several outlets are located in urban and suburban areas.

"It was too convenient, they make it way too convenient for the poor people or the low income people." (Borrower interviewee)

"It's quick it's easy; there's no questions, no embarrassment really." (Borrower interviewee)

Another reason some people prefer to go to a payday lender is because compared to banks, they are accessible and they have a reputation for relaxed, friendly customer service. One interviewee outlined some of the qualities that make payday lenders more approachable than traditional banks:

"I could see why people like to use them, because they are bright, they're not intimidating, they're open when you need them to be open, the staff are dressed like you are... so you're not feeling like you're a second class citizen like when you walk into banks they can be very intimidating with the marble and security guards and you go to the bank and hand them your bank book or bank card and they go talk to somebody else, so you can see it makes perfect sense." (Key informant)

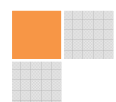
Other borrowers emphasized the level of service and the way they are/were treated by payday lender employees. One even received a sympathy card when a parent passed away.

"The people are terrific, they are really well skilled at what they do, and I've never had a problem with either of the places." (Borrower interviewee)

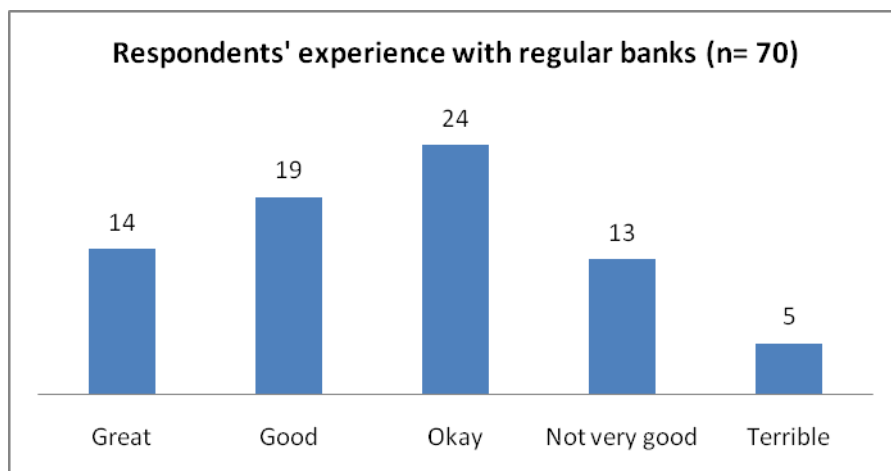
"The individual people, I deal with the same people so you get to know them after a few years you know them pretty well. When my father passed in January I actually got a condolence card from one of the women that worked in one of the money places I deal with, ... which was so nice and unexpected, and it's that kind of stuff." (Borrower interviewee)

In particular, borrowers appreciate that they are not being judged.

"I have a poor credit rating. There is little scrutiny and no judgement of character. The service is always good." (Survey participant)



Not surprisingly, all of the research participants have banking accounts with traditional financial institutions, as it is a requirement for receiving a payday loan. As part of our larger research question about the motivations and satisfaction levels with payday lending, borrowers were asked about their experiences with banks or credit unions. Most responses indicated that people were either satisfied or neutral about their overall banking experiences. Despite this level of satisfaction, participants did not



have their banking needs met by traditional banks. In fact, for those that expressed some dissatisfaction with the banks, the most common reason mentioned was the lack of access to a small loan, and the tight restrictions on a minimum credit rating. Some also mentioned they would like to see banks offer more services and smaller loans to low-income people.

“Well just because with my expenses being so high and the amount of income I make bi-weekly, sometimes it’s just the money isn’t available in the account, so waiting for my next pay cheque to come around, this was the only way to access funds at that time when I needed it because of course there was no lending capabilities from the banking, it was merely chequing account usually.” (Borrower interviewee)

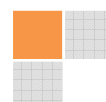
“I have found that the people in the bank are, for the most part, very friendly, but not very helpful. I have huge student loans that loom over my head and when I spoke with somebody at the bank about this, they were not at all helpful and didn't offer any alternatives to paying back huge monthly amounts.” (Survey Participant)

In the current economic context, anecdotal evidence indicates that banks have even further tightened lending restrictions to people with low incomes and low credit ratings. Nevertheless, these findings indicate a potential positive business opportunity for banks and other financial institutions to build on their relationships with people on lower incomes by offering increased services for this population.

Why do people borrow repeatedly?

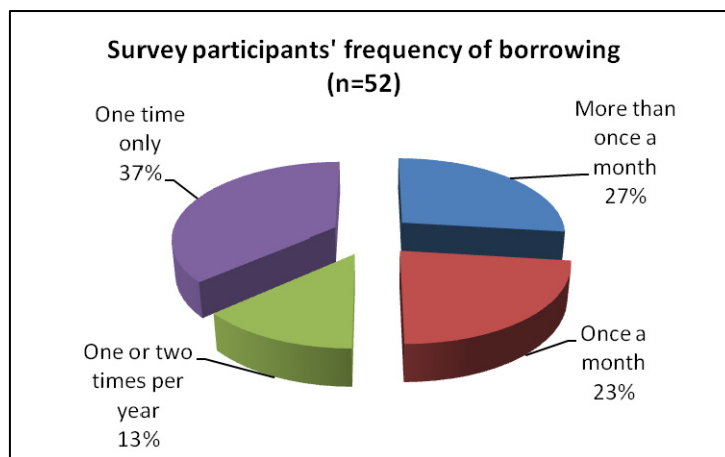
The overwhelming reason why most of the borrowers interviewed and half of the survey participants borrow payday loans once or twice a month is because they do not have enough money on the next payday to repay the loan principal and fees in full, so they need to borrow again to keep up with the inflexible payback period.

For people living pay cheque to pay cheque, payday loans represent a significant challenge to pay back on time due to the very short term payback period and high fees. Because payday loan terms are so short, many borrowers do not have the means to pay it back in full so they need to borrow again to pay



off the first loan. *"It can be a big difference between budgets working and not working...Sometimes people ... get in too deep and start going from one to another to the other and the payments get too big and impossible to sort out."* (Key informant)

As outlined on page six of this report, in 2009, the government of Ontario implemented legislation that prevents any single payday lender from offering 'rollovers' (serial borrowing every two weeks). Nevertheless, there are no measures or tracking in place to allow for borrowers who cannot pay back the full amount on time to pay it back over a longer period. Hence, borrowers are forced to borrow from more than one place as a way to keep up with repaying their loans.



"I borrow from two different places every month. It's a sinkhole. I just can't seem to climb out of it. It's not just one but its two that I'm using and neither one knows of the other. I've been going to these particular two for about three years now." (Borrower interviewee)

"You're paying that company another forty eighty dollars to roll over for another period of time and that's how they're making so much money. You think there has to be at least forty, fifty people that come in a day and they're making that from each person." (Borrower interviewee)

According to analysis of the Survey of Financial Security conducted in 2005 by Statistics Canada, those who borrow more frequently have a lower family income (below Low-Income Cut-Off) than those who borrow occasionally (Pyper, 2007).

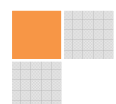
One key informant: *"One quarter of payday loan borrowers use service once a month and they tend to have lower family income than less frequent payday loan borrowers."* (Key informant)

What do borrowers see as disadvantages and negative impacts of payday loans?

The high cost of borrowing, short payback period, lack of full disclosure about that high cost, stress associated with debt, and the collection practices were all identified as disadvantages of borrowing.

All of the research participants noted the very high cost of borrowing, along with the short payback period as main drawbacks of borrowing a payday loan.

"From my experiences I think the most negative things were just the unbelievably high interest rates they have on their loans. Again you'll pay upwards, for \$100 you'd pay upwards of \$40-something on top of your hundred dollar loan which is nearly half of what you asked for in the first place which I find a little outrageous." (Borrower interviewee)



"That you have to pay it back so quickly, the bulk of it at the end of the month or whenever. And you get stuck." (Borrower interviewee)

Many participants reported that payday lenders did not explain to them about the interest rates they would be charged.

"I think they need to be more specific on what the interest is. They didn't really explain very much, they made it sort of short and sweet, beating around the bush kind of thing." (Borrower interviewee)

Others consider payday lending to be intentionally predatory and they criticize governments for allowing them to exist.

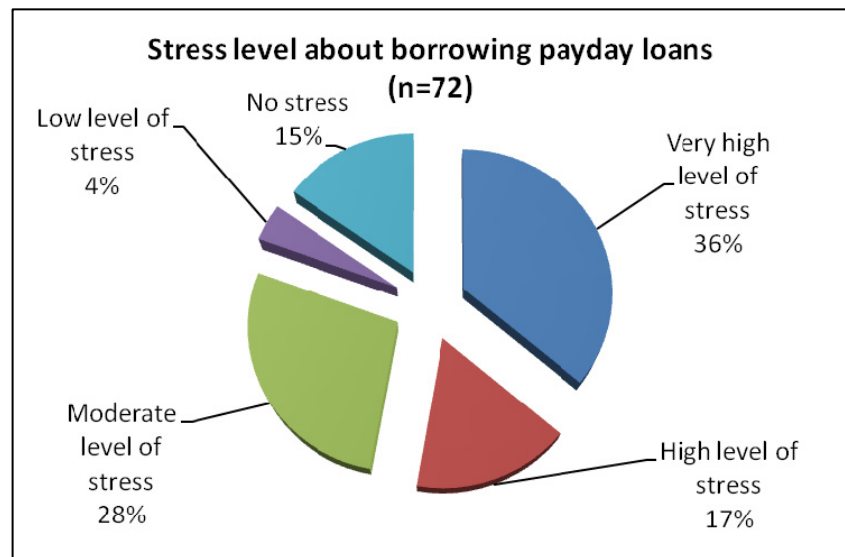
"They are legalized loan sharks. They need to be stopped. I can't believe places like this were ever able to be considered anything worthwhile. Only desperate people use them. They prey on the down-and-out who have nowhere else to turn." (Survey participant)

Borrowing payday loans represented a stressful experience for many borrowers who participated in the study, especially when they needed to borrow on an ongoing basis. One participant also talked about the collection practices having an impact on their lives. Participants found themselves 'debt trapped' by using payday loans.

