# Fringe Lending and "Alternative" Banking: The Consumer Experience

Written by Sue Lott and Michael Grant
Public Interest Advocacy Centre
1204 - ONE Nicholas St.
Ottawa, Ontario
K1N 7B7

November 2002

*With Funding from Industry Canada*

The Public Interest Advocacy Centre
(PIAC)
Suite 1204
ONE Nicholas Street
Ottawa, ON
K1N 7B7

Canadian Cataloguing and Publication Data

Lott, Susan
Grant, Michael

Fringe Lending and "Alternative" Banking:
The Consumer Experience

ISBN 1-895060-58-3

## Table of Contents

## Executive Summary

This report examines the recent growth of the alternative financial sector or "AFS". Specifically it looks at the current state of the alternative financial services industry and some of its key characteristics. The report also describes findings from a household survey of users of the AFS and the results of focus group discussions undertaken for this report. The report analyses key findings from the survey in light of options for regulatory and legislative responses to the industry and offers recommendations for policy makers.

The term AFS describes the financial services sector that lies outside mainstream, traditional financial institutions such as banks and credit unions. It includes cheque cashing, payday loans, pawnbrokers, rent-to-own stores, tax rebate discounting, loan brokers, and finance companies.

**Focus on payday loans**
The payday loan industry is the focus of this report because it is the most recent and fastest-growing sector of the AFS and poses the greatest financial risk to the borrower.

Payday loans are short-term cash loans, usually in the $100-$200 range, which are advanced in return for a post-dated cheque or a delayed automatic debit and which includes a fee. The term of the loan is usually 14 days or less. When the loan becomes due, the cheque may be either redeemed in cash or deposited. If the borrower is not able to pay off the loan in full, the loan is often extended, for a fee, which is called a "rollover" of the loan. It is this "rollover" element of the payday loan, which creates a significant financial risk for the borrower.

**Key issues**

**Growth of the industry**
The AFS in general and the payday loan industry in particular have had an explosive growth in the U.S. and Canada. It has been estimated that in the U.S. alone, the number of payday lending companies increased from 300 in 1992 to approximately 8,000 by 1999. Although there are no specific statistics on the growth in Canada, Dollar Financial Group, which represents over 60 percent of the cheque-cashing stores in Canada through its subsidiary Money Mart, reported that the face value of the cheques cashed through its outlets more than quadrupled from 1995 t o 1999, to just over $2.3 billion (U.S.). It is also a highly lucrative industry.

**Financial vulnerability of consumers**
High debt-to-income ratios of consumers and the declining ratio of savings to disposable income are two related phenomena that have contributed to the

increasing financial vulnerability of consumers and the growth of the AFS in Canada and the U.S.

**High interest rates and fees for services**
The fees and service charges attached to payday loans have been determined to be "interest", by a series of recent judicial decisions in Canada. This brings payday loans within the provision in the *Criminal Code* of Canada which describes the offence of a criminal interest rate being interest attached to a credit agreement or arrangement which is over 60%. An interest rate is commonly expressed as an annual percentage rate. The fees and service charges attached to payday loans may range from 300% to over 1000%, rendering them illegal under the *Criminal Code.*

**Rollovers**
The risk of entering into a cycle of renewals of a payday loan, due to the short term of the loan and the high cost of the loan, is one of the most controversial features of payday loans. There is debate between the industry and its critics over the extent to which customers engage in rollovers or loan renewals.

**Absence of strong regulatory responses**
The regulation of consumer credit and financial services falls under federal and provincial jurisdiction. Legal responses to payday lenders include legislation at the federal and provincial/territorial level to control interest rates, license payday lenders or regulate their practices, and disclose information.

The only current statutory control of interest rates is section 347 of the *Criminal Code*. Non-legislative responses may include the application of the common law doctrines of fraud, deception or unconscionability. Despite the presence of legislation and judicial decisions in these areas, regulatory attention to the payday loan industry in Canada has been minimal to non-existent.

**Other jurisdictions**
The report examines briefly the development of payday lending in the U.S. and Australia. The report focuses on the way in which the development of the payday industry and the nature of financial legislation have contributed to the intensity of litigation and consumer activism on payday lending in the U.S. Australia has noted parallels between itself and Canada with respect to the key issues identified by the Canadian research.

**Key findings from household survey**
A telephone survey was undertaken during September – October 2001 and involved a random sample of Canadian households. Out of 4,206 contacts, 202 completed in-depth interviews.

**How many people use alternative financial services?**
Incidence rate for the AFS in the last three years is 4.8% or between 1.0 million and 1.4 million Canadians.

**Who are the users of the AFS?**
The users of alternative financial services, with the exception of pawnshop customers, look like average Canadians, in terms of age, gender, and household income. A majority of AFS customers are employed and have a high school education. They are similar to average Canadian in that they have bank accounts but have a significantly lower usage of credit cards than the average Canadian.

**What are their reasons for using the AFS?**
The major reason for using the AFS is to meet day-to-day needs. The majority of respondents indicated that they did not have enough or had just barely enough cash at the end of their pay period to meet their needs.

**Financial literacy**
Most AFS customers are unaware of the cost of the services they use, whether cheque cashing or payday loans. AFS customers tend to emphasise the service aspects of the AFS as the major reasons why they choose these services over mainstream financial services.

**Repeat usage**
The majority of payday loan customers have had some experience with rolling over their loans, and 30% indicated that they had sometimes or frequently used the same source for more than one pay period in a row.

**Significance of the survey findings**
There are five significant findings of the survey for policy makers:

1) The key factors contributing to the usage of the AFS are Canadians' growing dependence upon credit and the stagnating incomes of the majority of Canadians.
2) A general lack of financial literacy is a major contributor to AFS usage.
3) Although not in the majority, a significant percentage of AFS users are engaging in high-risk repeat usage of payday loans.
4) AFS customers would not turn to more extreme forms of lending such as loan sharks if payday loans were prohibited.
5) AFS customers have turned away from mainstream financial institutions, emphasising the service aspects of the AFS as the major reason for their preference.

## Recommendations

### Financial Literacy

- Enact and update provincial disclosure of cost of credit legislation to apply to the AFS.
- Support and maintain credit-counselling services.
- Increase the availability and access to profession financial advice for all consumers, including those of modest incomes.
- The Financial Consumer Agency of Canada, whose mandate includes providing consumer education about financial matters, should publish information about the AFS and payday loans, in particular, comparing the APRs of these services with alternatives. It should also inform consumers about consumer protection measures relevant to the AFS.

### Legislative/Regulatory Responses

- Mainstream financial institutions must improve their approach and expand their services to their small volume customers as well as non-bank customers. This requires offering basic banking services and maintaining branch locations, as well as improving their services to existing small volume customers such as small-loan lending, lines of credit and overdraft protection.
- Ensure the provincial and territorial consumer protection framework applies to the AFS. This would first require conducting an inventory of all consumer protection statutes and regulations, cost of credit disclosure legislation, unconscionable transactions and trade practices legislation to determine the extent to which the current consumer protection framework is applicable to the AFS. Provinces and territories must then update this framework to ensure it applies to the AFS.
- License the AFS in order to address the core practices that have raised the concerns about the AFS in general and payday loans in particular, the high and disguised fees attached to the AFS and the repeat usage of payday loans.

## Introduction

The growth of an alternative financial sector ("AFS") or an alternative consumer credit market has been a developing concern for governments and consumer activists in a number of countries over the last few years. The term AFS loosely describes a financial industry that lies outside of mainstream, traditional financial institutions. The alternative financial sector offers financial services, which include:

- Cheque cashing – cheques are cashed for a fee
- Payday loans – cash advances based on a personal cheque, which includes a fee, held for future deposit , usually on the borrower's next payday
- Pawnbrokers – cash is advanced against personal items left as security
- Rent-to-Own stores – goods are leased on a weekly or monthly basis with the possibility of eventual ownership of the goods
- Tax rebate discounting – individuals are provided with an advance on their tax refund
- Loan brokers – offer to act on behalf of a consumer in obtaining a loan
- Finance companies – non-deposit-taking institutions which also offer refinancing of existing loans

A key characteristic of the AFS is that the industry targets primarily low-income individuals and those individuals with poor, faulty or non-existent credit ratings. This market has traditionally been characterised by subprime[1] lenders.

The alternative financial services industry is both candid and unabashed about its targeted approach to a very specific market:

> The Company's primary customers are working, lower-income individuals and families who require basic consumer financial services and are under-served by traditional retail banking networks…Management believes that growth in the lower-income segment of the population combined with the decreasing availability of traditional retail banking services, provides the Company with significant growth opportunities…The Company has carefully chosen metropolitan areas with growing low-income

[1] Subprime lending refers to an interest rate that is below the prime rate charged by a lender to its most credit worthy customers. Subprime loans have historically been made to borrowers with blemished or non-existent credit records and the borrower is charged a higher fee to compensate for the greater risk of default and the higher costs of loan servicing and collection.

> populations. Within the markets served by the Company, the Company’s stores are located in desirable locations near its targeted customer base.[2]

The alternative financial sector has had a swift and explosive development in North America. In little over 10 years, it has gone from a non-existent industry to approximately 10,000 cheque cashing stores in the U.S. alone, by January 2001.[3] In 1998, one of the largest national chains in the U.S., Ace Cash Express, reported revenues from loan fees of $100 million – an amount that had doubled in a period of only two years.[4]

There are no specific statistics on the growth of the industry in Canada, but overall statistics from corporations who operate in both Canada and the U.S. suggest that the Canadian expansion has also been exponential. Dollar Financial Group[5], which through its subsidiary Money Mart, represents over 60 percent of the cheque-cashing stores in Canada, reported that the face value of the cheques cashed through its outlets more than quadrupled from 1995 t o 1999, to just over $2.3 billion (U.S.).[6]

It has also become a highly lucrative business. From the period June 30, 2000 to June 30, 2001, a total of 9,406,749 cheques were cashed through Dollar Financial Group, with an average fee per cheque of $11.24.[7] U.S. consumer advocates have suggested that payday loans have become a billion-dollar business, with approximately 65 million transactions a year generating an estimated $2.4 billion in fees in 2001.[8] Some observers have suggested that the return on equity[9] for these businesses may range from 23 percent to as high as 35 percent, compared to a range of returns of 13 to 18 percent for traditional consumer lenders.[10]

---

[2] Dollar Financial Group, Inc. *Annual Report to the Securities and Exchange Commission for the Fiscal Year Ended June 30, 2001* at 3-4.
[3] *Ibid.* at 4.
[4] P. Kilborn, “New Lenders with Huge Fees Thrive on Workers with Debts” *The New York Times* (18 June, 1999) A1.
[5] Dollar Financial Group is the corporate owner of Money Mart, a cheque-cashing and payday loan outlet that represents 60% of such stores in Canada and is the second largest company in the U.S.
[6] S. Kari, “Street Smart” *Report on Business Magazine* (April 2000) 100.
[7] Dollar Financial Group, *supra* note 3 at 9.
[8] J.A. Fox, “The Debt Cycle: Using Payday Loans to Make Ends Meet” (February 28, 2002) NEFE/CFA Forum at 1.
[9] Return on equity is the amount earned on each dollar of invested capital expressed as a percentage.
[10] B.I. Koerner, “Preying on Payday” (May 2001) 26 *Mother Jones* 19; D. Foust, “Easy Money” *Business Week* (24 April 2000) 108.

The first comprehensive analysis of this phenomenon in Canada was a 2000 study by Iain Ramsay funded jointly by the Office of Consumer Affairs, Industry Canada and the Ministry of the Attorney General, British Columbia.[11]

Ramsay approached the subject of AFS by examining the growth of consumer vulnerability in relation to credit markets. He began by identifying a number of economic trends influencing the vulnerability of consumers: high debt-to-income ratios, the declining ratio of savings to disposable income, declining consumer access to traditional financial services, changes to the financial services market resulting in two-tiered customer marketing to either high-income or low-income customers, and racial discrimination in financial services. [12]

Ramsay suggested that the growth of an alternative financial sector was the direct result of this combination of factors. He then examined each of the various sectors of the industry and found that they had some common characteristics:

- Individual consumers pay much higher prices for goods and services in this sector
- There is some evidence of fraudulent selling practices and oppressive collection tactics in the mainstream and alternative financial sector
- Fewer resources in Canada are devoted to monitoring and policing the AFS than middle income markets
- Regulatory enforcement is challenged by the ability of financial services industry to restructure transactions to avoid regulation and the low costs of entering and exiting this market
- The growth of the AFS may be directly tied to the withdrawal of services to low income consumers by mainstream financial institutions[13]

Ramsay's report gave a brief overview of existing legal measures that have been employed to regulate or respond to the AFS in Canada and the United States.

Ramsay also addressed the issue of why individuals use alternative financial services. He suggested a number of possible reasons: lack of access to the 'mainstream' financial sector, individual choice, the phenomenon of "market irrationality" by certain classes of consumers, and consumer choices based on habit and convenience.[14]

[11] I. Ramsay, "Access to Credit in the Alternative Consumer Credit Market". Paper prepared for the Office of Consumer Affairs, Industry Canada and the Ministry of the Attorney General, British Columbia February 1, 2000.
[12] *Ibid.* at 1-2.
[13] *Ibid*. at 5.
[14] *Ibid.* at 17.

Ramsay was unable to draw any conclusions about motivation behind use of alternative financial services, as there has been little empirical research in Canada to draw on. He indicated that this kind of research was needed in order to develop appropriate public policy responses:

> It is obviously important to understand which is the primary reason for usage of the alternative financial sector because each reason might suggest a different policy response. If low-income consumers have no real choice in relation to credit, because of their life situations, this would suggest, for example, that disclosure legislation would be of modest assistance to them. It is necessary to attempt to expand their choice set, perhaps by encouraging new institutions to enter the market.[15]

Thus the impetus behind this report, which examines the results of a national survey of Canadian consumers of alternative financial services, was to know more about the users of these services and their reasons for turning to the AFS. This information will assist policy makers in knowing what, if any, are the most appropriate and effective public responses to the AFS.

This report also responds to the developing concern about the recent growth and expansion of the AFS industry in Canada. This is reflected in media reports and a joint statement in 2001 by the federal and provincial/territorial consumer affairs ministers expressing the need for future action with respect to the alternative consumer credit market.[16]

## *1.1 The Focus of this Report*

Researching a topic such as the characteristics of users of alternative financial services poses a fundamental challenge to the researcher, given the essentially private nature of personal financial transactions and the broad range of transactions that fall under the term "alternative financial services". The survey, therefore, focused on some specific sectors with the AFS: cheque cashing, payday loans, finance companies and pawnbrokers.

The payday loan industry appears to be the most recent and most quickly growing sector of the alternative financial services industry.[17] It is also the sector that the least is known about and involves practices that may pose the highest risk to consumers.

---

[15] *Ibid.*
[16] Minister of Industry, News Release, "Consumer Ministers Take Action to Improve Consumer Protection in the Evolving Marketplace" (25 May 2001).
[17] I. Ramsay, *supra* note 11 at 7.

The fees attached to the payday loans have been deemed to constitute interest at annual percentage rates that are usurious[18] or fall within the criminal interest rate provision of Canada's *Criminal Code.*[19] In addition, payday loans may involve the phenomenon of "rollovers", in which the borrower is pulled into a series of repeated loan transactions that may be financially devastating to the borrower.

Payday loans or cash advance loans[20] have been described as:

> Payday lenders make short-term cash loans – generally by taking a post-dated check from which they withhold a fee, and advance the remainder in cash. Some transactions use delayed automatic debit agreements instead of checks. Deposit of the check or automatic debit is deferred for an agreed-upon time, which may be tied to the next payday…The process works like this: If you want to borrow $100 and the fee is $15, you give the lender a check for $115, post-dated to the end of the loan term. The lender gives you back $100 in cash. When the loan becomes due, you can go back and give the lender $115 in cash or money order to redeem the check, or you can let the lender deposit your check to pay it off. If you cannot pay it back in the short turnaround time, you can pay another $15 fee to extend it.[21]

Payday loans have recently attracted both judicial and regulatory attention in the United States. In contrast, there has been very limited judicial and regulatory attention to this phenomenon in Canada. But the extraordinary growth in this industry has begun to attract media attention and some interest by government. As indicated above, in 2001 federal, provincial and territorial governments expressed a joint intention to take action concerning the payday loan industry

The recent growth and expansion of payday loans, the lack of regulatory attention in Canada, the high levels of interest generated by the fees attached to payday loans and the risk element entailed in the "turnover" aspect of payday loans, are key issues and were determining factors in focusing this research primarily on the payday loan sector.

[18] Usury is defined as interest in excess of a legal rate charged to a borrower for the use of money. [source: Merriam-Webster's Collegiate® Dictionary]

[19] R.S.C. 1985, c. C-46, s. 347.

[20] A payday loan has also be described as: payday advance, pay cheque advance, deferred deposit, deferred presentment, pay cheque loan, cash advance, post-dated cheque advance, sale/leaseback, purchase/rental, short term personal loan, and signature loan.

[21] L. Drysdale & K. Keest, "The Two-Tiered Consumer Financial Services Marketplace: The Fringe Banking System and Its Challenge to Current Thinking About the Role of Usury Laws in Today's Society" (2000) 51 South Carolina Law Review 589 at 600-601.

## *1.2 Payday Loans - Key Issues*

### ***1.2.1 Growth of the Industry***

As indicated above, payday loans have recently attracted the attention of media, consumer advocates and regulators because of the phenomenal growth in the AFS industry overall. The Canadian website for Money Mart, one of the largest payday loan companies in Canada and the U.S., proclaims that it has over 250 outlets, over one million registered users (of cheque cashing services and cash advances) and over $4 billion in total transactions annually.[22]

It has been estimated that the number of payday lending companies in the U.S. alone increased from 300 in 1992 to approximately 8,000 by 1999.[23]

Not surprisingly, this numerical growth has been accompanied by exceptional financial results. It has been suggested that if the subprime lending industry overall were a single financial institution, it would be one of the largest banks in the U.S., with over $400 billion in assets, compared to $183.2 billion in consumer loans for Bank of America Corp., the largest retail bank in the U.S.[24]

It is also important to note that the number of participants in the industry is increasing. In addition to stand-alone companies and large franchises in the AFS, banks are increasingly entering the payday loan business, either through directly offering payday loans or by partnering with large payday loan companies.

In the U.S. national banks and state-chartered banks have linked with payday loan companies to offer payday loans. The Eagle National Bank in Philadelphia entered into a partnership with Dollar Financial Group, where it funded and processed payday loans:

> "We provide the loans and they find the customers," says Eagle President Murray Gorson, noting that this partnership has been going on for six years.
>
> "We wouldn't be doing this if it weren't profitable. A few years ago there were only couple of banks doing this, but now more and more are. I keep hearing from national banks who want to get into this."[25]

In 2000, the Federal Comptroller of the Currency in the U.S., citing regulatory violations, terminated this partnership.[26] However, Dollar Financial Group seems

---

[22] http://www.moneymart.ca/ (date accessed: August 13, 2002).
[23] P. Kilborn, *supra* note 4.
[24] D. Foust, *supra* note 10 at 108-109.
[25] K. Lydersen, "Payday Profiteers: Payday Lenders Target the Working Poor" Multinational Monitor (October 2001) 9.

to be continuing the partnership model. In its 2001 annual report to the Securities and Exchange Commission, it indicated it has partnerships with banks through its subsidiary moneymart.com™, in which it offers payday loans through 798 independent agents in 41 states.[27]

A 2001 survey conducted by the Consumer Federation of America and the U.S. Public Interest Research Group found four national banks and five state chartered banks linked with payday loan companies.[28] This is very much a live issue, as these partnerships have resulted in pending litigation and class actions lawsuits in a number of states.[29]

There is further evidence of practices going well beyond mere partnerships. In Illinois, the parent company of the payday loan company, Check 'n Go has recently applied to the Federal Reserve Bank of Chicago to purchase the Bank of Kenney in Illinois.[30]

Banks also benefit financially from these partnerships. Republic First Bancorp. Inc. of Philadelphia has entered the payday lending business with lucrative financial results:

> It is attracted to these businesses, of course, because of fee income. It attributed more than 50% of its $888,000 of first-quarter net income to payday and tax-anticipation lending, and Harry Madonna, the company's president and chief executive officer, said he is actively seeking new partners in each.[31]

Payday lenders obtain charters in states with no payday loan regulation or partner with banks in states where the payday lender's terms would otherwise be illegal. In most partnerships the bank holding the charter makes the loan, but sells the accounts receivable almost immediately back to the payday lender, thus taking the accounts off their books.[32] The result is that payday lenders are effectively 'renting' bank charters, which allow them to operate in states where the fees attached to their loans might otherwise be deemed illegal under state laws.

---

[26] M. Lynch, "Legal loan sharking or essential service? The great "payday loan" controversy" Reason (April 2002) at 38.
[27] Dollar Financial Group, *supra* note 2 at 3.
[28] Consumer Federation of America & U.S. Public Interest Research Group, "Rent-A-Bank Payday Lending: How Banks Help Payday Lenders Evade State Consumer Protections" (November 2001) 21.
[29] See *Ibid*. at 15-25 for a detailed description of litigation in a number of states.
[30] B. Jackson, "Can't Rent? Payday Shop Files to Buy a Charter" *American Banker* (9 July 2002).
[31] J. Reosti, "Why Republic First Still Likes Tax, Payday Loans" *American Banker* (2 July 2002).
[32] L. Drysdale, *supra* note 21 at 646-647 and J. Reosti, *Ibid.*

Critics have also argued that the payday loan industry uses the "bank model" as a double-edged sword by:

> …urging state legislators to legalise payday loans to "keep out" the out-of-state banks and provide "competition" for banks. Then, when industry-friendly laws are enacted, some payday lenders partner with out-of-state banks to by-pass the limits in the new payday loan law. For example, ACE Cash Express was a leader in enacting the Colorado payday loan law, then dropped its state license, claiming its loans were made by a national bank.[33]

Another recent development has been the growth of payday loans offered over the Internet. These loans are the same as other non-electronic payday loans in terms of the process and the fee structure with the obvious exception that the application is done on-line and the funds are electronically deposited into the customer's account.[34]

It can be argued that an Internet payday loan has the potential to be much riskier to the consumer, due to ease of application and in particular, the ease of the loan extension process. In fact, one Internet payday loan company encourages loan extensions by defining the initial *loan process itself* as a loan extension:

> Every customer is required to submit a payment request **ONLINE**. You must agree to this before you can be approved. All requests must be submitted **2 BUSINESS DAYS** before your due date. A payment request is simply an electronically submitted form which notifies us how much you wish to pay when your due date arrives. Further, a payment request is equivalent to a loan extension.[35]

As consumer access to the Internet increases, this Internet offshoot of the payday loan business seems likely to expand rapidly.

### *1.2.2 Increasing Financial Vulnerability of Consumers*

Ramsay suggested that two of the economic trends influencing the vulnerability of consumers was the high debt-to-income ratios of consumers and the perhaps related phenomenon of the declining ratio of savings to disposable income.

Recent statistics suggest that a high level of consumer debt is a growing trend in Canada and the U.S. It is likely that this phenomenon is also a contributing factor to the rapid growth in the AFS.

---

[33] Consumer Federation of America, *supra* note 28 at 16.

[34] A single on-line search for Canadian payday lender web sites turned up 14 such sites (date accessed: 16 August, 2002).

[35] My Payday Loan.com, online: http://www.mypaydayloan.com/faq.htm

Recent surveys of Canadian income trends and Canadians' own views of the their economic security suggest that the financial vulnerability of low income Canadians is increasing, a phenomenon characterised by stagnating incomes and accompanied by high levels of household debt.

Historical income trends indicate that the incomes of Canadians at the lower end of income distributions have been stagnant. Between 1984 and 1999, the net worth or financial wealth of the bottom 75% of families did not increase, while the net worth of families at the top end of income distributions increased by 14%.[36] In 1999, the typical low-income family had only $300 in savings to protect it against an unexpected financial emergency and 75% had less than $6,000 in assets that could be liquidated in an emergency.[37]

Research by the Canadian Council on Social Development ("CCSD") suggests that the financial vulnerability of the average Canadian is increasing, due to an extraordinary increase in household debt. Since 1984, the amount that Canadians borrowed, on average, to buy homes and consumer goods increased from 56% of their total disposable income to 98% by 2001.[38]

As Ramsay suggests, high debt to income ratios raise concerns where disposable incomes are not increasing and where the debt is not incurred to buy an asset of significant value such as a home, but simply to make ends meet. The CCSD survey suggests that these debts are increasingly being incurred to make ends meet.

There is further evidence for the concern that debt is being incurred to make ends meets from Canadians' own perception of their financial vulnerability. In 2001, one-fifth of households with incomes under $20,000 a year indicated that they had insufficient savings to sustain themselves beyond one month.[39]

Research in the U.S. suggests a very similar trend concerning the proportion of debt to income ratios by American consumers. From 1995 to 1998, the proportion of families with high payment to income ratios (greater than 40 percent) increased across every income category, with the greatest increase among households with annual incomes of less than $50,000.[40]

---

[36] Statistics Canada, *The Daily* (18 July 2002) at 13.
[37] *Ibid.*
[38] Canadian Council on Social Development, *The Personal Security Index, 2002: After September 11th* at 17.
[39] *Ibid*. at 18.
[40] J.A. Fox, *supra* note 8 at 3.

Americans also exhibit similar patterns of dramatically reduced levels of savings. The percentage of Americans' disposable income that is saved dropped from 6% in 1989 to 0% by 1999. [41]

### *1.2.3 High Interest Rates and Fees for Services*

Payday loans have attracted the attention of legislators, consumer advocates and the media because they involve fees that constitute interest rates[42], which may range from 300% to over 1,000%, depending upon the cost of the loan, the length of the loan, and the number of other fees attached to the loan.[43]

A brief sample of payday loan fees on-line web sites suggests interest rates within these ranges of 300% to over 1000%. The terms of the loans also reveal a complex variety of "fees" and "interest rates" attached to these loans. To receive a $100 loan from Money Mart for a term of 7 days would cost $119.02. This consists of "interest" of $.89, a "standard first party cheque-cashing fee" of 2.99% of the advance, plus $14.99 which is described as the "per item fee".[44]

Other payday loan web sites advertise flat fees of 20% to 25% of the amount borrowed and percentage fees that decline as the amount borrowed increases (i.e. 25% on $100, 22.5% on $200 borrowed, 21% on $300 borrowed, etc.). Another company's payday loan charges are made up of a "verification fee", interest and a "defined benefit plan", which is described as a protection plan, covering such contingencies as the customer's inability to repay the loan due to job loss, disability or illness.[45]

#### Criminal Interest Rate

The *Criminal Code* of Canada defines a criminal interest rate as being over 60% and deems it an offence to enter into an agreement or arrangement to receive interest or a portion of interest at a criminal rate. Under section 347, a "criminal rate" is defined as "an effective annual rate of interest calculated in accordance with generally accepted actuarial practices and principles that exceeds sixty per cent on the credit advanced under an agreement or arrangement".

[41] P. Kilborn, *supra* note 4 at A28.
[42] An interest rate is the percentage of an amount of money, which is paid for its use for a specified time and is commonly expressed as an annual percentage rate ("APR"). [Source: H. Black, *Black's Law Dictionary* (St. Paul: West Publishing, 1991) at 562].
[43] Ramsay, *supra* note 11 at 9. Ramsay uses a nominal annual percentage rate rather than the effective annual interest rate required by the definition of criminal interest rate in section 347 of the *Criminal Code*; the effective annual interest rate would be higher still.
[44] http://www.moneymart.ca/
[45] http://mypaydayloan.com/, http://www.cashx.ca/, http://www.cashfactory.ca/. http://www.canadianchequeadvance.ca/

The payday loan industry argues that their 'fees' do not constitute 'interest' and are therefore not offences as defined by section 347. As indicated above, Money Mart distinguishes "fees" from "interest", indicating that it charges an effective annual interest rate of 59% on its loans which works out to $.89 on a $100 loan for one week. Not surprisingly, this rate is set just below what would be considered a criminal rate of interest.