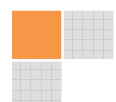
"It kind of ended up getting me in to more of a debt than anything to be honest with you, because you were just paying it off paying it off paying it off using pay and it just became a little too much." (Borrower interviewee)

Participants indicated that payday lending has been a stressful experience for them. Over 50% of survey respondents reported a high level or very high level of stress associated with borrowing payday loans, while less than 20% reported a low level or no stress.

"It makes one worry more, because you've added one more bill to your bills that you couldn't pay in the first place." (Borrower interviewee)



One participant talked about his or her experience when the payday loan was overdue: *"They call your family or friends. That's embarrassing and it is stressful. You're like, oh man don't call them. And you've got your friends calling you, oh well so and so called you and they were looking for you, and they called me at 7 o'clock in the morning or they called late at night."* (Borrower interviewee)



Cost of borrowing repeated payday loans

In Ontario, lenders are allowed to charge up to \$21 for every \$100 borrowed. When an individual borrows \$300, she or he is charged \$63 for what is typically a 10-14 day loan. On the date payment is due, it is due in full. Several borrowers interviewed and surveyed indicated that they usually need to borrow repeatedly (once or twice per month).

A person working full-time at minimum wage (\$9.50/hr x 40 hours/week x 52 weeks) earns \$19,760 per year. If that individual borrows a payday loan of \$300 once per month, they pay \$756 per year in interest, or 3.83% of their total gross earnings for the year. Borrowing \$300 twice per month would result in paying \$1512 in interest, or 7.65% of their total gross earnings for the year.

Is there a need for a local alternative to payday lending?

Participants of this study shared individual stories of the impact of payday lending. When we look at the negative impacts of payday lending at the community level, we can see wider implications including widespread chronic debt, vulnerable groups at increased risk of poverty, and some see it as a symptom of wider social problems.

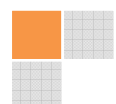
For borrowers with five, ten or even twenty repeat loans per year, payday lending functions as chronic debt, instead of helpful credit. These borrowers pay additional loan fees for no new money each time the loan is renewed. In the United States, the Centre for Responsible Lending estimates that “predatory” payday lending costs five million Americans \$3.4 billion annually (Centre for Responsible Lending, 2009). This amount represents a steep cost to consumers.

People from particularly vulnerable populations are more susceptible to being left with fewer or no banking options.

“When the Mental illness I have got out of control, I wasn't able to work for a long time and thus slowly went into debt. O.D.S.P. income doesn't qualify as income for a loan at a Bank (though they will accept C.P.P. income as such). I was turned down by several Banks and Credit Union type places-I wanted to consolidate my debts in order to pay them off at a lower interest rate. I couldn't find any place to lend me the money. As a result, I recently had to declare bankruptcy! Something I never thought would happen in my life. Sad situation.” (Survey participant)

These findings highlight the precarious state of an increasing number of Canadians' personal finances. The widespread use of expensive credit is seen by some as a symptom of larger social problems, such as poverty, lack of financial literacy, and lack of accessible financial services. These problems point to a need for other stakeholders to get involved, including bankers, educators, social service providers, and governments.

For example, if the provincial or municipal government were to adopt a living wage policy, as suggested by some community members at the community forum held as part of this study, it would contribute to increased stability and decreased need for people to turn to payday lending. A study was conducted in 2003 to determine the living wage in Waterloo Region to sustain a family of three. At that time, the recommended sustainable hourly wage for a single income family of three was \$17.88 (Opportunities



Waterloo Region, 2003). Later, the calculated living wage for a single-person household was reportedly \$13.62 per hour (Social Services, 2009).

Despite recent increases, the Ontario government-legislated hourly minimum wage (as of April 2010, this will be \$10.25) has remained substantially below the nationally recognized Low Income Cut-Off (LICO) amount and even farther below a living wage amount. In April 2010, the minimum hourly wage for Ontario will be raised to \$10.25. Clearly this discrepancy is problematic.

Other potential players to be part of developing solutions to the abundant use of expensive credit, as suggested by the community forum findings, include banks, credit unions, all three levels of government, educators, and non-profit agencies. These stakeholders were also mentioned in one study:

“If mainstream lenders provided more accessible services, and educational institutions and non-profit or government agencies gave more objective information about payday lenders in public service advertisements, perhaps these borrowers might attempt to access other lending options.” (Berry & Duncan, 2007)

One solution that has been posed in several Western countries is an alternative payday lending option. The question of whether or not an alternative is needed was posed to participants in the study *Payday Lending: In Search of a Local Alternative*. In response to this question, the overwhelming majority of participants from all data sources indicated that an alternative is needed.

Survey participants emphasized the need to provide low-income people with a more affordable option when in a time of need.

“Something for the 'working poor' would be good - help folks that are trying to keep their heads above water by giving loans (if needed) that are small but without a big fee.” (Survey participant)

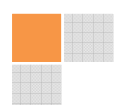
“Of course if they can do it at a reasonable rate, absolutely, ... they would get tonnes of business and make their money on volume of people rather than exorbitant rates.” (Borrower interviewee)

Most key informants also expressed a need for supports to people with no back-up plan.

“Our community needs more of a crisis fund” (Key informant).

The question of improving regulations was discussed by some key informants. One suggested we do not need an alternative, but rather we need improved and enforced regulations to “make them nicer and less expensive, and figure out a way to just solve the big problem. That would be better than coming up with another option” (Key informant). Other key informants believed tighter regulations are not the answer: *“if you legislate too highly it goes under the table and people will find loans and find cheque cashing or money or cash, money under the table’s been there forever”* (Key informant).

Root causes of poverty were talked about by key informants, but they all indicated at the same time that the longer term strategy to address root causes of poverty do not help people in the short-term:



“Obviously the solution is to eliminate the need for these things in the first placeReally what you want to do is make social change so that you put yourself out of business and that you’re no longer needed. On the other hand in the meantime you are needed so what’s the best way to provide the services?” (Key informant)

What payday lending alternatives exist across North America and globally?

To better understand existing models that might be replicable, the literature review and some key informant interviews focused on existing models of payday lending alternatives. Several models of alternatives to payday loan services were examined. In this section, a few of these are described to illustrate models that are quite different from each other. *To see the full literature review, please see Appendix.*

In the literature, different terminology is used to describe efforts to provide increased access to financial services to people. Payday loan alternatives are often one product or service offered in conjunction with other supports. Combined, these supports are sometimes called community banking projects, and more often they are called *microfinance* projects. The United Nations defines microfinance as the provision of small-scale financial services such as savings, credit and other basic financial services to poor and low-income people.

High level of government support and interest in microfinance

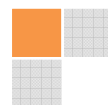
In Australia, the federal and state/territory governments invest in various collaborative initiatives that seek to decrease the rate of financial exclusion. Microfinance services, strategies and supports are offered by community organizations and financial institutions to low-income people for the purpose of increasing their access to basic financial services. Since 2003, the microfinance movement in Australia has developed with significant support from the government, resulting in a range of models and solutions (Burkett & Sheehan, 2009).

Wider movement of active financial institutions, supported by moderate government interest

Throughout the USA, the availability of payday loans and microfinance options varies widely from state to state. Some states have entirely banned payday lending, while others have regulations and some have no regulations on the industry.

Credit unions across the United States are the most common providers of alternative loan products. One such credit union situated in Wisconsin where no regulation exists has partnered with Goodwill to offer a unique product called GoodMoney. Prospera Credit Union has set up counters within Goodwill thrift shops to provide their payday loan alternatives. They use a break-even model with a product that has all the qualities of a payday loan, including a due date of the next payday except the interest rate is approximately half the cost of a payday loan.

In February 2008, the Federal Deposit Insurance Corporation (FDIC) of the United States began a two-year pilot project to review affordable and responsible small-dollar loan programs offered in the United States by financial institutions. The pilot is a case study intended to identify effective and replicable business practices to help banks incorporate affordable small-dollar loans into their other mainstream banking services. Best practices resulting from the pilot will be identified and become a resource for other institutions. So far, FDIC data shows that most affordable loan programs require a certain level of



subsidy, but many financial institutions see it as a lost leader opportunity for attracting new clients who will later become profitable clients for the bank once financial situations improve. Some small loan programs are breaking even, with the potential to be profitable.

Closer to home: Two Canadian case studies

Up until recently, the Canadian government has not shown a strong interest in supporting microfinance on home turf (Canada provides international support to microfinance initiatives in developing countries). In 2009, the federal government launched a Task Force for Financial Literacy to develop a national prevention strategy. With support from various municipalities, financial institutions, foundations, and agencies, Canada has several examples of community banking projects that have sought to meet the needs of individuals not being served by traditional banks. Only two of those offer short-term micro credit for the purpose of meeting household expenses. One of these is a small pilot project taking place in Winnipeg, and the other is a large scale established program offered in various parts of the province of Quebec.