However, judicial interpretations of section 347 support the argument that the fees and charges associated with payday loans constitute "interest". It is important to note that phrase "credit advanced" which is used in the definition of "criminal rate" (see above) is defined as:

> The aggregate of the money and the monetary value of any goods, services or benefits actually advanced or to be advanced under an agreement or arrangement minus the aggregate of any required deposit balance and any fee, fine, penalty, commission and other similar charge or expense directly or indirectly incurred under the original or any collateral agreement or arrangement.

In *Garland* v. *Consumers' Gas Co.*[46] the Supreme Court affirmed a broad interpretation of section 347.[47] The issue before the Court was whether a late payment penalty applied by a utility company against a customer constituted "interest" under section 347, requiring the Court to interpret the scope of the provision. The Court concluded that in adopting this section, Parliament had opted for an inclusive concept of "interest" which would encompass the notion of the "cost of the loan" derived from the legislation that section 347 had replaced, the *Small Loans Act*[48]:

> The broad language of s. 347 was presumably intended (as it was in the *Small Loans Act*) to prevent creditors from avoiding the statute simply by manipulating the form of the payment exacted from their debtors…It is the substance, and not merely the form, of a charge or expense which determines whether it is governed by s. 347.[49]

The Court also stated:

> …Parliament expressly expanded the meaning of interest under s. 347 to include one-time charges, whether payable at the outset of a transaction (e.g. fees and commissions) or after repayment is due (e.g. fines and penalties).[50]

---

[46] [1998] 3 S.C.R. 112.
[47] See also, H. Reid's analysis of the applicability of *Garland* to consumer transactions. H. Reid, *A Garland for Consumers: Will the Garland Case Provide Safeguards for Vulnerable Consumers?* (Ottawa: Public Interest Advocacy Centre, 2000).
[48] R.S.C. 1970, c. S-11.
[49] *Garland, supra* note 46 at para. 28.
[50] *Ibid.* at para. 29.

Recent case law has suggested that the courts are applying this interpretation of section 347 to civil actions involving payday loans and are disallowing the loans in their entirety or severing the criminal interest portion of the fees attached to such loans.

In three recent cases in Alberta, the provincial court interpreted section 347 with respect to a payday loan in accordance with *Garland* and held that the "fee" attached to the loan was "interest" under section 347. In *Dean's Cash Connection Ltd.* v. *Nelson-Wiger*[51] the court held that the $25 fee which had been applied to an 11-day loan of $100 created an effective annual rate of interest which was approximately 800%, far exceeding the criminal rate of 60%. The court severed the interest portion of the transaction from the principle of the loan and disallowed the $25 fee under section 347 of the *Criminal Code*.

In *Cash Store (Advance Finance Co.)* v. *Lajoie*[52] the court considered whether a series of fees attached to a payday loan described as "broker fees" were "interest" pursuant to section 347. The court held that they were "interest" and further held that the interest charges applied to the loan, based on an annual interest rate of 59% were unconscionable[53], being "sufficiently divergent from community standards of commercial morality that they should not be enforced".[54]

In this case, the court did not sever the illegal, interest portion from the principle part of the loan. It noted that the borrower had already made a series of payments, which amounted to $691.81 on a $400 loan. It also indicated that the parties did not appear to be sophisticated and of equal bargaining power (one of the criteria to be considered in deciding whether to refuse to enforce an illegal contract or to enforce all but the illegal portion). The court simply dismissed the payday loan company's claim of $657.14 for further charges and interest.

*Affordable Payday Loans* v. *Harrison*[55] affirms not only the application of section 347 to payday loans but also illustrates the extraordinary risk element of rollover of payday loans. In this case, the plaintiff (the payday loan company) claimed the balance owing in respect of two loans. The balance included "charges" that the court held was usurious. It therefore disallowed the balance that included such charges, allowing only a single NSF fee, which it determined did not come within the definition of "interest" in section 347 of the *Criminal Code*. The defendant counterclaimed over loans that had been rolled over or repeated over a *16-month period*. The court allowed the defendant's claim for all the interest paid above the criminal interest rate.

---

[51] [2001] A.J. No. 246, online: QL (CJ).
[52] [2002] A.J. No. 780, online: QL (CJ).
[53] This conclusion was based on the *Unconscionable Transactions Act,* RSA 2000, c. U-2.
[54] *Cash Store, supra* note 52 at para. 27.
[55] *Affordable Payday Loans* v. *Harrison*, [2002] A.J. No. 824, online: QL (ABPC).

In a recent Manitoba case[56], the court held that an "administration fee" attached to a short-term loan (six months) together with the repayment terms constituted a criminal interest rate of 80%. The court disallowed the entire amount of the loan, indicating that it was necessary to make a strong public policy statement about criminal interest rates, in accordance with the public policy objective behind section 347:

> The charging of a criminal interest rate is not a technicality. It is illegal and demands close scrutiny by the courts. This is particularly so when the plaintiff is in the business of making short term small loans to unsophisticated customers. I say unsophisticated because, although no evidence was lead specifically on this point, it is reasonable to infer that customers of such loans are not sophisticated borrowers. They are often in difficult, if not desperate, financial situations. That is why they are high-risk loans.[57]

These cases clearly indicate that the courts are applying the broad definition of interest as interpreted by the Supreme Court in *Garland* to the fees and charges associated with payday loans. The decisions also reinforce the courts' concern regarding the generally inequitable nature of the payday loan transaction and the corresponding affirmation of the public policy objective behind section 347, to protect the public from usury.

### The Industry's Response

The industry argues that the use of the annual percentage rate ("APR") is an inappropriate measure for a short-term loan, because it wrongly implies that the product is being marketed as a long-term financial option. One industry representative stated that "[U]sing an APR analysis on deferred deposit transactions is like going to a cabdriver in New York and asking the fare to San Francisco."[58]

Critics respond that the purpose behind establishing standardised pricing of credit in terms of annual percentage rates provides the only way for consumers to be able to compare the relative costs of credit.[59] It is also clearly been adopted as the standard for regulations that deal with the mainstream financial services sector. Federal regulations governing disclosure of interest rates relating to deposit accounts and credit agreements made with federally regulated banks require these costs to be expressed as annual percentage rates.[60]

---

[56] *C.A.P.S. International Inc.* v. *Kotello*, [2002] M.J. No. 205, online at: QL (MBQB).
[57] *Ibid.* at para. 34.
[58] Comment by Robert E. Rochford, deputy general counsel to the National Check Cashers Association in "Legislators Review Payday Lending Practices" (2000) 26 *State Legislatures* 9.
[59] L. Drysdale, *supra* note 21 at 603.
[60] See SOR/92-321, s.3 and SOR/2001-101, s. 3.

The industry also argues that their fees compare favourably with the high cost of NSF (non-sufficient funds) cheques charged by merchants and by banks, which together may amount to twice the fees applied to a payday loan.

Critics respond that using a payday lender doesn't necessarily avoid a NSF fee. Some payday lenders also use the leverage of applying a NSF fee on top of other fees, in order to ensure the borrower contacts them for a loan extension if they are unable to pay back the full amount of the loan.[61] An in-depth interview with a former Money Mart manager, which was part of the focus group interviews of this report, suggested that it is a management practice to ensure that "a certain number of cheques "go NSF"".[62]

Finally, the industry argues that their fees are justified by the credit-risky nature of their customers and the high default rate on loans.[63] However, the industry's own figures suggest otherwise. The risks and default rates in this industry appear to be very low.

For Dollar Financial Group's fiscal year ending June 30, 2001, the net write-offs as a percentage of the face amount of cheques cashed were 0.26%. Loan losses as a percentage of original loans and extensions of payday loans were only 1.4%.[64] A publication put out by a member of the industry concerning the payday loan business estimated bad debt rates of 1% on the face amount of cheques processed, or 8% of revenues lost to bad cheques.[65]

### *1.2.4 Rollovers of Payday Loans*

The rollover or extension of an original payday loan is one of the most controversial features of payday loans because it carries great financial risk for consumers and is perhaps the key to the lucrative nature of the business for lenders.

As the time frame of the loans are so short and the costs of the loan are so steep, many borrowers may find that they are unable to pay the loans off in full when they come due. The borrower then enters into a cycle of renewals or new loans with other lenders, with increased fees, interest, and possible NSF charges added on and no reduction in the principle of the loan. This situation may be financially devastating for the borrower. Borrowers renewing loans over time

[61] Drysdale, *supra* note 21 at 606; http://www.1-payday-loans-cash-advance-personal-fast-cash-payday-loans.com/faq.html
[62] See Appendix C to this Report at 101.
[63] P. Kilborn, *supra* note 4 at A28; D. Menzies, "Waiting for payday" *Financial Post (National Post)* (22 September, 2001) D4.
[64] Dollar Financial Group, *supra* note 2 at 8.
[65] Stephens Inc., "The Emerging Business of Deferred Presentment (Payday Advance)" (April 1, 1999) at 5.

periods of up to two years and owing thousands of dollars on initial loans that were initially in the low one hundreds have been documented.[66]

To respond to this issue, some states place limits on rollovers or have established waiting periods between paying off a loan and taking out a new loan. The Community Financial Services Association of America, an organisation that represents a number of payday loan operators in the United States has also stated that its voluntary code for the industry limits rollovers to the lower of four or the state maximum, with prohibition where rollovers are not specifically allowed.[67]

However, consumer-based research comparing customer usage in states with rollover limits and those without suggests that limits appear have no effect on the total number of loans taken out by borrowers. Critics further argue that the financial risk to the borrower posed by back to back loans is equivalent to the risk posed by rollovers.[68]

There is debate between the industry and its critics concerning the extent to which borrower rollover or renewal of loans. The industry argues that the number of renewals or rollovers of loans is limited and that the average customer is an occasional customer, citing research showing customers use payday loans an average of 5-7 times per year.[69] However, even industry-sponsored research suggests that a significant percentage of customers engage in repeat usage of payday loans, with over 22% entering into 14 or more transactions in a twelve-month period.[70]

Some industry representatives admit that the rollover phenomenon is a problem for the industry: "We clearly believe that the industry is more vulnerable to the rollover issue than the fee size."[71]

Critics point to state-sponsored studies, which show a much higher incidence of repeat use over a twelve-month period. Data from Indiana regulators showed that 77% of customers renewed their loans with an average of 10 loans each. Similarly, data from regulators in Illinois showed an average of 13 contracts and 12 loans on average in Iowa.[72] A recent study of payday lending transactions in

---

[66] D. Menzies, *supra* note 63; L. Drysdale, *supra* note 21 at 607.
[67] G. Elliehausen & E.C. Lawrence, "Payday Advance Credit in America: An Analysis of Customer Demand" (Credit Research Center, Georgetown University: April 2001) at 8.
[68] Consumer Federation of America, *supra* note 28 at 9.
[69] Stephens Inc., *supra* note 65 at 3.
[70] G. Elliehausen, *supra* note 67 at 38. This study was financed in part by the Community Financial Services Association of America, a trade association of the payday loan industry.
[71] Stephens Inc., *supra* note 65.
[72] K. Keest, "Credit in the Alternative Financial Sector: The U.S. Experience" 35 Canadian Business Law Journal (2001) 409 at 416.

Wisconsin found that customers averaged 11.9 loan transactions over a 12-month period.[73]

### *1.2.5 Absence of Strong Regulatory Responses in Canada*

Regulation of consumer credit and financial services falls under both federal and provincial jurisdiction. The federal government regulates banks and federally incorporated trust and loan companies. Provincial governments regulate credit unions and provincially incorporated insurance companies and trust and loan companies.

With respect to interest rates, although the federal government has exclusive jurisdiction over interest, there has been recognition by the courts of concurrent jurisdiction by the federal and provincial governments to regulate interest rates.

Legal responses to payday lenders include legislation at the provincial or federal level to: control interest rates, license payday lenders or regulate their practices, and/or disclose information. Non-legislative regulation may include the application of the common law doctrines of fraud, deception or unconscionability. Despite the presence of legislation and judicial decisions at the federal and provincial levels in these areas, regulatory activity on these fronts has been minimal.

#### Interest Rate Ceilings and Licensing

The only current statutory control of interest rates is section 347 of the *Criminal Code.* Subsection 347(7) requires the consent of the provincial Attorney General to commence proceedings. Despite a clear indication by the courts that this provision is to be interpreted broadly with respect to fees and charges associated with payday loans, provinces have been reluctant to initiate prosecutions of payday lenders, many of whom appear to be applying APRs far in excess of 60%.

Reasons that have been given for provinces' reluctance to prosecute include: the impracticality of prosecuting where the number of transactions is great, but the amounts of the transactions are small; many consumers do not want payday lenders to be closed down, lack of alternative sources for short-term loans; concerns that forcing out payday lenders would drive consumers to illegal alternatives such as loan sharks.

[73] J. Caskey, "Payday Lending" (2001) 12(2) The Journal of the Association for Financial Counselling and Planning Education 1.