In Quebec, the Caisse Populaires Desjardins and several consumer advocacy groups have come together to offer an interesting package for people interested in small, short-term loans. This is called Mutual Aid Funds. It is a community partnership project between the Desjardins Group and budget consulting organizations that “aim to help people in financial difficulty by offering budget management advisory services and, if needed, a ‘tide-over’ loan. The average loan amount is \$500 and the repayment period is spread over a maximum of 24 months. Most Desjardins Mutual Aid Funds offer interest-free loans... [and] individual budget advice is offered free of charge” (Desjardins, 2010).

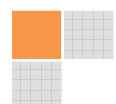
A collaboration between Assiniboine Credit Union and the North End Community Renewal Corporation (NECRC) in Winnipeg offers a range of community banking supports to low-income people. Services include free photo identification, assistance with developing a relationship with a mainstream financial institution, one-on-one financial counselling, and access to micro-loans ranging from \$40 to \$100 with a fee of \$1 per \$20 borrowed.

How should the need for an alternative to payday lending be approached locally?

A blend of diverse perspectives offered opinions about how to best address the need for an alternative to payday lending in Waterloo Region. Based on the research data, the community of Waterloo Region is recommending a holistic comprehensive microfinance model, rather than an isolated payday loan alternative service. The most prevalent response was to approach the issue by offering more than just a more affordable loan service. People talked about the need for increased preventative efforts, specifically financial literacy and credit counselling as well as the need to work with people from a relationship-building stand-point.

Almost all key informants mentioned the need for increased financial literacy: *“Financial literacy is the fancy word for what I think people actually really need”* (Key informant).

Borrowers also were in favour of receiving financial management education:



“Definitely money management! Because most people don’t, well myself I don’t know how to manage money how to stretch a buck or prioritize, the scope is beyond me and I haven’t learned it.” (Borrower interviewee)

“Nobody showed me how to do anything so I just had to figure it out all on my own, but if somebody were to offer something like that [financial counselling, budgeting, etc.] that would be something I would be interested in doing, definitely.” (Borrower interviewee)

Financial management education would encourage people to make ends meet without credit when possible. One study conducted in Arkansas, U.S. (Huddleston et al, 2005) revealed that borrowers found that using credit cards to meet their short term cash needs worked well in the case of emergencies. Many of the participants shared other ways they could obtain emergency money or anticipate hard times. Garage sales, savings accounts, rent-to-own, and bartering were just a few of their alternatives when the car broke down or the refrigerator broke.

Some borrowers indicated the need for other services to be made available as well, such as credit counseling: *“I also think that debt counselling should be more readily available”* (Survey participant).

“Even when they apply for [a loan] say look, we’ll set you up with a financial counsellor and show you how to budget this, because you’ve got a real hard time when you just get paid once a month.” (Borrower interviewee)

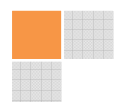
They also talked about the need to ensure borrowers are aware of the terms of a loan: *“Standards be set about ensuring full disclosure (and understanding of implications) of information before a loan can take place”* (Survey participant).

Several key informants talked about an alternative that reaches beyond a set of services for people to access, to offer ongoing relationships with people, so that individuals feel supported enough to discuss their financial situations and work toward solutions.

“If you’re going to get into this for the reasons of improving the people’s lives... you have to be able to find out what the real problem is to see if you can help. If you’re getting into it just to say let people do what they’ve always done and just save them money, that’s a different approach altogether, just give them their money and don’t ask them anything...that’s a business.” (Key informant)

The Waterloo way

Each community will have its own set of existing resources and its own unique approach to an issue. Waterloo Region has several examples of initiatives that offer multiple supports using a wrap-around approach, such as the Family Violence Prevention Program housed at Mosaic Family Counselling, or the Social Work Bridge Training project led by The Working Centre. It has become the *Waterloo way* to offer multiple services and supports in a comprehensive way that supports the whole person, rather than offering one service at a time in isolation of each other.



Recognizing the challenges of implementing such a model, it may be that interested collaborators on a Waterloo Region community banking initiative would need to start small at first, but to have a vision for a more comprehensive approach seems to be very important to the people of our Region. In this way, when a person comes seeking help, the solutions can be creative and unique to each situation. One key informant called this approach an outreach model:

“Embedding it in an outreach model as opposed to a service model, we’re trying to follow you the person and see what works for you, and have you thought of this, have you tried this, what do you think would work, that kind of following the person.... Everybody is thinking in services, we’ll offer this service or that, if you think in services it won’t work.” (Key informant)

Key elements of a potential community banking model

Study participants were asked about what specific elements would be important in a payday lending alternative in Waterloo Region. Their answers, along with literature review findings were shared with participants of a community meeting for verification and additional insights. According to study sources, the following elements were identified as important to include in a community banking alternative for Waterloo Region.

1. Establishment of infrastructure:
 - a. Collaboration among financial institutions, non-profit community agencies
 - b. Convenient hours
 - c. Accessibility from different neighbourhoods in the Region
 - d. Friendly, comfortable setting where trust is already established
 - i. Need to partner with location that people are already connected with, for example food banks, housing services, utilities’ bills
 - e. Relationship building over longer term

Services and supports to offer

Key informants, particularly those coming from the perspective of the social services sector and academic content expertise, provided feedback on the types of services and supports that should be included in a Waterloo Region community banking initiative. Several key informants from all sectors emphasized the need for a multi-pronged approach rather than a single alternative service.

1. Small short term emergency loan, from \$ 100 to \$500
 - a. Charge lower interest rate than payday loan
 - b. Negotiable pay back period (repayable in installments)
 - c. Full consideration of borrower’s ability to repay the loan
2. Encourage individuals to build personal savings
 - a. Asset-building program with matching 3 to 1 dollars provided by external source
 - b. Restricted Savings Account (pay into savings a portion of each loan re-payment)



- c. Optional savings account
- 3. Financial management / budgeting education
- 4. Credit counselling
- 5. One-on-one ongoing support (in some cases mentoring for borrowers)
- 6. Credit restoration (help build credit rating)
- 7. No credit report requirement
- 8. Links to crisis supports and additional community supports

Additional considerations for payday loan alternative

How will people find out about the program? *Suggestions from data:*

- Promote where people have crisis – welcome wagon, pharmacy, car shop, grocery store, community centres, mental health and addictions organizations
- Identify and target at-risk populations: retiring; E.L.; moving; newcomers; consumers

What will be people's first point of entry? *Suggestions from data:*

- Offer phone intake for microloan applications
- Drop-in style

How will accessibility be assured? *Suggestions from data:*

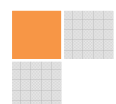
- Inclusive/flexible eligibility criteria
- Offer translation services
- Sensitivity training / skilled staff knowledgeable about resources and options
- Offer the option to volunteer work in lieu of paying interest

How will the expectation of accountability on the part of borrowers be communicated and reinforced?

How will the expectation of non-judgemental supports on the part of stakeholders be communicated and reinforced?

What potential partners / stakeholders would collaborate? *Suggestions from data:*

- Mentorship program: connect those with high level money management skills with people interested in guidance
- Work with mainstream banks to incorporate increased access to financial services
- Community hub of services combined under one roof (credit counseling, credit union, financial management courses)
- Municipalities
- More credit unions
- Health care services
 - Mental health care services; community health services



- Provincial government Ministry of Consumer Services
- Regulators from city and province
- University of Waterloo

What is the default rate for payday loans?

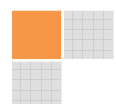
What would be the operating cost of providing a payday loan alternative?

What would be some possible funding sources? *Suggestions from data:*

- Canadian Alternative Investment Cooperatives
- Grants from government or foundations
- Private donors
- Member assistance program @ credit unions or banks: Members can sign up to transfer a small amount of money into a member assistance fund at the end of each month

What community banking supports and resources does Waterloo Region already have?

1. Access to basic necessities
 - Foodbank
 - St. Vincent de Paul
 - I.D. clinic to support people to secure a bank account
2. Access to microcredit
 - Rent bank (Lutherwood-CODA)
 - Share the warmth (Ontario); Heat Bank (Region of Waterloo)
 - Immigrant loan program – up to \$5000
3. Financial literacy
 - Budgeting & financial management workshops (The Working Centre; K-W Counselling; Mosaic; others)
 - Credit counseling (Mosaic & K-W Counselling)
4. Co-operative banking
 - Credit unions
5. Asset-building
 - (Previously) LearnSave asset-building for low incomes (Lutherwood-CODA)
6. Networks of community based and local government resources
 - Strong community organizations and foundations
 - Outreach workers



- Municipal governments supportive of innovative initiatives
- Opportunities Waterloo advocacy work (ex. Living Wage)

Who should operate the alternative?

The data does not point to a single organization to lead the next step, but two key learnings are that it needs to be a collaborative, and that for long-term sustainability, a financial institution should have a sense of ownership in the collaborative.

Most data sources were either neutral about what sector should operate the alternative, or they suggested a not-for-profit should be involved in operation of an alternative. Furthermore, according to a content expert, community banking projects tend to be the most viable when they are collaborations and when *“a financial institution is fully supportive and takes ownership in the model.”* (Key informant)

Two large credit unions have taken part in this study, and indications show that they are willing to explore possibilities to work towards solutions:

“We do our best. It’s not easy sometimes. We certainly have to compete with those big banks that have the technology and the wealth to be able to manage the market. It is a challenge sometimes....But yes it would be nice to be part of the solution rather than just recognizing the problem.” (Key informant)

Several community organizations in the region have taken keen interest in the study, and leaders from these groups have indicated they would be interested to explore next steps toward a collaborative model.

Policy implications

A number of policy implications emerged from the data. These are organized according to provincial and federal points.

Provincial policy areas

1. Enforcement of current regulations

The Payday Loans Act was passed in 2008, to ensure that only registered lenders who comply with the law can supply payday loans. According to this act, the Ministry of Consumer Services is in charge of monitoring compliance. Lenders were given a grace period for registering, which is now ended, and as of January 2010, it is unclear what actions have been taken to monitor payday lenders. Monitoring all 700+ payday lenders dispersed throughout Ontario likely presents logistical challenges, but it is essential for our government to take on this challenge as a way to establish the new regulations.

The Ontario Government needs to:

- ENSURE that only registered lenders are supplying payday loans;
- ENSURE that all payday lenders have educational materials available on-site



- IMPLEMENT the Ontario Payday Lending Education Fund
- ENFORCE all current payday lending laws

2. Consumer protection

The Ministry of Consumer Services has a mandate “to promote a fair, safe and informed marketplace, in which your rights as a consumer are fully protected” (Ministry of Consumer Services, 2010).

The Ministry actively lobbies for transparency with respect to a number of products, such as gym membership, car sales, real estate, and payday loans.

Payday loan consumers are among the most financially vulnerable demographic in Ontario, so their rights as consumers need to be more **fully** protected. The Ministry of Consumer Services Consumer Protection Branch should:

- FEATURE educational materials (videos and written material) on their website about the rights of consumers regarding payday loans
- PROVIDE public service announcements in mainstream media and on public transportation advertisement spaces
- UPDATE those materials regularly to ensure that they remain relevant and accessible.

3. Financial Literacy in Ontario schools.

Starting in September 2011, Ontario education curriculum will include financial literacy units for grades 4 to 12 students. A working group, co-chaired by Parliamentary Assistant Leeanna Pendergast, will recommend strategies for how to introduce financial literacy into Ontario's curriculum to the Ministry of Education's [Curriculum Council](#) in summer 2010.

The findings of this research study need to be shared with this working group because they offer relevant insights.

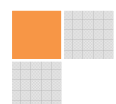
Financial literacy curriculum for Ontario should include the learning goal of increased awareness of payday lending, its high interest rates and short pay-back periods. This should be included in all units about borrowing and credit.

4. Financial Literacy for adults

Early financial literacy is only part of the solution. Financial literacy for adults in Ontario needs to be a priority.

5. Poverty Reduction: Building Stronger Communities

Most of the borrowers interviewed and surveyed in this study were living on low incomes, including those working full-time. The Living Wage movement needs to be supported by local and provincial governments, to ensure that Ontario's Poverty Reduction Strategy is effective.



Ontario's Poverty Reduction Strategy is investing \$5 million annually in a Community Opportunities Fund. More information needs to be shared to clarify how this money becomes available for community partnerships to apply for funding, and also to report publicly on how it has been spent each year.

The government of Ontario needs to clarify and widely promote how community partnerships can access the Community Opportunities Fund

Federal policy areas

6. Task Force on Financial Literacy

The Task Force on Financial Literacy was created by the federal government in June 2009 to recommend a national strategy for strengthening financial literacy in Canada. In the spring of 2010, the Task Force will host public consultations across Canada to obtain feedback from citizens and organizations so that final recommendations submitted in December 2010 reflect the ideas and thoughts of Canadians. For more information: www.financialliteracyincanada.com or info@financialliteracyincanada.com.

It will be important to share the results of this research project at a consultation because it reinforces the need for increased financial literacy efforts. The Canadian government should highlight payday lending as a focus point of the forthcoming national strategy for strengthening financial literacy in Canada. As part of a financial literacy plan, the government should offer microfinance incentives including:

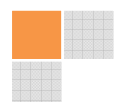
- micro-loan funding
- asset-building programs
- credit restoration opportunities

7. Banking services extended to more low-income people

The Financial Consumer Agency of Canada has made some efforts to ensure low-cost accounts are made available to low-income people. Still, a significant number of people have not accessed these accounts for various reasons, a primary reason being the limited number of transactions allowed per month without additional charges. More can be done. It is the responsibility of our governments to ensure access to financial services for low-income people.

Low-cost accounts should be revisited to ensure they are effective.

Other financial services offered by banks should also be revisited by the FCAC to ensure access by low-income people.

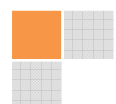


Recommendations for next steps

1. Disseminate finalized research report using web-based approach, including social media, website, email lists.
2. Finalize and separate Waterloo Region-focused aspects into practical document.
3. Explore potential next steps for developing a collaborative microfinance project in Waterloo Region.
 - a. Large community forum
 - b. Small meeting of potential collaborators
 - c. Engage with each stakeholder group: financial institutions; community organizations; potential funding sources; borrowers; governments
4. Communicate policy recommendations to appropriate bodies

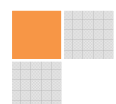
Findings indicating need for further study outside the scope of our topic:

- Buying of gold at payday loan operations
- Ontario Disability Support Program and Ontario Works payment frequency



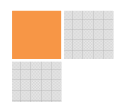
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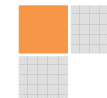
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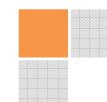


Appendix A: Payday Lending Alternatives Literature Review Summary

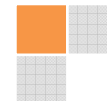
#	Alternative	Key Features and Source
1	State Employees' Credit Union (SECU) Salary Advance Loan Program—known as SALO	<ul style="list-style-type: none"> - Introduced in 2001 - Short term loans - Credit union members can borrow up to \$500 per month - 12% annual interest rate - repaid monthly with funds from their next pay check. - Borrowers to repay via direct deposit - Borrower to put 5% of loan proceeds in savings account - Each month more than 40,000 people use the product with a maximum 31-day term - \$10 million accumulated in savings accounts <p>USA Today (no date). Breaking the Cycle of Payday Loan 'Trap' http://www.usatoday.com/money/perfi/general/2006-09-19-credit-unions-usat_x.htm (accessed October 6, 2009)</p> <p>Jackson, M. Nancy. (no date). 4 Alternatives to payday lending http://www.bankrate.com/finance/personal-finance/4-alternatives-to-payday-lending-1.aspx (accessed October 6, 2009)</p>
2	Prospera Credit Union in Appleton in collaboration with the Goodwill Industries (GoodMoney)	<ul style="list-style-type: none"> - Launched in 2005 - \$ 9.90 fee per \$ 100 loan (around 200 percent annual rate) - After the third loan, borrowers get a voucher for free counselling and opportunities to consolidate and pay off previous loans. - The program offers check cashing, money wire transfer and other services - Five dollars of the \$ 9.90 fee covers defaults. - access to Goodwill's Financial Information & Service Centre where financial workshops, money and budget counselling, and debt management plans are offered to help people better understand and manage money. <p>USA Today (no date). Breaking the Cycle of Payday Loan 'Trap' http://www.usatoday.com/money/perfi/general/2006-09-19-credit-unions-usat_x.htm (accessed October 6, 2009)</p> <p>Jackson, M. Nancy. (no date). 4 Alternatives to payday lending http://www.bankrate.com/finance/personal-finance/4-alternatives-to-payday-lending-1.aspx (accessed October 6, 2009)</p>



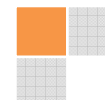
3	Hogreb's council committee	<ul style="list-style-type: none"> - a loan program that charges just 3 percent interest, and offers a flexible repayment schedule and finance education. - the committee reached out to St. Vincent de Paul conferences - With \$15,000 from conference donations, the St. Vincent de Paul council approached another organization, the Catholic and Community Credit Union, for help in implementing the program. - Potential borrowers go to St. Vincent de Paul and fill out an application. St. Vincent de Paul reviews that application with the assistance of the credit union loan officers. - If approved, St. Vincent de Paul pays the \$25 savings account fee or share fee of the credit union and a \$300 loan is made to the borrower from the \$15,000 fund. - Borrowers participate in a budgeting class and are taught how to save money. - The program provides mentors for borrowers so they can learn new habits - After successfully completing the budgeting class, the borrowers receive a \$5 grocery store gift card. - The 3 percent interest will go back into the loan fund with the hopes of creating greater resources for more loans. - For those who don't qualify due to enormous debt, no income or dishonesty, they are directed to consumer credit counsellors and other sources of assistance. <p>National Catholic Reporter (no date). An alternative to payday loans for the working poor http://ncronline.org/news/justice/alternative-payday-loans-working-poor (accessed October 6, 2009)</p>
4	Golden 1 Credit Union (California)	<ul style="list-style-type: none"> - offers cash advances of up to \$300 - 15 percent APR - a one-time, \$15 application fee - a repayment period of up to 35 days - Borrowers also must take an additional 15 percent of the loan amount (\$45 on \$300 cash advance), which is deposited into a restricted savings account. These funds can be withdrawn once the balance reaches \$300. <p>Payday Loans: Taking the Pay Out of Payday http://www.cbp.org/pdfs/2008/080926_paydaychartbook.pdf (accessed October 6, 2009)</p>
5	Pentagon Federal Credit Union Foundation (Pentagon Federal) Asset Recovery Kit (ARK) product	<ul style="list-style-type: none"> - borrowers must agree to financial counselling, or already be receiving counselling - a loan of up to \$500 - borrower pays a \$6 flat fee for the loan - no credit report is required - financial counselling is mandatory <p>Akaka, D. Kahikina (2005). The Low Cost Alternatives to Payday Loans Act http://akaka.senate.gov/public/index.cfm?FuseAction=Speeches.Home&month=6&year=2005&release_id=339 (accessed October 6, 2009)</p>