One province has enacted legislation that may have some impact on the payday loan industry and the fees charged, by imposing licensing conditions on payday lenders. In 1999 Saskatchewan enacted legislation, *The Trust and Loan Corporations Act*[74] which may require payday lenders, as "financing corporations", to be licensed by the provincial government. Licences have included conditions such as loan limits of $1,000, setting maximum interest rates of 52% per annum, limits imposed for fees charged for other services (such as cheque cashing) and a requirement to comply with the *Cost of Credit Disclosure Act*.[75]

### Disclosure Legislation

Information disclosure is a critical element of consumer protection in credit transactions. In financial markets, the APR is the key standard to allow consumers to compare the relative costs of financial services. Saskatchewan's *Cost of Credit Disclosure Act*[76] is based on uniform legislation adopted by the Uniform Law Conference of Canada. Its purpose is to unify the rules for calculating and disclosing the cost of consumer loans. Provincial ministers of consumer affairs have undertaken to implement harmonised cost of credit legislation, adopting substantially similar legislation in British Columbia, Ontario (provisions relating to disclosure of interest rates by short-term lenders have not yet been proclaimed), and Nova Scotia.[77]

### Trade Practices Legislation

Trade practices legislation has been introduced in almost all provinces. The purpose of the legislation is to describe and prohibit deceptive and unconscionable practices by businesses. The legislation may also include, as in Ontario, practices that may impact directly on payday lending, such as 'grossly excessive prices' and 'failure to state a material fact' or 'terms and conditions, which are inequitable to the consumer'.[78]

Ramsay suggests that this legislation has not been utilised effectively on behalf of consumers, generally, much less with respect to payday lenders and has not achieved its general policy objectives. It was introduced in order to ensure a higher compliance by businesses than has been achieved by private court action. It was also intended to reduce consumer enforcement costs and lead to the development of norms related to consumer markets.[79]

---

[74] R.S.S. 1997, c. T-22.2.
[75] J. Hall, Superintendent of Financial Institutions, Sask. Dept. of Justice, Presentation to the Vancouver Roundtable on the Alternative Consumer Credit Market (9 June 2000).
[76] R.S.S. 1978, c. 21.
[77] This information based on the Uniform Law Conference of Canada's Table of Uniform Statutes enacted, online: http://www.ulcc.ca. (date accessed: 30 August 2002).
[78] *Business Practices Act,* R.S.O. 1990, c. B. 17, s. 2.
[79] Ramsay, *supra* note 11 at 29.

## 1.2 Payday Loans and Other Jurisdictions

### *1.3.1 The United States*

Payday lending has drawn much more intensive media scrutiny, consumer activism, litigation and regulatory response in the United States than in Canada. It is difficult to know why this is the situation. The reason may be the deeper penetration by the payday lending industry in U.S. consumer financial markets, combined with that country’s stronger foundation of consumer activism and consumer-based research.

#### Federal and State Legislation

Both federal and state levels have legislation that regulates payday lending. Most states have enacted general usury laws, which set out interest rate ceilings. At the federal level, three statutes are relevant to payday lending: the *National Bank Act*[80]*,* the *Truth in Lending Act*[81] (*TILA*) and the *Racketeering Influenced and Corrupt Organizations Act*[82](*RICO*).

The approaches of the individual states to payday lenders may be broken down into three categories: 1) those states that prohibit payday loans, 2) those with no cap on small loan rates or no usury cap, and 3) those states with specific legislation permitting payday loans.

By November 2001, there were twenty-one states prohibiting payday loans by some rate cap, usury law or specific prohibitions against cheque cashers. Six states had no small loan interest rate restrictions or usury caps on licensed payday lenders and twenty-five states plus the District of Columbia had specific laws that permit payday loans.[83]

At the federal level, the *National Bank Act* has played a critical role in allowing payday lenders to bypass state usury laws. As discussed above, the practice of partnering with banks by payday loan companies allows payday lenders to circumvent potentially restrictive state laws on usury, interest rate caps and/or extension of credit. Under the *National Bank Act*, a national bank may ‘export’ the law of its home state nation-wide, allowing it to pre-empt any state law restricting “interest” in the borrower’s state. Thus payday lenders, by affiliating

[80] 12 U.S.C. § 85 (1994).
[81] 15 U.S.C. §§ 1601-1693r (1994).
[82] 18 U.S.C.S. § 1961 n.1 (1991).
[83] Consumer Federation of America, *supra* note 28 at 26-27. There is ongoing and active litigation at the state level in this area as well as lobbying by the industry for payday lending-friendly legislation, which may have produced changes in these categories since November 2001.

with banks situated in states with no interest rate restrictions, may evade restrictive state usury legislation.[84]

This practice may also apply to state chartered banks. By means of another piece of federal legislation, the *Depository Institutions Deregulation and Monetary Control Act*, state chartered banks have been placed on a level playing field with national banks, allowing them to assert similar exportation rights.[85]

The *Truth in Lending Act* concerns the issue of disclosure to consumers of the cost of credit and contains a broad definition of credit that would appear to encompass payday lending. This Act has not been generally invoked in payday litigation, despite the fact that an official staff commentary was added to the Act in May 2000, specifically stating that payday loans were a form of credit under the Act.[86]

Finally, *RICO*, the federal statute focused on organised crime, has been utilised against payday lenders, despite the fact that usury is not defined as criminal activity under state law.[87]

### Case Law

Much of the litigation in the U.S. has centred on payday lender attempts to disguise payday loans as cheque cashing, rather than credit transactions. One method has been to describe the payday loan as a deferral of the cashing of a cheque to the issuer's bank. Courts appear to be looking at the substance of the transaction, not its form and finding these transactions are loans and therefore subject to usury legislation as well as *RICO* and *TILA*.[88] More recent litigation has centred on payday lender attempts to evade state laws through partnering with chartered banks.

### Customer Profile

There has been limited research on payday loan customers in the U.S. Existing research produced by the payday loan industry and government regulators shows divergent conclusions about the customer profile. Industry-based research suggests that the majority of payday loan customers are between 18 and 49 years of age, employed in a professional or managerial capacity, with annual incomes between $15,000 - $40,000 or between $25,000 - $50,000.[89] State-based regulators surveys suggest that the average age is 32 years, with

[84] L. Drysdale, *supra* note 21 at 646.
[85] *Ibid.*
[86] C. Bruch, "Taking the Pay Out of Payday Loans: Putting an End to the Usurious and Unconscionable Interest Rates Charged by Payday Lenders" (2001) 69 U. of Cincinnati Law Review 1257 at 1262-1263.
[87] *Ibid.* at 1263.
[88] *Ibid.* at 1274-1275; K. Keest, *supra* note 69 at 412.
[89] Dollar Financial Group, *supra* note 2 at 8; G. Elliehausen, *supra* note 67 at 28.

much lower incomes: between $18,000 and $25,000.[90] The industry and its critics also dispute the extent to which customers engage in rollovers or repeat transactions.

### *1.3.2 Australia*

Payday lending is a relatively recent but fast-growing phenomenon in Australia. The first payday lender appeared in December 1998, but recent estimates suggest that by 82 outlets were operating throughout Australia by August 2000.[91] The industry estimates total annual revenues for payday lending were approximately $200 million in 2001.[92]

As in Canada, research on this issue is minimal, but Australians have noted parallels between the Australian and Canadian experience with respect to the key issues associated with the AFS identified in Ramsay's report, such as high fees, "rollovers", growing dependence on credit and rising household debt, and the focus of payday lenders on more vulnerable consumers.[93]

The national statute governing payday lenders, *The Uniform Consumer Credit Code*, has recently been amended to ensure that payday lenders are subject to the Code. The Code is a consumer protection statute which includes: cost of credit disclosure (including the APR), unconscionability provisions, regulation of repossession methods for defaults and positive or negative licensing (depending upon the state's regulation of the industry).[94]

A recent study of payday lending in Australia notes the limitations of the Code and its amendments. The Code focuses on disclosure, which critics suggest may not have measurable impact on consumer behaviour. Also, it has been noted that the amendments contain some important gaps. They do not require payday lenders to disclose the cost of credit as an APR. They do not implement a national interest rate cap of 48% (the 48% cap only applies in some States) and the do not specify whether the Code interest rate cap (where it applies) includes all relevant fees attached to the payday loan.[95]

The report also contained the results of a street and survey of 72 payday loan customers. The survey suggested that the users of payday loans were mostly low-income individuals who borrowed to pay bills or cover day to day living expenses. Over 65% of customers surveyed had taken out more than one

---

[90] J. A. Fox, *supra* note 8 at 5.
[91] Queensland Office of Fair Trading, *Payday Lending – A Report to the Minister for Fair Trading* (August 2000) at 5.
[92] D. Wilson, *Payday Lending in Victoria – A Research Report* (Melbourne: Consumer Law Centre Victoria Ltd, 2002 at 34.
[93] T. Duggan, "Access to Credit in the Alternative Consumer Credit Market: An Australian Comparison" (2001) 35 Canadian Business Law Journal 402; D. Wilson, *supra* note 92 at 19.
[94] T. Duggan, *Ibid.* at 404.
[95] D. Wilson, *supra* note 92 at 39.

payday loan, and the average number of payday loans was six over a 12-month period.[96]

### *1.4 Roadmap to the Report*

The primary research for this report used focus groups and surveys to inquire into the use of payday loans, but it also examined the associated service of cheque cashing offered at most payday loan companies. The reason was to provide some context for the examination of payday loan customers, as well as widening the base of potential survey respondents.

Use of finance companies and pawnbrokers were also investigated, to determine if there were consumers who used more than one AFS product, or if a contrast could be drawn between the consumers of one product versus another.
The research was aimed at finding out the demographics of the users of these sectors of the AFS, their experiences, preferences and motivations, but perhaps most importantly, their understanding of what their costs and options are, both inside the AFS and without.

## 2.0 Research Methodology

### *2.1 Approach to Sampling*

The main challenge facing this research project was to identify users of alternative financial services (AFS) and to encourage them to explain their experience with the industry. Almost by definition, the alternative financial services sector is marginalized and focuses on customers who either cannot access mainstream financial institutions or who otherwise choose not to. Indeed a key hypothesis that the research sought to test was that the alternative financial services sector seeks out customers who are among society's disadvantaged.

The sample design for the research began with a relatively broad definition of the alternative financial sector. The questioning of respondents focused more specifically on their experience with those parts of the industry of greatest immediate concern, particularly the payday-lending sub-sector.[97] The industry was defined to include the payday lending, cheque cashing, pawnshop loans, and debt consolidation loans through finance companies. As suggested above, the payday lending business is of greatest immediate interest because there are

---

[96] *Ibid.* at 53.
[97] Although the AFS industry was 'broadly' defined in this study, it was still not as broadly defined as others have defined it. For instance, Ramsay defines the industry in terms of cheque cashing, payday lending, pawnbrokers and second-hand dealers, rent-to-own, tax rebate accounting, loan brokers, finance companies and other sub-prime lending. See Ramsay, *supra* note 11.

concerns that it may be in violation of federal usury statutes as well as being of interest to a number of provinces from a consumer protection perspective.

It was felt that a broader definition of the industry would encourage people to come forward who may not initially wish to identify themselves as payday loan customers. In addition, this broader market could be considered representative of that part of the population that has experience with various aspects of alternative financial services and therefore which may also be likely to experience any of the specific sub-sectors of the industry over time.
The research methodology consisted of focus groups and a household survey. Each of these methodologies had unique contributions to make to the understanding of the industry. The role of the focus groups was to delve into the qualitative aspects of usage and to pre-test some of the hypotheses and questions for the household survey. The household survey was designed to generate estimates of the number of Canadians that use the alternative financial services sector and its sub-sector components.

The use of a random sampling methodology for the household survey allows for specific estimates of the size of the market and statistical tolerances around these estimates. This is an important contribution of the research as the size of the market in Canada has been the topic of some speculation. From a policy perspective, it is crucial to understand the size and nature of the market to determine the appropriate scale and level of any proposed regulatory approach.

## *2.2 The Focus Groups*

The challenge of recruiting willing respondents for the study proved to be greater for the household survey than the focus groups. Forty-seven people showed up for focus groups in Toronto, Calgary and Vancouver in August 2001. Moreover, those that attended were, apparently, not stigmatised by their experience with the AFS and spoke very openly about it.

In addition, a disclosure interview was held with a former employee of Money Mart, the largest cheque cashing and payday lending company in Canada. This interview revealed a number of industry practices that were geared toward maximising revenue. Most noteworthy was the management of item fees for security cheques for payday loans. Although payday loans are, ostensibly, structured to allow the customer to avoid item fees, it was very common for these fees to be charged. This was because the customer has a very limited window for redeeming their security cheque and usually does not go through the inconvenience of redeeming the cheque. The disclosure interview also revealed that the risk associated with the customer base was not as great as one might think because of the customers' limited options to access finance.

The full focus group report is appended to this study (Appendix C). It may be useful, however, to highlight some of the findings especially as they pertain to the issues that were addressed in the household survey.

### *2.2.1 Key Findings from the Focus Groups*

The focus groups were most revealing in determining the rationale behind alternative financial sector use and specifically cheque cashing and payday lending. Rationally, the industry will price its products to its costs of delivery and the risks attached to the customer. From the consumer perspective, however, it makes sense to obtain financial services from the cheapest source available or, if a higher cost option is chosen, to have those costs justified in terms of a tangible benefit. Yet the focus groups revealed a rather fundamental flaw in the way customers calculate the relative cost of financial products.

Costs where calculated in a dichotomous way: credit was perceived to be either ‘cheap’ or ‘expensive’, and not calculated in more precise ways. Bank loans were considered to be cheap but for various reasons were thought to be unavailable or undesirable. Other credit including credit cards cash advances, finance company loans, pawnshops and payday loans were considered to be ‘expensive’ yet widely available. Although a few attendees were fairly sophisticated in the management of their debt, for the most part the calculation of financial services costs was not accurate. This raises the question of the ability of many AFS customers to make trade-offs between the cost and benefits of various products.

This financial literacy issue was further complicated by attitudes toward mainline financial institutions. In general, the view prevailed that banks were unwelcoming and judgmental whereas finance companies and payday lenders just ‘want to give you the money’. This posture of the AFS versus mainline deposit-taking institutions is perhaps not surprising given the differing fiduciary responsibilities and fee structures of these sub-sectors.

This difference ultimately manifests itself in mainline policies and practices that may not be altogether to the liking of some customers. For example, bank and trust company hold periods on cheques were seen as being a major reason why cheque-cashing institutions were attractive. Yet when the banks offer a product, like credit card cash advances, that seeks to improve access to higher cost credit, some customers are concerned that this will lead them into spiralling debt. Indeed the open-ended nature of credit cards was a major reason why some customers preferred payday loans to credit cards.

Although payday lending is ‘expensive’ it is relatively closed-ended and therefore was seen as a way of managing the volume of debt. The total cost of credit was calculated in terms of the volume times the unit cost (i.e. the interest rate). Customers who see themselves as unable to control the volume are more likely to favour a high cost. The psychological burden associated high levels of outstanding debt was significant for these customers. Given their tendency to equate the cost of credit card cash advances with payday loans, the closed-ended nature of these payday loans took on even greater significance.

The users of cheque cashing and payday lending do not necessarily follow a path of higher levels of debt leading to worsening credit ratings ending in the sub-prime lending market. Although there is an identifiable market segment that does follow this path, they are more likely to see payday lending as the end of the road and to be avoided. However, another segment has simply chosen the cheque-cashing and payday lending companies because of their perceived advantages including location, friendliness, the closed-ended nature of the relationship and so on. These customers are not likely to manage their finances in a systematic way and yet may very well have reasonably good incomes and credit ratings. They simply pay more for their financial services because of a financial habit that usually starts in the early years of employment when the industries late opening hours and no-cheque-holding policies are of greatest attraction to them.

Many people are attracted to cheque cashing and payday lending institutions because they are 'non-judgemental'. They are therefore equally disdainful of policy interventions that seek to judge their financial habits. Younger customers in particular are likely to see their use of these fringe institutions as part of an alternative lifestyle choice, a refutation of mainstream institutions. Moreover, the customers were, on the whole, very satisfied with the service they received from the payday lending and cheque-cashing institutions.

### *2.2.2 Implications for the Household Survey*

The focus groups provided rich qualitative data and raised a number of new issues that have not been considered before in the Canadian literature on the AFS. However, the question remained as to how representative the focus group attendees were of the AFS market. In particular, it was imperative to attempt to estimate of the numbers of Canadians who actually use these services and their characteristics. This could best be done through a large-scale household survey.

An additional objective of the household survey was to gain a further understanding as to why people use the AFS and especially the payday lending part of the AFS. Ultimately this would allow for a segmentation analysis, where estimates of numbers and characteristics could be related to the attitude and behaviours to create identifiable market segments.

## *2.3 Household Survey Methodology*

Forum Research, a Toronto-based market research company conducted the household survey. The survey, which was undertaken during September-October 2001, was based on a random sample of Canadian households with telephones. People contacted by telephone where asked the following question:

"Have you or has anyone in your household 15 years or older ever gotten a cash advance or credit from any of the following sources in the past three years?"

- A *payday lending* company (like Money Mart, Stop 'n' Cash or Financial Stop);
- A *cheque-cashing* outlet (like Money Mart or Stop 'n' Cash);
- A *pawnshop* where you are advanced cash against personal items left as security;
- A *debt consolidation loan* from a finance company (like Avco Financial or HFC).

These AFS sub- sectors were organised in a hierarchy based on those that are of greatest concern to the Public Interest Advocacy Centre (PIAC). Although incidences of usage were gathered for all the above sub-sectors of the AFS, in-depth interviews were only completed for the highest priority sector. For instance, if a respondent indicated payday lending usage and debt consolidation usage, the subsequent in-depth interview would be conducted about their payday lending usage.

Exhibit 1 (page 32) presents a summary of the methodology and the associated call record. The questionnaire was organised around first determining the incidence of usage and then drilling down on the priority sub-sector. This questionnaire is provided in Appendix A. Respondents were asked about their preferred supplier, their usage, where they found out about the provider, and their satisfaction with the level of service. The respondents were also asked about how they calculated the price of the product and how important the price was in deciding to use the product when compared to other factors. It is these questions about usage and attitudes that form the basis for the segmentation analysis later in this report.

**Exhibit 1:**

**Summary of Survey Methodology and Call Record**

| | | |
|---|---|---|
| **Method:** | Telephone Survey | |
| **Sample Size:** | 4206 contacts | |
| | 202 completed in-depth interviews | |
| **Respondent Qualification:** | 15 years of age or older and had used one of 4 types of alternative financing in past 3 years | |
| **Sampling Method:** | Random digit dial (RDD) from a database of all working Canadian telephone numbers. Up to three callbacks were made to obtain a completion. | |
| **Call Record** | ***Number*** | ***Per cent*** |
| **Total dialling** | **31,590** | **100%** |
| Refusal | 9,691 | 10 |
| Call-back appointment | 1,798 | 7 |
| Answer machine/Fax | 6,789 | 21 |
| No answer (3 times) | 4,448 | 14 |
| Wrong number | 865 | 3 |
| Not in service | 2,266 | 7 |
| Language | 803 | 3 |
| Vacation | 51 | * |
| Busy (3 times) | 639 | 2 |
| Duplicate number | 34 | * |
| **Live contacts** | **4,206** | **13** |
| **Completed interviews** | **202** | |

### *2.3.1 Comparison to Other Methodologies and Surveys*

A random telephone survey methodology is an effective way to determine the incidence of a particular phenomenon among the general population. As subjects are selected on a random basis, probability theory can be applied and statistical tolerances can be attached to the data. There is a science to the sampling that allows for an impartial examination of the results and testing of hypotheses.

Other methodologies, such as focus groups, interventions (where respondents are interviewed outside a supplier after usage) and personal interviews are less reliable because respondents are not selected randomly and therefore there is no way to legitimately make inferences from the findings from these methods to the population at large.

Nevertheless, there is still an art to telephone questioning. This is particularly the case for surveys of small incidence or marginalized activities like AFS usage. The main risk comes from respondent's unwillingness to be interviewed although, surprisingly, lower-income people are often more forthcoming in this regard than higher income people.

Another risk is that potential respondents may not have access to a telephone or may be living in situations where that access is shared and the person answering the telephone may not have knowledge of their usage of the AFS. Given that telephone penetration rates in Canada are in excess of 95 per cent and that for the vast majority shared access is within related families, this risk is possibly not as great as that from non-response. Shared phones are most likely to be the situation for cheque-cashing customers who, as will be seen later, are more likely to share accommodation with non-relatives. As well as shared accommodation, the telephone penetration rates do not capture large sectors of the low income population, including people living on crown lands, Indian reserves and military bases or in rooming houses, homes for the aged, etc, who may in fact be among the population without phones.[98]

These factors may have the effect of underestimating the number of Canadians using the AFS when using a telephone survey, so that it is difficult to know the extent of the effect of phonelessness and unrelated people sharing one phone on our ability to reach the market segment we intended.

Although it somewhat expands the definition of the AFS from payday lending and cheque cashing, this survey was fairly specific in its qualifying question about usage. Other surveys that have followed a similarly focused qualifying question, such as one attempted by the Quebec-based advocacy organisation Option consommateurs, have lead to relatively small response rates.

However, a survey by Ekos research for the federal Task Force on the Future of the Canadian Financial Services Sector generated an incidence rate for cheque cashing alone that was 8 per cent of the Canadian population.[99] In this case, the survey-qualifying question referred to usage *ever* as opposed to our question that asked about usage *in the last three years*. The qualifying question used for our survey asked about the last three years because we were interested in having the respondents recall their recent experience. Beyond three years, it was felt that the reliability of this recall might be suspect. Moreover, the usage of the last three years is probably more indicative of the current market.[100]

[98] P. Lawson, *Eliminating Phonelessness in Canada: Possible Approaches 2d ed.* (Ottawa: Public Interest Advocacy Centre, 2002).
[99] Ekos Research Associates Inc. Public Opinion Research Relating to the Financial Services Sector (Ottawa: The Task Force on the Future of the Canadian Financial Services Sector, 1998).
[100] At the risk of exaggeration, consider a survey posing the following question "have you ever used a diaper?" compared to one asking "have you used a diaper in the last three years". The latter is more likely to be indicative of the current diaper market.

In addition, the Ekos survey contained a lengthy preamble indicating that the survey was about general financial issues and that the Government of Canada was looking for the opinions of Canadians. Both the general qualification and the specific qualification for the Ekos survey were different and therefore the incidence results are not comparable.

## 3.0 Key Findings from the Household Survey

It is important to note, initially, that this survey provides very useful indicators about attitudes and experiences with the AFS. However, due to the relatively small sample size of completed interviews, 202 out of 4206 contacts, as indicated in Appendix B of this report, the margins of error increase significantly for questions on specific AFS sub-categories. A follow-up survey with a larger sample size (1200-1500) would have to be conducted to improve the level of confidence about the information and analysis in this survey.

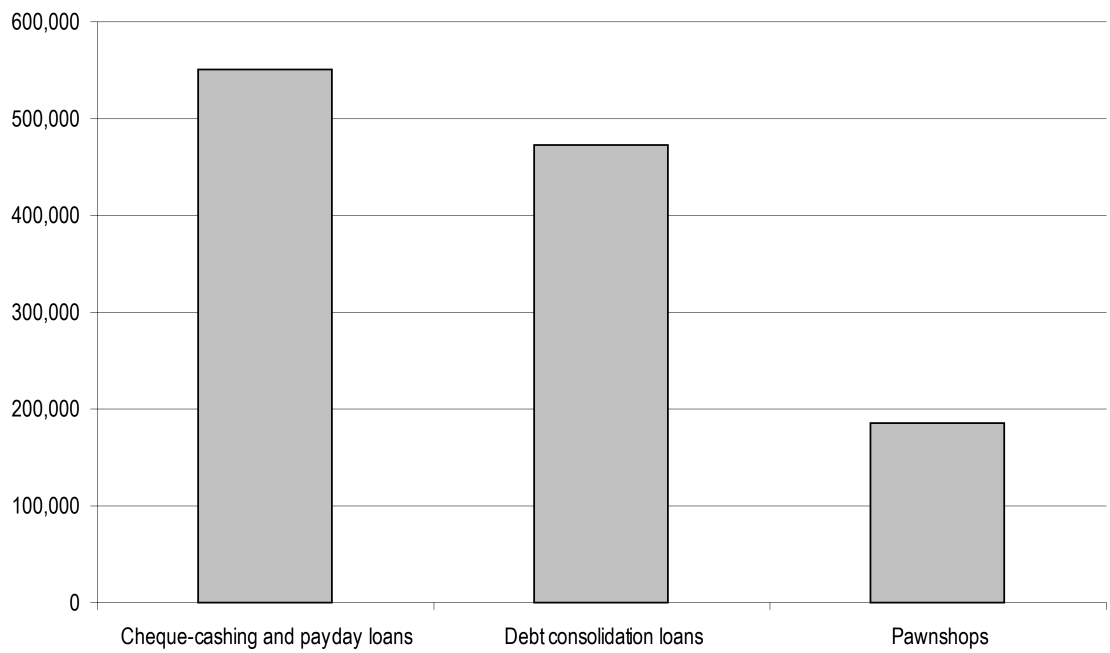
The objective of the household survey was to answer three basic questions about the alternative financial services (AFS) market:

1) How many people use the AFS (i.e. the incidence)?
2) Who are they?
3) Why are they using the AFS?

### *3.1 How Many People Use the AFS?*

The household survey was, first and foremost, geared towards finding the number of Canadians who have used alternative financial services in the last three years. The survey found that 202 respondents had some experience in the last three years with one or more of the four sub-sectors defined in the qualifying question. This amounts to an incidence rate for the AFS of 4.8 per cent.

**Chart 1:**
**Canadians Using Alternative Financial Services in Last Three Years**
**Estimated Thousands (Based on n=202)**




This overall incidence is accurate to within less than 1%, either way, nineteen out of twenty times. If all Canadians were polled, their answers would be within plus or minus 1% of the percentages indicated, nineteen out of twenty times asking the identical question about usage. A complete table of margins of error is provided in Appendix B.

When applied to the overall Canadian population aged 15 and over, this suggests that between 1.0 million and 1.4 million Canadians have experienced some part of the AFS in the last three years. This is the most statistically reliable part of the entire survey because it is based on over 4000 responses to the opening question. As seen in Appendix B, margins of error are significantly higher for questions on specific AFS sub-sectors. For this reason, the further the findings detail sub-sectors of the industry, the less confidence there is that the findings can be generalised to the population at large.

Chart 1 (this page) shows the estimated numbers of Canadians using various parts of the AFS in the last few years. Cheque-cashing and payday loans are combined, as they are two related products provided by the same companies. We estimate that just over half of this market is comprised of payday advance customers, about a third are cheque-cashing customers with the remainder using both products. This confirms a finding from the disclosure interview that was conducted in conjunction with the focus groups: the cheque cashing and payday lending institutions have been rapidly losing cheque cashing business to direct deposit systems and therefore must increasingly rely on payday loans for their business.

## *3.2 Who Are They? Demographic Characteristics*

Table 1 (page 39) highlights some demographic characteristics of the AFS market. In most respects, the market does not differ greatly from the overall Canadian population. For instance, the age and gender distributions are virtually the same as for Canada adult population at large.

One of the key hypotheses going into the household survey was that the AFS was "preying on the poor". The "poor" are usually defined in terms of characteristics like household income, education, employment and housing. On all these accounts, one must reject the hypothesis that the AFS is primarily a market of society's most disadvantaged. We estimate about 15 per cent of the AFS market would fall under Statistics Canada's before-tax Low-Income Cut-Off (LICO).[101]

According to the National Council of Welfare, the percentage of the Canadian population falling under LICO in 1998 was 16.4 per cent.[102] Moreover the average income of AFS customers is roughly in line with the Canadian average household income. Specific vulnerable groups are also not heavily represented. For instance, less than 1 per cent of the entire AFS market are single mothers. Similarly, less than 1 per cent is seniors and only about 4 per cent are youth under 21 years old.

The pawnshop sub-sector more correctly fits the characterisation of a business "preying on the poor" as their customers' average household income was about $20 thousand lower than the Canadian average and their employment rate was about 20 percentage points lower than the average. They are also somewhat more likely to have children living in their home and are significantly less likely to own their home (32 per cent compared to 59 per cent overall).

The employment rate for AFS customers is actually slightly higher than the Canadian average. The educational and occupational profiles lean slightly more toward the blue and grey collar employees lacking university education. Indeed, we found no professionals among cheque-cashing customers.