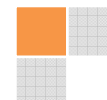
		October 6, 2009)
6	Langley Federal Credit Union (Langley Federal) QuickCash product	<ul style="list-style-type: none"> - 18 percent annual percentage rate - does not have the financial counselling requirement <p>Akaka, Daniel Kahikina (2005). The Low Cost Alternatives to Payday Loans Act. Retrieved May 14, 2010 from http://akaka.senate.gov/statements-and-speeches.cfm?method=releases.view&id=4b971a0a-8b60-4088-baab-69ca87abb67a</p>
7	Elite Cash Services (California)	<p>The types of loans that Elite Cash Services is currently offering are:</p> <ul style="list-style-type: none"> - The Short Term Instalment Loan: These loans range from \$300--\$499 for a term of 6-10 weeks. - The Classic Instalment Loan: These loans range from \$500-\$699 for a term of 12-20 weeks. - The Six Month Instalment Loan: These loans range from \$700-\$899 for a term of 22-26 weeks. o these loans have a set payment schedule that is broken down into substantially equal semi-monthly payments that are paid over the life of the loan making the payments for these loans more manageable. o consumer would be able to get a loan for \$300-\$899 for a term of 6 weeks—6 months o APR ranges from 81.17657%-38.33709%. <p>Elite Cash Services also offers a payday loan or what they call a Turnaround Loan for the consumers that are looking for the same type of loan that the traditional payday lenders are offering.</p> <ul style="list-style-type: none"> - For these Turnaround Loans Elite Cash Services charges \$8 per \$100 - APR of 208.57140%-104.28570% (half of what a consumer would pay at a traditional payday loan lender) <p>Elite Cash Services (2008). A Safe New Alternative to Payday Loans in California http://express-press-release.net/48/A%20Safe%20New%20Alternative%20to%20Payday%20Loans%20in%20California.php (accessed October 6, 2009)</p>
8	APPLE GRANTS (In 2004-05, JPMorgan Chase & Co. And the Federation selected six credit unions in five states to create and develop	<ul style="list-style-type: none"> - Interest rates: APRs ranged from 10% to 18% (median of 16%) - Fees: Application fees ranged from \$10 to \$35 (median \$15) plus late fees - Minimum loan: Ranged from \$0 to \$500 (median of \$100) - Maximum loan: Ranged from \$300 to \$3,000 (median of \$8,00) - Loan types: Mostly installment loans, with some line-of-credit and single payment loans <p>Restrictions:</p> <ul style="list-style-type: none"> o Three sites had no restrictions



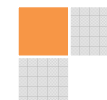
	alternatives to high-cost 'payday' loans for consumers.)	<ul style="list-style-type: none"> ○ Three sites had limits on maximum number of loans per period—e.g., no more than 2 loans per year or no more than on LOC draw per months. ○ One site restricted the use of their emergency loans to consolidate the debts from payday lenders; the credit union itself would make the payments to the payday lenders and borrower must sign statement not to use payday lenders during term of loan. <p>Underwriting:</p> <ul style="list-style-type: none"> ○ Membership: Half had no or minimal membership requirements; the rest required 3 to 6 months membership to be eligible ○ Credit reports: Half required credit reports, half did not require them ○ Direct deposit: Strongly encouraged or required by all ○ Financial education: Required by one site, offered and strongly encouraged by all ○ Bankruptcy: Recent filing or liens disqualify borrowers at two sites ○ Savings: Two sites require minimum savings deposits <p>Best Practices:</p> <ul style="list-style-type: none"> - Interest rates and fees: None were higher than 18% and fees were low in all case - Direct deposit: Recommended by all sites - Credit reports: are not needed if the borrower has a relationship with the financial institution or if direct deposit is required - Financial education: should be easily available and strongly encouraged - Payday-alternative loans should be used to build credit: every site reported the payment history of their APPLE loan products to the major credit bureaus. - No special technology: was used in underwriting, tracking or reporting on these loans. - Rapid follow-up on delinquencies: First contact generally by telephone within 10 days of first missed payment. <p>Payday Lending Alternatives http://www.natfed.org/i4a/pages/index.cfm?pageid=902 (accessed October 6, 2009)</p>
9	Pennsylvania Credit Union Association	<ul style="list-style-type: none"> - a short-term installment loan of \$100 to \$500 for a maximum of 90 days - There are no rollovers and additional loans are not permitted until the first loan is paid off



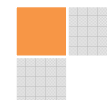
	<p>(PCUA)</p> <p>created Credit Union Better Choice (CUBC) and offered to its members credit unions</p>	<ul style="list-style-type: none"> - A maximum of 18 percent APR - a \$25 application fee may be charged - Employment verification and other loan decision criteria are determined by the credit union - The product provides for some forced savings. At loan disbursement, 10 percent of the loan amount is deposited into a savings account in the member's name - The borrower cannot withdraw any portion of the deposit or close the account until the loan is paid in full - The interest that the credit union pays on the deposit is rebated to the savings account upon payoff. - Participating credit unions offer financial education to CUBC borrowers, although borrowers are not required to receive it - Financial education is typically provided by non-profits in the local community or by the credit unions - The credit unions do their best to move consumers from CUBC to traditional products - Borrower repayment record on the CUBC loans are reported to the credit bureaus - participating credit unions do not check the credit score or credit record of CUBC applicants <p>Rolland, L. Keith (2008). Pennsylvania Credit Union offer Payday Lending Alternative http://www.philadelphiafed.org/community-development/publications/cascade/69/04_PA-credit-unions-offer-payday-lending.cfm (accessed October 6, 2009)</p>
10	<p>Federal Deposit Insurance Group</p> <p>(. In early 2008, the Federal Deposit Insurance Group, or FDIC, launched its Small-Dollar Loan Program, a two year case study designed to illustrate how banks can profitably offer affordable small dollar loans as an alternative to high –cost financial</p>	<ul style="list-style-type: none"> - The loans, \$2,500 or less, are issued under FDIC guidelines that cap their interest at 36 percent. - In the first quarter of 2008, the banks issued 3,140 loans, 1,535 of which were for less than \$1,000 - The average term was 10 months with a 15.05 annual percentage rate. <p>Washington Post (Aug 12, 2008). FDIC Pilot Program Explores Alternatives to Payday Loans http://www.washingtonpost.com/wp-dyn/content/article/2008/08/11/AR2008081102363.html (accessed October 6, 2009)</p> <p>Jackson, M. Nancy. (no date). 4 Alternatives to payday lending http://www.bankrate.com/finance/personal-finance/4-alternatives-to-payday-lending-1.aspx (accessed October 6, 2009)</p>



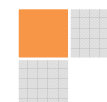
	products, such as payday loans.)	
	RESEARCH	<p>In discussion about payday loan alternatives, several factors that bank representatives thought were critical to successful alternatives:</p> <ul style="list-style-type: none"> - Product alternatives should be easily available and handled as transactions rather than as loans. This would allow the customer to access small amounts of cash without having to go through a lengthy approval process or 'credit decision'. For example, the initial decision for the 'loan' could be made at the customer service representative level to make it more like a payday lender and ease bank costs. However, some thought it unlikely that such decisions could be made at that level. - They generally agreed there should be designated time frame for repayment - The customers should be encouraged, and perhaps required to enroll in credit counselling and to open a savings account to avoid future problems. - Some suggested that the alternatives be 'bundled' such as into a checking and savings account, and that it is a one-time loan with an incentive to build up to more traditional credit options with the bank. <p>Banks and credit unions have the potential to offer realistic low-cost alternatives to payday loans because:</p> <ul style="list-style-type: none"> - Their operational costs are minimized given their pre-existing infrastructure. They already have the physical facilities, loan staff, collection processes, etc. , in place - They are in a better position to minimize credit losses through the use of direct deposit and automatic deductions for repayment-- tools generally unavailable to payday lenders. - They have the advantage of offering and deriving revenue from a variety of products and services, allowing them to profitably offer small dollar credit at lower margins. - Payday loan alternatives offered by banks and credit unions in the form of revolving lines of credit are superior to payday loans in terms of customer convenience, speed and privacy. <p>Those same financial institutions, however, face three major obstacles to creating these alternatives:</p> <ul style="list-style-type: none"> - Though depository institutions have the means to offer low-cost payday loan alternatives, the proliferation of fee-



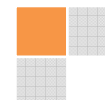
		<p>based bounce protection programs represents a significant impediment to competition.</p> <ul style="list-style-type: none"> - To promote competition and help consumers identify the lowest cost credit product, the Federal Reserve Board would have to impose homogenous disclosure requirements on all functionally equivalent forms of small dollar credit. - Perceptions of regulatory hostility discourage banks and credit unions from offering low-cost payday loan alternatives. <p>Huddleston, Rich, Kelly, Paul., and Haslett, Kathryn. (2005). 'Alternatives to Payday Loans' in Paycheck \$ and Politics, Issue 34, http://www.aradvocates.org/images/pdfs/Alternatives2.pdf (accessed October 6, 2009)</p>
	RESEARCH	<p>Alternatives to payday loans should have these features:</p> <ul style="list-style-type: none"> - At least a 90-day repayment term, repayable in installments; - No personal check mechanism or other unfair collateral (such as a car title) - Reasonable limits on renewals (if borrowers are renewing short-term loans more than four times per year, the loans are not helping them) - Full consideration of borrower's ability to repay the loan - No mandatory arbitration clause <p>Centre for Responsible Lending (no date). Alternatives to Payday Loans http://www.responsiblelending.org/payday-lending/tools-resources/alternatives-to-payday-loans.html (accessed October 6, 2009)</p>
	<p>Community Banking Projects (defined as an identifiable outlet or service tied to existing outlets that offers one or more financial services for</p>	<ul style="list-style-type: none"> - 3 of the 4 projects (Cash & Save, CFSC and PPS) are located in one or more inner-city neighbourhoods, which are characterized by disadvantage - All of the community banking projects face unique financial challenges which require partnerships with banks/credit unions/community organizations to help them be viable - One key conclusion is that community banking projects are expensive and are not likely to become self-sufficient and that the role of government in these projects needs to be clarified, both in terms of public policy and in terms of funding