[101] This is the measure used to define incomes which fall below the poverty line. In 2001, a single individual with an income of $18,849 or below, living in a city with a population of 500,000 or more, was considered poor.
[102] See the National Council of Welfare online at: http://www.ncwcnbes.net/htmdocument/principles/povertyline.htm

Cheque-cashing customers are also more likely to be single (49 per cent). Notwithstanding this, their average household size is actually higher than for others. The average age of cheque-cashers (32 years) tends to be significantly lower than payday loans or debt consolidation customers (42 years for both) and they are also more likely to be students. All this suggests that cheque cashers are typically young people sharing accommodation with friends.

**Table 1:**
**Characteristics of the Alternative Financial Services Users**
**Per cent**

| | | | |
|---|---|---|---|
| **Gender** | **%** | **Household Income** | **%** |
| Males | 50 | Under $20 thousand | 14 |
| Females | 50 | $20,000 to $39,000 | 30 |
| | | $40,000 to $59,000 | 18 |
| **Age** | **%** | $60,000 to $79,000 | 10 |
| 15 - 20 years | 4 | $80,000 to $99,000 | 4 |
| 20 - 24 years | 15 | $100,000 and over | 6 |
| 25 - 29 years | 15 | Refused | 18 |
| 30 - 34 years | 13 | | |
| 35 - 44 years | 26 | **Home Tenure** | **%** |
| 45 - 54 years | 17 | Rent | 41 |
| 55 years or more | 9 | Own | 59 |
| ***Average age*** | ***38*** | ***Average household income*** | ***$51,400*** |
| **Marital Status** | **%** | **Employment Status** | **%** |
| Married/common law | 59 | Working | 70 |
| Single/ | 31 | Not Employed | 10 |
| Divorced/separated | 7 | Student | 8 |
| Widowed | 3 | Retired | 7 |
| **Average size of household** | **2.9** | Homemaker | 5 |
| **Education** | **%** | **Occupational Status (n=176)** | **%** |
| Up to grade school | 6 | Skilled labour | 37 |
| Up to high school | 52 | Unskilled labour | 25 |
| Up to community college | 23 | Self-employed/ manager | 16 |
| Up to university | 15 | Sales or clerical | 6 |
| Post graduate | 3 | Professional | 4 |
| | | Other | 12 |

## *3.3 Why Do They Use the AFS?*

The users of the AFS, (with the exception of pawnshop customers) look very much like average Canadians. If their demographic characteristics do not distinguish them, then there must be other factors driving their use of the AFS.

The focus groups revealed two groups of users: those that used the AFS because of their poor credit rating and another group who had other options available but who chose to use the AFS for reasons other than cost. Through various answers to the survey it is possible to construct the main paths to the AFS and whether financial circumstances or other preferences drive these.

### *3.3.1 Starting Financial Position*

We expected to find that users of the AFS would have poor credit rating that limited their access to lower cost credit alternatives. Table 2 (page 39) looks at various aspects of the financial position of AFS users.

The first two questions are assessments of credit liabilities: question 1 relates to a personal assessment and question 2 to an institutional assessment. The focus groups clearly showed that one constraint on debt accumulation is personal comfort level. A second constraint is based on the external assessments of credit worthiness by credit agencies and lending institutions. The two measures can be very different because a person may have a very good credit rating but be uncomfortable with their debt level. Another recent survey has shown that, on average, Canadians carry $1,269 just on their credit cards, so the “normal” amount of debt can be fairly significant.[103]

A surprising result is that the self-assessed financial position of these respondents is reasonably good. Only 9 per cent have a poor credit rating and well over half are carrying less debt than they normally have. The main constraint is not so much the existing debt position as the fact that money is tight, as over half indicated that they either had a shortfall from their pay period or just barely enough to cover expenses.

These results were fairly consistent through the sub-sectors of the AFS with the exception, once again, of pawnshop users who were significantly more likely to have higher than normal debt levels, poor credit ratings and tight cash constraints. There was very little difference in the averages and the findings for payday loan, cheque-cashing and debt consolidation customers, except in terms of cash needs where payday loan customers were only about half as likely to indicate that they had more than enough for their needs.

[103] Canadian Press/Leger Marketing, “Canadians and Credit Cards”, (10 December 2001). Online at: http://www.legermarketing.com/

**Table 2:**
**Characteristics of the Alternative Financial Services Users**
**Percent of Respondents (n=202)**

| | Much higher | Higher | Normal | Lower | Much Lower |
|---|---|---|---|---|---|
| | % | % | % | % | % |
| 1.How would you describe the debt that you are carrying compared to your normal debt? | 8 | 19 | 47 | 12 | 14 |
| | **Poor** | **Fair** | **Average** | **Good** | **Very Good** |
| | % | % | % | % | % |
| 2.How good would you say your credit rating is right now? | 9 | 10 | 21 | 28 | 32 |
| | **Not nearly enough** | **Not quite enough** | **Just Barely enough** | **A little more than enough** | **More than enough** |
| | % | % | % | % | % |
| 3.How would you rate the amount of cash that you have at the end of the pay period in relation to your needs? | 11 | 11 | 31 | 28 | 19 |

### *3.3.2 Financing Needs*

One of the claims of the payday lending companies is that their service is used primarily to finance emergencies and that it makes sense to use short term finance in this way, especially when compared to the option of not dealing with the emergency. The survey tested this claim directly by asking respondents how they used their AFS finance.

Chart 2 (page 40) shows the major reasons for using AFS finance overall (excluding debt consolidation loans). These usage patterns are in line with the characterisation of the AFS users being short on cash as it is most common to use AFS finance to cover cash shortfalls for day-to-day expenses. The usage patterns are essentially the same for the three sub-sectors considered (payday loans, pawnshop loans and debt consolidation). There is some truth to the claim that payday lending is used for emergencies but genuine emergencies and avoiding bouncing a cheque accounted for less than 30 per cent of total usage.

### *3.3.3 Average Amounts*

The average amounts borrowed or cashed in the last usage of the AFS are presented in Table 3 (page 40). Not surprisingly, debt consolidation loans were significantly higher and pawnshop loans were significantly lower than payday loans.

**Chart 2:**
**Uses of Alternative Financial Services**
**Percent of Respondents (n=175)**

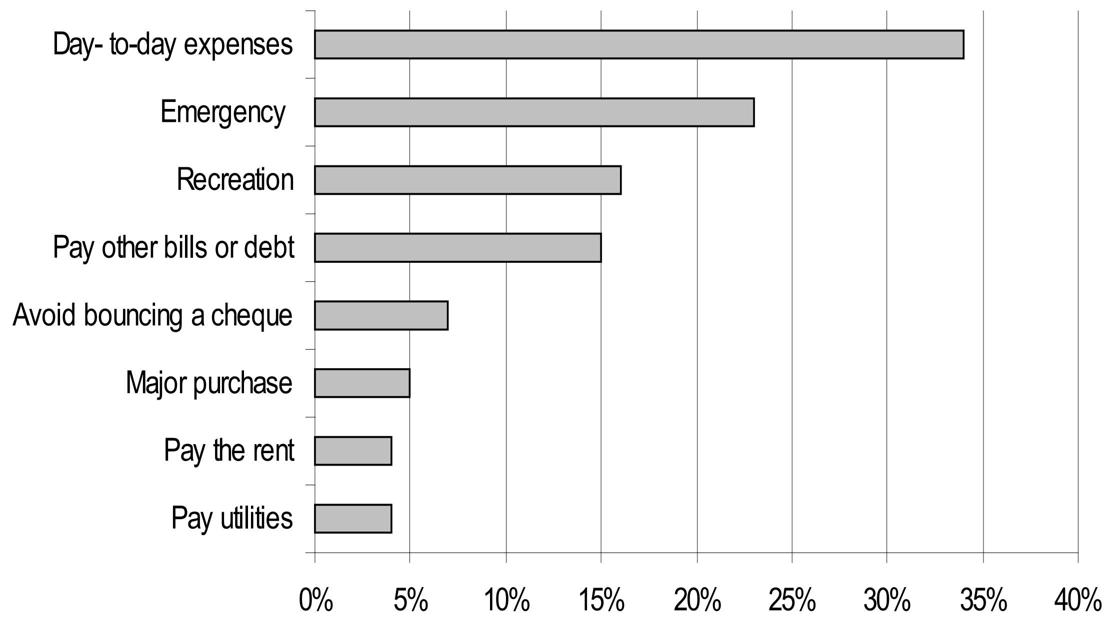


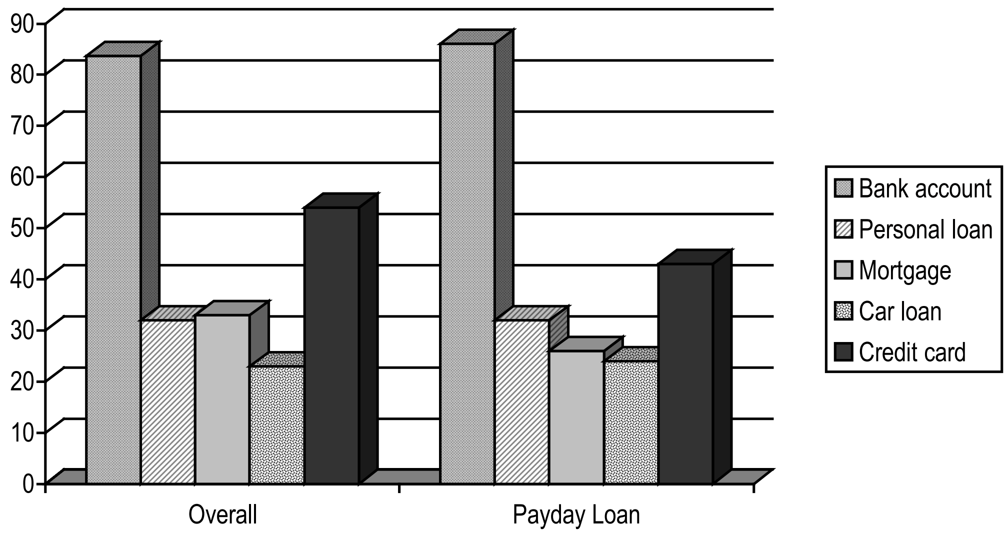

**Table 3:**
**Average Amounts for Different AFS Products**
**Dollars**

| Product | Average in dollars $ |
|---|---|
| Payday loan | 573 |
| Cheque cashing (average size of cheque) | 536 |
| Debt consolidation loan | 2806 |
| Pawnshop loan | 156 |

### *3.3.4 Available Options*

One of the purposes for the survey was to find out which of the options was available to the users of the AFS. Based on the self-assessment of credit ratings, it would appear that there are relatively few institutional constraints on AFS users accessing credit. Rather, their personal comfort level with outstanding debt was more likely to act as a constraint.

**Chart 3:**
**Characteristics of the Alternative Financial Services Users**
**Per cent of Respondents (n=202 overall and n=57 payday loans)**




The percent of banked respondents – those with access to traditional banking services, particularly bank accounts - is very much in keeping with the general population for both the overall AFS customer base as well as the particular case of payday loan customers. It is especially interesting to note that the cheque-cashing customers had a banked rate of over 90 per cent. AFS users have significantly less use of credit cards as about 75 per cent of Canadians have credit cards compared to around 53 per cent for AFS customers.[104]

Given the self –assessments of credit ratings and debt levels, this lower level of credit card ownership is more likely to be through choice than a lack of availability. This supposition is further supported by the fact that over 75 per cent of AFS credit card holders indicated "normal" or "below normal" levels of current debt. As in other areas, pawnshop customers were most unlikely to have financial products other than a bank account.

### *3.3.5 Financial Literacy Issues*

A key finding emerging from the focus groups was that a basic lack of financial literacy was leading to customers to place less emphasis on the cost of alternative financial services and more on other factors. The household survey consequently investigated how respondents calculate the cost of their AFS products. Respondents were asked annual total costs in fees and interest and could answer in either in annual percent terms or in dollar amounts.

[104] *Ibid.* at 1.

### 3.3.5.1 Calculating Costs

Table 4 (this page) estimates the accuracy of these responses based on the published rates of the main providers for payday loans and debt consolidation loans. The first noteworthy fact is the relatively high numbers of respondents who did not know how much the loan was costing them. Payday loan customers were somewhat more likely to underestimate the amount of their payday loan. Payday loan respondents were most likely to answer in terms of dollar cost (40 compared to 17 for percent). When they did use percentage terms, they were most likely to calculate this over the term of the loan (usually two weeks). No respondents converted their percent estimate into annual percentage rate (APR).

**Table 4:**
**Estimates of Costs**
**Percent of Respondents**

| Product | Did Not Know | Overestimated | Under-estimated | Correct |
|---|---|---|---|---|
| Payday loan (n=57) | 21 | 8 | 20 | 8 |
| Debt Consolidation loan (n=76) | 40 | 6 | 7 | 23 |

Note: based on published rates by National Money Mart Company and Household Finance Company. Assumes one loan at the average surveyed rate. Payday loans assume all fees are attached to the loan, which is standard practice in the industry. If respondents redeemed their security cheque with cash prior to the term, thereby avoiding item fees, 5 respondents that are categorised as "underestimated" would in fact be correct in their estimate. "Correct" answers were accepted within a 5 per cent margin of error.

---

Cheque cashing customers were similarly challenged when calculating costs. Twenty-one of thirty-five respondents did not know how much it was costing them to cash their cheques and only 5 came close to the right answer.

Debt consolidation customers seemed to have a slightly better grasp of the cost of servicing their debt although, again, there are many who do not know. But the ones who did know were more likely to be correct in their estimates. This is consistent with the focus group finding that debt consolidation customers are much more aware of the cost of their debt than payday loan customers.

Although the financial illiteracy of AFS users is significant, this fact is not as significant when placed within the larger context of the general financial literacy of the Canadian population. A recent national survey of Canadian's credit card usage found that over 41 per cent of Canadians did not know how much interest they were paying on their credit cards, and that 4% thought they were not paying any interest at all on credit cards.[105]

A 1997 survey of Canadians' economic and financial understanding, by the Canadian Bankers Association and the Canadian Foundation for Economic Education, supports the theory of Canadians' general lack of financial literacy. The survey found that Canadians' knowledge of general economic indicators and personal financial issues was very limited. For example, although 58% of respondents indicated RRSP (Registered Retirement Savings Plan) ownership, only 9% understood what the maximum allowable contribution was to an RRSP.[106]

The percentage of respondents from the credit card survey who indicated they did not know the interest rate on their credit card is almost the same percentage as that of payday loan and debt consolidation customers combined. These miscalculations are obviously the most costly for the highest cost sources of credit, namely, payday loans.

#### 3.3.5.2 Where do ASF Consumers Get Their Information?

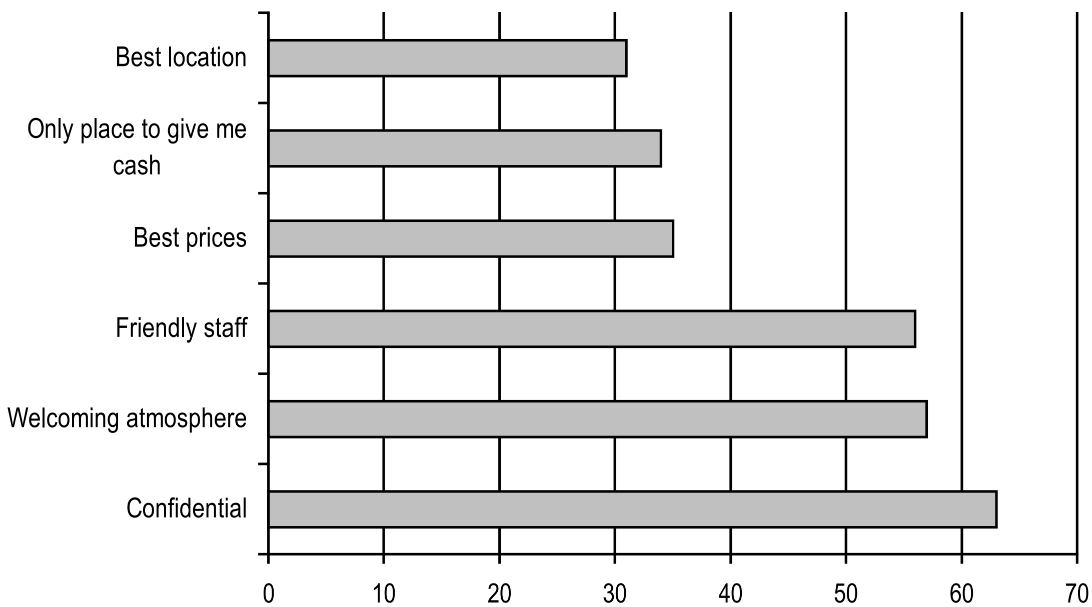
The most common source of information about the AFS was advertising. Almost half (48 per cent) of AFS users were made aware of the option they used through various forms of advertising. By order of importance these advertising media were street signage, television or radio and print media. Word of mouth was also important as about one third of AFS respondents found out about the option through friends, relatives and acquaintances.

### *3.3.6 Other Factors That Affect the Decision to Use AFS*

Given the answers on calculating costs, it was natural that AFS customers put a relatively small emphasis on cost when deciding to choose an AFS provider. Consistent with the focus group findings, AFS customers are most likely to prefer service aspects of the AFS, especially the confidentiality of the service and the fact that the atmosphere was friendly and welcoming. It is also noteworthy that only about a third of these respondents indicated that it was "very important" that the AFS was the only place that would provide them with cash. This answer was most likely to be given by pawnshop customers.

[105] *Ibid.* at 3.
[106] Canadian Bankers Association & Canadian Foundation for Economic Education, *Survey of Canadians' Economic and Financial Understanding* (December 1997) at 14-15.

**Chart 4:**
**Factors in Choosing Source**
**Percent Responding "Very Important" (n=202)**




Apparently, the AFS providers are delivering to these service expectations. The percent of AFS customers saying that they are "very satisfied" with these aspects of AFS service range between 60 and 75 per cent. There is certainly some awareness of cost inasmuch only about half as many people indicated that they were very satisfied that the AFS provider had the best prices compared to other aspects of service.

It is also instructive to compare overall satisfaction levels of the AFS with satisfaction with banks and trust companies (Table 5 – page 45). The satisfaction with the AFS is rather high with 90 per cent of respondents indicating some satisfaction, which is very consistent with the findings in the focus groups.

**Table 5:**
**Satisfaction Level with the AFS and Banks and Trust Companies**
**Percent of Respondents (n=202)**

| | Not at all Satisfied % | Not Very Satisfied % | Somewhat Satisfied % | Very Satisfied % |
|---|---|---|---|---|
| How would you rate you satisfaction with the AFS? | 4 | 5 | 25 | 65 |
| How would you rate your satisfaction with banks/trusts? | 6 | 12 | 43 | 39 |

Although satisfaction with banks and trust companies is generally lower, it would not appear that these differences in satisfaction are major drivers in customers moving from the mainstream financial institutions to the AFS, as the number expressing some satisfaction with the mainstream financial institutions is also high.

Still some customers are likely to use the AFS because of dissatisfaction with the mainstream financial institutions. But, based on the numbers that expressed both dissatisfaction with the mainstream institution and satisfaction with the AFS, we estimate that this constitutes no more than about 10 per cent of the AFS market. Payday advance users are the most likely to be dissatisfied with mainstream financial services as only 21 per cent indicated they were very satisfied with banks and trusts.

### *3.3.7 Repeat Usage and Provider Abuse*

A concern of consumer advocates has been that the users of the AFS, and especially payday loans users, are vulnerable to repeat usage or rolling over loans and thereby generating astronomical effective annual interest rates. Consequently, a question was asked about repeat usage.

Overall about 67 per cent of AFS users stated that they have never used the AFS for transactions during consecutive pay periods. However, payday loan customers were more likely to answer either that they "sometimes" did this or they "frequently" did this. Thirty percent indicated that they sometimes or frequently used the same source for more than one pay period in a row. Indeed the majority of payday loans customers had at least some experience with rolling over their loans.

**Table 6:**
**Have You Used This Source for More than One Pay Period in a Row**
**Percent of Respondents**

| | Never % | Rarely % | Sometimes % | Frequently % |
|---|---|---|---|---|
| AFS Users (n=202) | 67 | 16 | 9 | 8 |
| Payday loan customers (n=57) | 49 | 21 | 18 | 12 |

The share of those who frequently rollover their payday loans is similar to those reporting difficulty in paying their loans (14 per cent). However, the payday loan customers were the least likely of all the loan sub-sectors to report that they had difficulty in paying their loans. Again, this accords with the focus group finding that an attraction of the payday loan is that it is highly structured and geared toward paying off at maturity, albeit at high costs.

Punitive actions in the event of non-payment were fairly rare for these respondents. Over three-quarters reported no experience at all with punitive actions and those few instances where it did exist were likely to be in the form of either calls to the home or credit downgrading.

## *3.4 Summary of Alternative Financial Services Segments*

Exhibit 2 (page 48) summarises the picture that emerges from the household survey and the focus groups of the various market segments of the AFS. There are essentially three drivers of usage: demographics, financial position and preferences.

*Pawnshop users* are most likely to have their AFS usage driven by their disadvantaged economic position. They are the market segment that is most likely to be unemployed or working poor. These people have the hardest time making ends meet and will occasionally pawn possessions for small loans (around $150 on average), especially when an emergency arises or if they are behind on utility payments. This is the smallest of the market segments, constituting about 200 thousand Canadians.

*Cheque cashing* users have lower middle incomes but not so much because they are disadvantaged but rather because are likely to be young people at an early stage of their working life. They may work for smaller employers and/or in trades where payment by cheque is still commonplace. Their money is sufficiently tight that the hold periods that are typically placed on cheques by mainstream financial institutions are a source of dissatisfaction that may lead them to use cheque-cashing institutions. They also are likely to be influenced by advertising that emphasizes the service aspects and downplays the costs of cheque cashing institutions. The actual cost and comparisons to other more cost-effective options (e.g. a short-term credit card cash advance during the hold period) is rarely considered. We estimate that there are about 200 thousand Canadian adults who use cheque-cashing services. These customers may eventually get up-sold to payday loans as about 80 thousand of the combined cheque cashing and payday loan user base will have had experience with both products.

*Payday loan* users tend to be somewhat older than cheque-cashing customers are. They are attracted to payday loans because of the confidentiality aspects and because the loans are highly structured forms of short term cash. These individuals are inclined to be debt-averse, especially open-ended debt like credit card cash advances. They obviously pay a lot for short-term loans, but they tend to calculate the cost in dollar terms that make the cost seem more palatable or, just as likely, don't consider the cost. A portion of the market rolls over these loans and therefore pay very high total APR's for their cash.

Although the overall levels of debt for these customers, by their reckoning, is “about average”, about 20 per cent of the market is at significant risk of running into debt problems through roll-over behaviour, which is a similar percent of the market that uses both cheque-cashing and payday loan products. Our estimate is that around 350 thousand Canadians use payday loans.

*Debt consolidation* users are probably the most conscious of their financial situation, inasmuch as they are taking steps to deal with it. They are very likely to be placed in their situation through the use of credit cards. They tend to be married, middle-aged adults with children with a history of money management problems. These customers are very unlikely to become payday loan customers and are more likely to see their debt consolidation as a means of returning to mainstream financial institutions, with which they have a reasonably high level of satisfaction.

**Exhibit 2:**
**Characteristics of Alternative Financial Services Market Segments**

| Segment | Demographics | Financial Position | Reasons for using |
|---|---|---|---|
| Pawnshop loans | • Middle age<br>• High school or less<br>• Married with children<br>• Working poor or unemployed | • Low income<br>• Very tight cash | • Daily expenses<br>• Emergencies |
| Cheque-cashing | • Young adults<br>• High school and some postsecondary<br>• Early career<br>• May still be in school | • Lower-middle income<br>• Occasionally tight cash<br>• Low debt | • Convenience<br>• Service<br>• Avoid holds<br>• Recreational use<br>• Cost not considered |
| Payday loans | • Middle age adults<br>• High school and some postsecondary<br>• Blue or grey collar<br>• Middle career<br>• Married or common law<br>• Children | • Lower to middle incomes<br>• "Average" debt<br>• Tight cash | • Daily expenses<br>• Emergencies<br>• Confidentiality<br>• Cost not considered or inaccurately calculated |
| Debt consolidation | • Similar to payday loan customers | • Lower to middle incomes<br>• High debt levels | • Control of debt<br>• Aware of cost of credit |

## 4.0 Implication of Survey Results for Policy Makers

There are five important findings that emerge from the survey and focus groups that have implications for policy makers, some of which coincide with key issues identified by Ramsay. They can be summarised as: dependence on credit, financial illiteracy, rollovers of payday loans, alternatives to payday loans, and the effect of turning away from mainstream financial services.

The survey also produced results that are somewhat more ambiguous with respect to what legislative or regulatory responses should be put in place. At a minimum, however, understanding more about the characteristics of customers and their reasons for using payday loans provides a realistic basis for understanding what policy options chosen by regulators may or may not work in relation to the AFS.

## 4.1 Dependence on Credit

As discussed above, the growing use of the AFS and payday loans in particular, is a subset of a much larger phenomenon, Canadians' growing dependence on consumer credit. As Ramsay pointed out, two important economic trends contributing to the financial vulnerability of consumers are declining ratios of savings to disposable income and high debt to income ratios.

Ramsay also suggested that the dependence on credit should raise concerns when it is used to meet basic needs and not for the purchase of an asset with some value (such as a home) or where the purchaser does not have a high or steady income stream.

The survey results suggest that payday loans are used to meet basic needs and that many payday customers' incomes are simply not sufficient to meet those needs. Fifty-three percent of respondents indicated that they didn't have enough or had just barely enough cash at the end of a pay period in relation to their needs. The major reason identified for using the AFS was to meet day-to-day expenses.

Pawnshop customers are most likely to fit the characterisation of the vulnerable consumers of the AFS. We estimate that there are over 300 thousand Canadians using pawnshop loans to deal with financial shortfalls. However, we also believe that about 100 thousand of the customers using payday lending and cheque cashing facilities in Canada may be financially vulnerable consumers.

In addition to any regulatory approaches to the industry, AFS customers need credit counselling assistance for any income shortfalls that are leading them to use high cost credit. However, if chronic dependence on credit and inadequacy of income is a major driver of usage of the AFS, overall usage will only increase if the economic factors driving the increasing financial vulnerability of consumers remain unchanged.

## 4.2 Financial Literacy

The household survey suggests that a general lack financial literacy may be a major contributor to AFS usage. The majority of AFS customers did not know the cost of their loan or underestimated the cost. Where respondents gave a percentage term (rather than a dollar figure) as the cost of the loan, none described the rate as an annual percentage rate.

Approximately 35% of respondents to the survey indicated that "best prices" was a "very important" reason for using the AFS.

We estimate that approximately 400,000 payday loan and cheque-cashing customers do not know how much they pay for the service or underestimate the cost. Having a better framework for making financial decisions would assist consumers to make choices that, if not improve their financial position, would at the least allow them to make financial credit decisions based on understandable and good information.

An important question raised by the survey results on financial literacy is whether practices by the industry assist or deter the financial literacy of AFS customers. A cursory examination of the fee structures and practices of some payday lenders suggests that there is little effort to assist the financial literacy of payday loan customers and probably a greater contribution to customer confusion.

Some payday loan providers such as National Money Mart Company provide some disclosure of costs.[107] This is, in fact, much greater disclosure than many financial institutions provide of the fees and charges on bank services. However, it is also important to note that Money Mart does not explain its fees. For example, the "per item fee", which constitutes $14.99 of the total loan cost of $118.89 on a $100 loan over 6 days, is not explained as to its purpose. It is also important to note that many payday lenders offer no explanation for the fees and charges for their services on their web sites. These charges are also described in a variety of ways: "verification fee", "defined benefit plan", and "finance charge" among others.