	<p>4) The Desjardins Federation Fonds d'entraide Desjardin</p>	<ul style="list-style-type: none"> - The idea is to assist people experiencing financial difficulties through financial counselling and access to small emergency loans of \$500 to \$1,000 - The loans are provided at a low or no interest rate to people otherwise unable to access credit - The project involves the federation, a local <i>caisse populaire</i> and a credit counselling agency - The budget counselling agency refers clients to the program, does pre-lending counselling and monitors repayment. - As of December 2007, approximately \$1.3 million in loans were made in 2,421 loans with an average loan size of \$549 and repayment rate of 89%. - The typical borrower is between 25 and 54 years of age, often female relying on social assistance and with annual income less than \$10,000.
	<p>Grand Central Savings (Scotland, UK)</p>	<ul style="list-style-type: none"> - Provides a "basic transactional" type service for the 'unbanked' homeless community and is funded with lottery money - Serves customers with little or no choice for their banking, who are unable and often unwilling to engage with mainstream banking or who are forced to pay hefty charges at cheque point centres to access their benefit payments - The bank offers free banking at convenient locations with understanding and empathetic customer service - Does not require customers to have the traditional forms of ID and address verification (e.g., passport and driving licenses, tenancy agreements, benefit books and utility bills, etc.). Instead, they take a photograph of the customer, store it on a database, obtain two sample signatures and an address and national insurance number. The Bank keeps a manual record of every account holder as well as a photograph in the database
	<p>Delivering the Post Bank: Financial services for people, communities, and small businesses at the Post Office (July, 2009)</p> <p>UK</p>	<ul style="list-style-type: none"> - Proposes that a Post Bank be created modeled on the Post Office network - Argues that big retail banks have not fully carried out their legal obligation to tackle financial exclusion and that a Post Bank (local and widely inclusive) would help the government to make progress in combating financial exclusion - A Post Bank was identified as a possible key solution to financial inclusion through providing strong marketing, partnering with local credit unions and using a social enterprise model <p>Innovations at the Post Bank include:</p> <ul style="list-style-type: none"> o Offering low interest rates to everyone o Not charging the poor (or "riskier") higher rates o Will offer socially-focused insurance, such as home and contents insurance, which could be targeted at those who are currently financially excluded



		<ul style="list-style-type: none"> ○ Work in partnership with local credit unions and provide access points to a range of other financial services, including debt advice and financial management schemes (allowing people who are poor to budget and pay utilities by direct debit weekly) ○ Proposes a mobile payments system <ul style="list-style-type: none"> ▪ People who are currently financially excluded can get discounts on utility bills (currently enjoyed by wealthier people on direct debit) ▪ Allows people to text cash to ATM machines ▪ Gives people unique account numbers that people can take with them when they change mobile phones ▪ Can enable people to pay utility bills without queuing ▪ Allows the government to pay simple benefits out in mobile payments rather than by cheque ▪ Advantage of the m-payments system is that it would greatly reduce the cost of providing basic banking services to the unbanked as well as attracting young people looking for innovation and convenience ○ Proposes that the Post Bank be a not-for-profit organization, where profits are returned to business, and with access to both government and private funding, free of government control or interference, able to borrow on the open market and can hire from the best of private sector management with a clear public service remit
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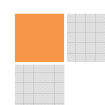


Appendix B: Payday Lending – Environmental Scan¹

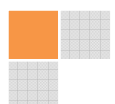
CANADA

1. **Regulation of Payday Lending in Canada: A Report to ACORN (May, 2006)**
 - Proposes a fee structure that would replace the current rule of 60% maximum interest contained in the Criminal Code so that mainstream financial institutions could compete in the short-term lending field legally
 - Proposes that one of the following 2 fee schedules be adopted for payday lending:
 - Fixed fee of \$10 per loan + interest charged at a rate of no higher than 60% per annum, effective annual rate + a fee that is a fixed percentage of the dollar value of the loan no larger than 5%
 - A fee that is 12% of the first \$250 of the loan principal + 6% of the loan principal in excess of the first \$250
 - Recommends that the lender be allowed to charge 60% effective annual rate (EAR) on any loan in arrears but no other fees except cost recovery of bank charges for returned cheques
2. **St. Christopher House – Financial Advocacy and Problem-Solving Proposal**
 - Just completed its 5th year of operation; provides consumer financial information and problem-solving for low-income families and individuals in downtown west Toronto, including newcomers, people with disabilities, homeless people, youth, adults and seniors
 - Found that the majority of poor families are skilled at budgeting but the following types of financial issues make inadequate incomes even worse:
 - Barriers to information about financial matters
 - Worse for low-income people, especially if they have limited English language or literacy skills
 - Barriers to appropriate financial tools/services (e.g., credit, registered retirement savings, banking services)
 - Because most financial services are geared to higher-income ‘markets’, many savings and credit vehicles are not income-sensitive and have significant negative consequences for low-income people
 - Barriers to asset-building/saving
 - There are a number of disincentives in many income assistance programs and taxation policies that discourage people saving and accumulating assets that allow individuals and households to escape poverty
3. **Life Goals, Finances and Financial Service Choice: Using ‘Financial’ Life Histories to Understand Low-income Peoples’ Financial Coping (a component of the research project: Financial Exclusion & Poverty in Canada: Individual Coping, Community Action & Policy Reform, Fikkert et al, 2008)**
 - Summarizes interviews undertaken with 15 low-income respondents in Vancouver, Winnipeg and Toronto about their financial life history (between Aug 06 and March 08)

¹ This Environmental Scan was conducted by Wellesley Institute.



- Purpose was to identify significant changes in people's lives and finances and to examine how these changes interact with financial service choice (much higher level of mental illness reported from male Toronto respondents – all 5 reported mental health problems, but no respondents from Vancouver or Winnipeg did – related to cutbacks in 1990s?)
- Found that there was a cyclical relationship between poverty, mental illness and addiction in participants' lives and that financial hardship was often a result of a series of unavoidable events that prevented positive change – challenges (from this study) involved mental illness and addiction but also institutional barriers
- Respondents mentioned that mainstream services would have helped them to achieve their savings goals but that they had been excluded from such services (e.g., by unexpected service charges) which had meant that the finances and life goals of the respondents had changed
- Fringe banking services were said to have filled holes in respondents' communities left by mainstream banks which did not want to deal with inner-city clients
- During periods of relative financial well-being, respondents were able to use mainstream services but when facing financial hardship, ill health and addiction, they tended to use fringe services
- During low-to-modest income periods, use of financial service providers was undertaken by a form of 'grazing' – weighing up the pros and cons of different providers using such criteria as direct economic costs, location, identification requirements, cheque holding policy, hours of operation and respect from staff (for many, but not all, respondents)
- In Vancouver, Pigeon Park Savings (a community financial service) was popular and demonstrated how an alternative to fringe banking is appreciated as they can meet the needs not met by mainstream and expensive fringe services. However, barriers to their usage included: unsatisfactory hours of operation, time required for transactions, fear of disclosure to government agencies, all of which need to be addressed if these are to present a viable alternative to fringe banking.
- Beyond covering basic needs, respondents did not place a huge amount of emphasis on financial status in terms of their quality of life and seemed to want to talk about other (non-financial) aspects of life that for them were more important
- Fears of garnishment and disclosure were significant barriers for respondents in terms of accessing potential assistance from banking and government institutions
- Social services had played a large – and often negative – role in respondents' lives, with respondents saying that income assistance was inadequate and often obstructive and that they would rather see changes in social assistance than changes to banking services
- In conclusion, study found that the life transitions of the respondents were often due to factors beyond the control of the individual and that they were mutually reinforcing. They were often brought about by accident or ill-health, which led to health problems and substance abuse, which affected employment and income (addiction and selling drugs were often result of insufficient resources and addiction was huge drain on finances, leading to difficulties with budgeting and inability to save). These were then exacerbated by institutional barriers created and enforced by government and financial service industries. The study found no significant



differences between low- and middle-income Canadians apart from these unavoidable external events and institutions.

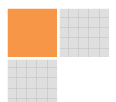
4. Community Banking Projects for Low-Income Canadians: A Report Examining Four Projects to Promote Financial Inclusion (J. Buckland, 29 October 2008, Menno Simons College, University of Winnipeg)

- Looked at 4 community banking projects (defined as an identifiable outlet or service tied to existing outlets that offers one or more financial services for low-income people) using organization publications, newspaper articles and interviews with key informants: Cash & Save (Toronto), Pigeon Park Savings (Vancouver), Community Financial Service Centre (Winnipeg), and Desjardins Mutual Assistance Fund (Quebec)
- **Found that stakeholders involved in these projects have different interests, understandings and values which can lead to constructive tensions between them and requires understanding of values**
- 3 of the 4 projects (Cash & Save, CFSC and PPS) are located in one or more inner-city neighbourhoods, which are characterized by disadvantage (e.g., Vancouver's Downtown Eastside and Toronto's Parkdale neighbourhoods have relatively high levels of people with mental illness or people dealing with substance abuse issues)
- Neighbourhoods have experienced changes in availability of financial services over time
- All of the community banking projects face unique financial challenges which require partnerships with banks/credit unions/community organizations to help them be viable
- Author talks about the need for dialogue across 'cultures' – differences in attitudes and experiences across different SES in society, esp. between banks and inner-city residents, and between community organizations and financial institutions
- One key conclusion is that community banking projects are expensive and are not likely to become self-sufficient and that the role of government in these projects needs to be clarified, both in terms of public policy and in terms of funding

UNITED KINGDOM

5. Grand Central Savings (Scotland, UK)

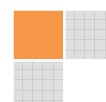
- Provides a "basic transactional" type service for the 'unbanked' homeless community and is funded with lottery money
- Serves customers with little or no choice for their banking, who are unable and often unwilling to engage with mainstream banking or who are forced to pay hefty charges at cheque point centres to access their benefit payments
- The bank offers free banking at convenient locations with understanding and empathetic customer service
- Does not require customers to have the traditional forms of ID and address verification (e.g., passport and driving licenses, tenancy agreements, benefit books and utility bills, etc.). Instead, they take a photograph of the customer, store it on a database, obtain two sample signatures



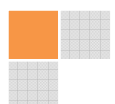
and an address and national insurance number. The Bank keeps a manual record of every account holder as well as a photograph in the database

6. Delivering the Post Bank: Financial services for people, communities, and small businesses at the Post Office (July, 2009)

- Proposes that a Post Bank be created modeled on the Post Office network
- One of the aims of the Post Bank are to combat social exclusion and financial inequalities and to provide an accessible payments system for people currently excluded from the banking system
- One of the criticisms of the Cruickshank Report on competition in UK banking (2000) was that there was a lack of access to banking services for lower income earners
- Trend of declining number of bank branches, particularly problematic in low income areas
- Argues that big retail banks have not fully carried out their legal obligation to tackle financial exclusion and that a Post Bank (local and widely inclusive) would help the government to make progress in combating financial exclusion
- Shared goal (agreed by the government and major UK retail banks in Dec 2004) was to halve the number of adults without access to a bank account (in 2002-3, 2.8 million adults in 1.8 million households found to have no access to a bank account)
- Have reported a slight decrease in the number of adults without access to a transactional bank account and in 2003, banks created and promised to provide a “no frills” basic bank accounts but problematic because offered no interest, not well-promoted and not always act as a gateway to further financial products and greater inclusion. Figures for overall unbanked population suggest that those opening accounts were not from the most excluded, some accounts are lying dormant and others have all the money withdrawn from them in one transaction
- Problem is that things are moving too slowly (as reported by the Financial Services Taskforce)
- A Post Bank was identified as a possible key solution to financial inclusion through providing strong marketing, partnering with local credit unions and using a social enterprise model
- Innovations at the Post Bank include:
 - Offering low interest rates to everyone
 - Not charging the poor (or “riskier”) higher rates
 - Will offer socially-focused insurance, such as home and contents insurance, which could be targeted at those who are currently financially excluded
 - Work in partnership with local credit unions and provide access points to a range of other financial services, including debt advice and financial management schemes (allowing people who are poor to budget and pay utilities by direct debit weekly)
 - Proposes a mobile payments system
 - People who are currently financially excluded can get discounts on utility bills (currently enjoyed by wealthier people on direct debit)
 - Allows people to text cash to ATM machines
 - Gives people unique account numbers that people can take with them when they change mobile phones



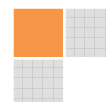
- Can enable people to pay utility bills without queuing
 - Allows the government to pay simple benefits out in mobile payments rather than by cheque
 - Advantage of the m-payments system is that it would greatly reduce the cost of providing basic banking services to the unbanked as well as attracting young people looking for innovation and convenience
 - Proposes that the Post Bank be a not-for-profit organization, where profits are returned to business, and with access to both government and private funding, free of government control or interference, able to borrow on the open market and can hire from the best of private sector management with a clear public service remit
- 7. The financial exclusion of adults with multiple needs (Friends Provident Foundation, June 2009, UK)**
- Conducted interviews and focus groups with people who face multiple problems such as homelessness, mental ill health, drug and alcohol use, and involvement with the criminal justice system and explored their access to mainstream financial services, their financial management skills and the interplay between key life events, mental health and financial exclusion
 - Key findings:
 - The majority of interviewees were living in poverty, unable to afford even the bare essentials
 - Those with mental health problems said financial difficulties added to their distress
 - They faced barriers to accessing mainstream financial services, such as the need for identification and a permanent address. This often forced people to turn to more expensive – and sometimes illegal – sources of credit
 - The benefits system often acted as a further barrier to financial inclusion, where delays and excessive paperwork defined many people’s experience of the system
 - Life events had a significant impact on people’s financial stability, whereby entering or leaving prison and/or becoming homeless often led to both personal and financial crisis. These events were a particularly common experience for adults with multiple needs
 - Interviewees preferred to get their financial advice from someone they already knew (e.g., a support worker) rather than specialist money and debt advice agencies. However, many practitioners in these support roles did not feel equipped to help people with their finances.
 - All interviewees aspired to a future that included working, supporting family members and contributing to society
 - Key recommendation:
 - Adults with multiple needs require a range of supportive measures to enable them to achieve financial inclusion.
 - Interventions must take into account the breadth of their needs and ensure that services that support them work in partnership with specialist financial agencies



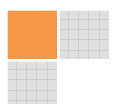
DEVELOPED ECONOMIES (WORLD BANK, 2006)

8. Policy level response to financial exclusion in developed economies: lessons for developing countries (Elaine Kempson, The Personal Finance Research Centre, University of Bristol)

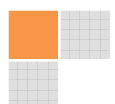
- Factors that deter or prevent some people from opening and using a bank account include: identity requirements, terms and conditions, charges, physical access problems and psychological barriers
- Draws on detailed case studies of Australia, Belgium, Canada, France, Great Britain and the US and collected information on policy responses in a range of countries, including Germany, New Zealand, Portugal and Sweden, South Africa
- In industrialized countries, between 1-17% of adults lack a bank account of any kind
- Countries with low levels of income inequality (measured by Gini coefficients for equivalent disposable income) tend to have lower levels of financial exclusion, while higher levels of exclusion are found in the least equal ones – e.g., Sweden <2% did not have an account in 2000; Germany = 3%; Canada = 3-4%; Belgium = 5%; UK = 7%; US = 9%; countries with highest levels of inequality also have the highest levels of banking exclusion (e.g., in Portugal, about 17% of adult population had no account of any kind in 2000)
- About half of those without an account have never had one
- There is a concern that there may be a group of people who are “under-banked” – i.e., people who have an account but make little use of it
- Growing awareness that people are becoming excluded from banking services because they lack access to banking facilities that are widespread in the rest of society – e.g., in France, key problem is not having access to cheques, which are the most common form of payment; in Sweden, where internet banking is well developed, people without access to a computer face growing difficulties and costs in making payment transfers
- Who are the banking excluded?
 - People living on low incomes, especially if not in employment and living on social security payments from the state (research in Belgium, the UK, the US and Canada have all shown that people with low incomes are also either refused an account outright or advised to go to another bank). In Canada, mystery shopping undertaken for the Task Force on the Future of the Canadian Services Sector showed that refusals continued to be a problem even after a voluntary agreement had been reached with the banks that should have solved the problem (see Department of Finance, Canada, 1998 for source).
 - People on the lowest incomes are twice as likely to be without a bank account as the average
 - People from low-income indigenous and ethnic minority communities have very low levels of engagement with banking
 - At risk of exclusion are people with a history of bad debt, who often have their accounts closed if they fail to reduce their overdraft and then find it difficult to open another one – especially a problem in Sweden and Germany where there is near universal access to banking



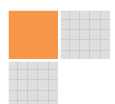
- Age and geographical location are important: the very young and the very old are more likely to be unbanked than the general population, as are people living in rural communities
- **Causes of banking exclusion:**
 - Refusal by banks
 - Evidence that people who have been refused seldom appeal against the decision, even when they have the legal right to do so
 - Identity requirements
 - In countries without a compulsory identity card, many people on low incomes and homeless people and refugees in particular find it very difficult to supply the types of proof of identity required by banks to open an account, made worse by the fact that governments and the banking industry have taken steps to combat money laundering and terrorism
 - Terms and conditions
 - In France, Canada, the USA and Australia, attention has been drawn to the minimum balances required for an account to be opened, which, in many cases, are beyond the budgets of people on low incomes
 - Conditions relating to the use of the accounts
 - E.g., Belgium: accounts have been closed by banks because customers use them too little or withdraw the money in the account too soon after it has been deposited
 - In other countries, banks can impose charges if a minimum balance is not maintained – e.g., in UK, one of the major causes of bank exclusion is that conventional current accounts have no safeguards against unintentional overdrawing. This can lead to unauthorized overdrafts, bounced cheques and failed direct debits which lead to high charges and people closing their bank accounts
 - People on low incomes or with a history of bad debt are offered accounts that either have very limited facilities or have facilities that inappropriate to the needs of someone living on a low income
 - In Canada, there is a problem with “holds on funds” where people with only small balances on their account have government cheques that they have deposited put on hold for a week before the funds are released to their account
 - Bank charges
 - Levels of bank charges can deter customers with low incomes from using transaction accounts – a significant problem in almost all the countries that were studied except for in Britain where transactional banking is free as long as there are sufficient funds to cover the transactions
 - As mentioned earlier, the costs of inadvertently over-drawing, bounced cheques and failed direct debits are a major deterrent to people on low incomes using a bank account to manage their day-to-day finances



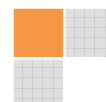
- Initiatives to combat financial exclusion in Australia, Belgium, Canada and the USA have focused on providing low cost bank accounts
- Physical access problems caused by bank branch closures
 - Because of international competition and the economics of international banking, there have been a number of bank branch closures across most developed countries, accelerated by technological developments (cash machines and telephone and internet banking)
 - Closures have tended to hit poor urban neighbourhoods and small rural communities the hardest
 - While there is evidence that lack of physical access to a bank branch greatly increases the psychological barriers from banking, research conducted in both the UK and the US shows that being unable to access a bank branch is not one of the main reasons given by people who are unbanked for lacking an account
- Psychological and cultural barriers
 - In many countries (especially those with higher levels of banking exclusion), self-exclusion by people on low incomes is far more important than direct exclusion by banks refusing to open accounts
 - Psychological and cultural barriers impede the use of banking services in indigenous populations in Australia and Canada
 - In the UK, the Pakistani and Bangladeshi communities face religious barriers to banking because overdrawn bank accounts are 'haram' (forbidden) under Islamic law
- Social security payments
 - Countries like Sweden, Germany and Australia pay social security payments directly into a bank account and have been doing so for some time – these are the same countries with the lowest proportions of people without a bank account
 - In countries like the UK, USA and Canada, payments not been made directly until very recently
 - In UK, being in receipt of social security was strongly associated with being unbanked
 - Concerns about financial exclusion, along with a desire to reduce the costs of social security administration, have encouraged the UK government, US federal and state governments and Canadian provincial governments to move towards making electronic transfer the normal method of payment for all social security benefits
- **Voluntary charters and codes of practice**
 - Most common response to financial exclusion
 - Earliest developed in France in 1992 – committed banks to opening an affordable account with facilities such as a cash card, free access to cash machine network, bank statements and negotiable number of cheques
 - Belgium



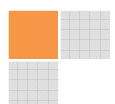
- Established voluntary code of practice in July 1997 by Belgian Bankers Association
 - Provides for basic banking services for people on modest incomes who lack a bank account
- Germany
 - Voluntary code introduced by German Bankers Association in 1996
 - Offers basic banking transactions without an overdraft facility
 - Debate as to whether these 'Everyman' accounts have reduced banking exclusion – some evidence that most of the people opening the accounts are young people and not those on low incomes
- UK and Australia
 - Access to basic banking achieved through voluntary arrangements with banks but not involved formal charters
 - Both countries have a more general Banking Code – a commitment to telling people about basic bank accounts – but not set down features about what accounts should offer
- UK
 - A policy action team put forward a blue-print for a 'basic bank account' which offers a full range of banking facilities but differs from conventional current accounts in that it cannot be overdrawn (all transactions are in real-time) and has a cash card for withdrawing money from cash machines but no cheque book (design based on needs identified by people on low incomes) – all banks complied with
- Australia
 - Proposal by Australian Bankers' Association to Australian Competition and Consumer Commission on behalf of 10 member retail banks to offer generic basic account with certain minimum features was eventually rejected as being 'anti-competitive' as consumer groups demonstrated that some banks already offered basic accounts with better features than those being proposed. In spite of this set-back, all 4 major banks now offer basic bank accounts, some of which go much further than the original generic account proposals.
- Although the above are promising voluntary developments, evidence to suggest that basic accounts are not always promoted to those who most need them. In UK, this led to the strengthening of code provisions related to basic bank accounts in 2005, with further tightening in 2006.
- France and Belgium have turned to the law to enforce previously voluntary charters
- **Legislation**
 - France –



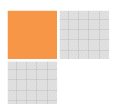
- Law on exclusion of 29 July 1998 reiterated the right to an account first set out in 1984 law and strengthened it with right to basic banking services as well as simplifying the process of exercising the right to an account
 - Therefore, any person with French nationality has the right to open an account at any private or public bank – if refused, they can apply to Banque de France for them to designate a bank that should open an account
 - Decree issued in January 2001 sets out right to simple transactional account with cash card for use at cash machines but no overdraft facility
- Belgium
 - Basic banking bill introduced in 2001, enacted and implemented in 2003
 - Applies to all banks; goes beyond provisions in earlier charter to set out further minimum standards for basic bank accounts (ceiling on charges, minimum number of free face-to-face transactions)
 - Requires banks to contribute to compensation fund to compensate financial institutions that open more than their 'share' of basic bank accounts
 - Stats on the number of basic bank accounts must be communicated to National Bank of Belgium
- US
 - Developments, like banking system, are more fragmented
 - Proposals that banks should be required to offer low-cost chequing accounts (with minimum balance requirements and low fees) for people on low incomes – some states have passed these laws but Federal Government hasn't
- Canada
 - Policy response combines best of developments in other countries
 - Federal government set up a task force on future of Canadian financial services sector – published its first report in 1998
 - In 1999, government responded with a report outlining 57 reform measures which were then included in legislation put before Parliament
 - Bill C-8 enacted in June 2001 and includes new rules to tackle financial exclusion, including rules requiring all banks to provide accounts without minimum opening balances to all Canadians, regardless of employment or credit history, with minimum identification requirements
 - The Act includes rules allowing the Government to make regulations regarding the provision of low-cost accounts
 - Banks were given opportunity to address this issue voluntarily before regulations were introduced
 - 8 banks signed a MOU with the Government pledging to offer low-cost accounts to their customers in 2001 and have recently renewed their public commitment
 - Financial Consumer Agency of Canada monitors whether financial institutions are adhering to their public commitments and report annually to Parliament
- Lessons that can be learnt from these experiences
 - **Summary of barriers to banking inclusion:**



- Features of bank accounts (including terms and conditions and charges)
- The way applicants are screened and vetted
- Physical access problems
- Cultural and psychological barriers
- **Possible solutions**
 - Ensure the availability of simple accounts that are both appropriate and affordable for people on low incomes
 - Maximize advantages of technology to provide appropriate access
 - Encourage take-up of banking services available
 - Involve not-for-profit organizations such as post offices
- **There is a need for low-cost no-frills accounts**
 - All countries studies for the report have needed to reinvent simple bank accounts to achieve banking inclusion
 - These accounts do not have an overdraft facility, have addressed both terms and conditions and charging structures that act as barriers to use by people on low incomes
 - All evidence suggests that people on low-incomes would prefer to have an account that cannot be overdrawn inadvertently as this gives them greater control over their finances
 - A 'no-frills' account overcomes the problems caused by opening an account by conditions such as requiring a minimum balance to open an account and/or a minimum number of transactions to keep it open
 - 'simple' accounts overcome the problem caused by charging structures for each transaction and for failing to maintain a minimum balance and monthly lump sum fees regardless of levels of use. With simple accounts, charged only relate to levels of use.
- **Developments in technology offer solutions and risks**
 - E.g., real-time banking – can be used to prevent unauthorized (and often unintended) over-drawing and allows customers to be in full control of their account
 - Means that credit checks become less important and allows young people to have access to electronic payment (and builds their confidence at a young age)
 - Countries which have developed real-time accounts only for people on low-incomes have created a system with restricted access – e.g., in UK, basic bank accounts have Solo or Electron cards which can be used at all ATMs, but not all retail unit because some of them lack the equipment needed to check accounts on-line in real-time. Unfortunately, as number of people with these types of accounts increase, so do signs outside petrol stations and small retailers which say that they do not accept payments by these cards.
 - Important that technological developments do not create new forms of exclusion – a particular danger of this happening in countries (like Sweden) where internet banking is fast becoming the norm



- **There is a need to encourage the use of banks**
 - Need to be mindful that access to appropriate and affordable banking is only part of the problem
 - In some very highly-banked countries, a number of people with a bank account are making very little use of the services on offer – they would be described as being “under-banked” and share many of the same characteristics as those who are unbanked in other countries
 - Important to address the underlying reasons for people being unbanked. E.g. In a number of countries that decided that wages and/or all state benefits and pensions would be paid into a bank account before addressing the need for accounts that were appropriate to the needs of people on low-incomes
 - If banks are seen as being mostly for the better-off, then people on low-incomes will be reluctant to use them
 - Experience shows that there is a need to promote the use of banking services as well as increase access to them
- **Not-for-profit organizations can have an important role to play**
 - Levels of banking exclusion tend to be lower where not-for-profit organizations (e.g., post offices) play a role in delivering banking services – because they have a much larger network of outlets and partly because poor people see them as more user-friendly
 - Important that such not-for-profit organizations are fully integrated into the systems for electronic transfer of funds used by banks – otherwise, people using the banking services will still remain on the margins of the banking system
- **Achieving universal access to banking**
 - Ideally everyone’s banking needs would be addressed
 - However in reality, some intervention is needed to ensure that appropriate provision is made for people on low incomes
 - Britain – voluntary agreement; Belgium – legislation; Canada – legislation underpinning a voluntary agreement
 - Least successful – legislation conferring right to a bank account without ensuring that appropriate accounts are in place or on relying on consumers themselves to seek redress
 - Experience shows that careful monitoring of compliance is more important than whether self-regulation or legislation has been used
 - Need for an independent body to monitor the extent to which banks have genuinely removed barriers to access, have developed an appropriate account and promoted it to the people who might benefit





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