## *4.3 Rollovers*

As identified above, one of the greatest risks associated with payday loans is rollovers or repeat usage. Although perhaps not as great as anticipated, we did find some evidence of compulsive usage of payday loans.

Thirty percent of payday loan customers indicated that they sometimes or frequently used the same source for more than one pay period in a row. There may be as many as 75 to 100 thousand Canadians who are using payday loans in this way and generating APR's in the thousands of percent in the process. Clearly this is a serious matter, particularly if the payday loans business continues to expand.

[107] See MoneyMart online at http://www.moneymart.ca/. National Money Mart's website contains a calculator, which shows the various costs of a payday loan and sets out the fees for cheque cashing services. The formal written contract is also available through the website, but, according to the focus groups and disclosure interviews, customers tend not to pay a great deal of attention to this document when contracting their loan.

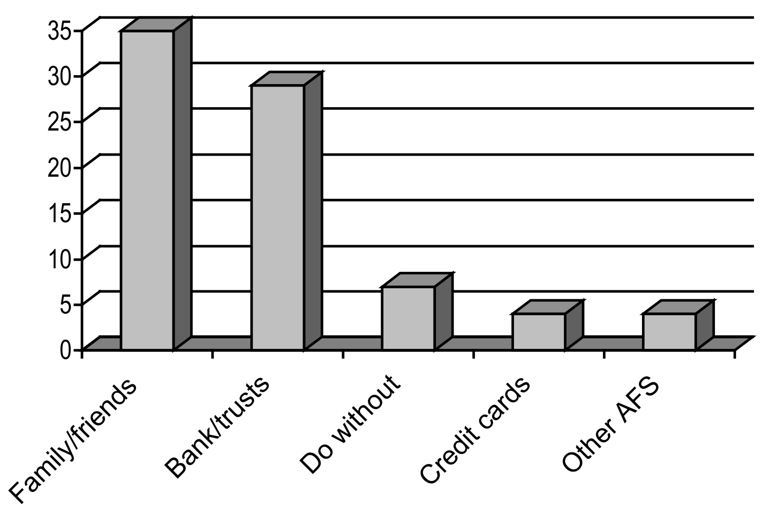
## 4.4 Other Financing Options

A standard response from the industry is that prohibition of payday loans and cheque-cashing outlets would lead to even worse outcomes, as people would turn to loan sharks and other unsavoury underground lenders, very much as the prohibition of alcohol encouraged people to turn to speakeasies operated by organised crime.

There was not a great deal of evidence to support the proposition that people would turn to more extreme forms of lending if payday loans were prohibited (Chart 5 this page). None of the respondents indicated that they would use loan sharks as an alternative to the AFS. This was not a surprising outcome, given that few people would admit to contemplating an illegal act. However, it also supports the idea that people are not acquainted with loan sharks, and would not know how to contact one.

The more surprising result is that relatively few would turn to another sector of the AFS for a loan. Unlike in the focus groups, the most common option indicated in the survey was obtaining money from family and friends. Turning to mainstream financial institutions, such as a bank or trust company, was the next highest alternative choice.

**Chart 5:**
**What Source Would You Go to if the AFS Provider You Used Was Unavailable?**
**Percent Responding (n=202)**



## *4.5 Market Power and Contestable Markets*[108]

Given the demographics of the users of payday loans: employed, with bank accounts and with (self-described) good credit ratings, the majority of people who use payday loan and cheque cashing companies would appear to qualify for mainstream financial services. However, many of these customers have turned away from mainstream financial services, indicating that they prefer the service aspects of the AFS compared to banks and other institutions. They specifically emphasised the confidentiality of the service and the friendly and welcoming atmosphere of AFS outlets.

There are two implications of this finding. The first is that banks are failing a large segment of the market and the second suggests that customers who turn away from mainstream services lose the benefits of competition.

The survey results suggest that mainstream financial institutions have done little to solicit, encourage or maintain business from low-volume customers. The survey respondents indicated that the main reason they gravitate to the AFS is service-related. The AFS was viewed as superior to banks in terms of client confidentiality, friendliness of staff and a generally welcoming atmosphere.

It is difficult to know why banks have ignored this segment of the population. One possible answer is that these customers do not represent a source of income for banks, since they don't have the financial resources to engage in the kind of services that contribute to bank profits. However, there is research that suggests this is a potentially profitable segment of the market. A recent U.S. report by the Brookings Institution found that households with annual incomes less than $25,000 are estimated to have $175 billion in financial assets and that "unbanked" customers spend at least $4 billion on check cashing and bill payment services annually.[109]

The second implication is that customers who choose the AFS enter a less competitive marketplace. Once customers begin defining themselves as primarily a payday loan and cheque-cashing customer, they have moved away from a market with many choices where the market presumably disciplines the players, toward one with fewer choices and less market disciplines. This occurs due to two factors.

First, the customer creates a self-fulfilling prophecy. He/she enters a market where the risks of not being able to pay off the debt become greater, due to the high fees and short time frame of the loan. This situation then further segregates

[108] Contestable markets are those where the presence of small numbers of competitors may not lead to monopoly pricing if entry into and exit from the market is relatively easy.
[109] R. Weissbourd, *Banking on Technology: Expanding Financial Markets and Economic Opportunity* (June 2002) at 8.

the borrower from improving their credit rating and being able to access mainstream financial services.

Secondly, the payday lending market is not as competitive as mainstream financial markets, which places less pressure upon payday lenders to reduce their associated fees. According to our survey, National Money Mart Company accounts for about 61 per cent of the payday lending market in Canada and over half of the cheque-cashing market. The next largest provider, CashStop has only about 11 per cent of the payday lending market and 17 per cent of the cheque cashing market. Given that most of the lending is done in person, this gives National Money Mart Company an effective monopoly in most of its local markets. This explains why National Money Mart Company is relatively untroubled about the default risk on its loans. In the words of the disclosure interviewee, “they have nowhere else to go”.

If the markets are contestable, any excess profit that National Money Mart Company makes should be bid away by competition. However, while there may be a social stigma attached to customers using the payday loan companies (which is more likely to apply to non-users than users), there has traditionally been a stigma attached to *companies* that enter this market.

That stigma may be disappearing. A brief survey of the yellow pages of the 2002/2003 Ottawa phonebook alone shows at least eight advertisements for payday lenders in addition to Money Mart. A quick search for Internet payday lenders in Canada turned up approximately 16 web sites.

Most of the mainstream financial institutions in Canada have not yet entered the short term lending market. To the extent they are involved, they will continue to do so through credit card cash advances. However, as discussed above, partnering between payday lenders and banks has become a growing phenomenon in the U.S. Given the financial results of payday lending, there would appear to be strong financial incentives for banks to enter this market.

It is interesting to note that a long-standing financial service company operating in Canada, H&R Block, now offers cheque cashing at its Financial Stop locations, although it declines to offer payday advances.[110]

## *4.6 The Debate about Regulation*

> We believe that the short-term loan or payday advance business has established itself and is in an evolving credit form that is here to stay. However, regulatory

[110] S. Kari, *supra* note 6 at 101.

> and legal attacks continue, as the product is a virtual poster child for liberal, consumer advocates.[111]
>
> It is disturbing…that there are companies feeding off the poor. The people who can least afford these loans are the ones falling prey. It is critical that we focus on making ethical decisions based on what[‘s] best for America and not what is best for lining our pockets.[112]

The debate about whether to regulate the AFS is rooted in very differing perceptions of the financial impact and risk of payday loans on consumers. The survey results are somewhat ambiguous on this issue. It is not clear the extent to which customers who use the AFS are aware of the financial impact and risk of payday loans.

The industry relies on the argument that it simply serves a market that desires its services and that is not being served by mainstream financial services. This survey indicates that many customers are willing to pay for the service even though they know full well that the cost is “high”. The AFS providers and customers in this survey tend to highlight service features that distinguish them from mainline financial institutions (no holds on cheques, non-judgmental lending processes) while downplaying their very high prices. Over 65% of AFS users in the survey indicated they were “very satisfied” with the AFS, compared to only 39% with banks or trust companies.

Although payday loan borrowers do not make the specific calculation of the real cost of their loan, as measured in annual percentage rates, users of the AFS may understand that this is not a cost-effective option. This is suggested by the low scores they give cost when assessing the reasons why they use the AFS, compared to the service elements of the AFS. As one of the focus group participants put it: “…when I go into the 7-Eleven I pay 6 bucks for box of cereal. But the place is open when I get out of work, so I pay it. Money Mart is just like that…you are paying for the convenience”.[113]

However, the survey is not completely unequivocal with respect to borrowers’ knowledge of the cost-effectiveness of payday loans. Approximately 35% of respondents to the survey indicated that “best prices” was a “very important” reason for using the AFS and over 40% of payday loan customers either didn’t know the cost of their loan or underestimated its cost.

---

[111] Stephens Inc., “The Developing “Payday Advance” Business”, (September 28, 1999) at 1. [Stephens Inc. holds common shares in U.S. payday loan companies.]

[112] Remarks by a navy captain testifying before a U.S. Congressional forum on payday loans convened by Sen. Joseph Lieberman, December 15, 1999. [source: L. Drysdale, *supra*, note 21 at 659]

[113] Appendix C, at 106.

Debt consolidation customers, at least, seem to understand that they pay high prices because they have accumulated large debt that makes them a poor lending risk. As the focus groups found, debt consolidation customers often see the debt consolidation process as the first step in getting their financial house in order. In this respect, these customers are probably in the best position to make trade-offs between the cost of credit and the benefits in which they would include the psychological benefit of managing one monthly payment.

Payday loan and cheque-cashing customers do not typically undertake the same sort of cost-benefit calculation. These customers clearly value many aspects of the services provided but, for the most part, do not fully appreciate how much the service costs them. Moreover, some payday loan users who have some difficulty controlling spending may be better off using payday loans periodically than credit cards. A person faced with paying $40 for a $580 loan for two weeks is better off than if they run up twice that much in credit card bills, which they end up carrying for a year.

The key however, is that such customers be only occasional users and be able to pay the loans off in full after the loan comes due. Customers who are using payday loans like credit card cash advances, in which they end up with a high volume of debt at a very high price, create a high-risk situation that could lead to severe financial difficulty. The survey results indicated that although not a majority, there is a significant percentage of payday loan users who are rolling over payday loans.

Proponents of the industry argue that although there are Canadians who will jeopardise their financial situation through chronic use, the highly structured and high cost of a payday loan may have a disciplinary effect. It may prevent some people from worsening their financial situation through high volumes of debt carried over long periods. They also argue that payday loans are a better alternative to the high fees charged by banks for NSF cheques.

Industry critics argue that the number of consumers who ‘benefit’ from the discipline imposed by such loans must be weighed against the numbers who may be captured by the debt treadmill or who simply cannot afford to take on any more debt entailed by the fees attached to payday loans.

Critics suggest that the criminally high interest rates generated and industry practices to disguise the true cost of these loans (as measured by APRs) which prevents consumers from being able to compare costs of financial services, necessitates regulation. They assert that the industry targets a modestly waged population who is inherently unable to repay the full costs of the loan within the tight time periods.[114] Thus payday loans have the effect of ‘capturing’ this market

[114] A U.S. Congressional forum in 1999 contained a presentation by Senator Joseph Lieberman, of a scenario showing the inherent inability to repay an average payday loan at the end of a pay period by modest income level families [source: K. Keest, *supra* note 72 at 416].

in a form of debt treadmill, while generating fees to the industry with interest rates in the thousands percent.

They also contend that engaging with this sector has no impact on a consumer's credit rating. Therefore, dependence upon this sector does not assist borrowers to improve their credit rating, a factor that may have been an initial reason for separating such borrowers from mainstream financial institutions.

The key policy issue regarding payday loans may be summarised simply as whether to regulate the industry and if so, how. Opponents of regulation argue that encouraging market-place forces to provide competition will bring prices to the lowest operable level, thus allowing consumer choice.

Proponents of regulation argue that measures are required to prohibit practices that prey upon consumers who may be without alternatives. Regulatory proposals may range from those who believe the *Criminal Code* provision should be actively enforced, which may have the effect of shutting down the industry, to those that argue for the adequacy of improving consumer protection measures. Consumer protection measures focus on the contracts with payday lenders and issues of disclosure or fair practices. Among those who believe protections are necessary, there is no agreement as to what steps ought to be taken.

## 5.0 Options and Recommendations

An examination of the alternative financial services industry cannot help but throw into relief the practices of the mainstream financial sector and encourage a general examination of the financial status of Canadians overall. The results of this survey support the contention made by other observers, of our growing dependence on credit as a society and the particular vulnerability of moderate and low-income consumers as a result of this dependence. It also suggests that customer isolation from or rejection of mainstream financial services has been an important contributing factor to the growth of the AFS.

How consumers make choices in the AFS and their understanding of various costs of financial services also raises the question of the financial literacy of Canadians generally. In response to the charge that AFS customers are uniquely unaware of the cost of financial transactions, it can be argued that the financial literacy of Canadians in general, is poor.

Examination of the practices of the AFS must also be compared to the practices of the mainstream financial sector and how we regulate the financial sector generally. Mainstream financial institutions are quite vulnerable to criticism over the charges that they place on financial services to consumers. Federally regulated banks are required to disclose bank charges[115] but there are no limits placed upon the type or amount of those charges. Customers are regularly faced with increases in bank service charges and fees as well as automatic banking machine fee increases.

The interrelationship between the practices by the mainstream and the recent developments in the alternative financial services sector requires that any meaningful recommendations must include both sectors.

## *5.1 Financial Literacy*

There are measures that can and should be immediately initiated to deal with the important issue of financial literacy, in the form of disclosure and plain language requirements placed on the industry and in the area of consumer assistance and education.

It is clear from this survey and from general surveys of Canadians, that financial illiteracy is a significant factor in the alternative (and mainstream) financial services sector. Payday loan customers do not have a clear idea of the costs of their loans compared to alternatives in the mainstream. Consumers have little understanding of how to compare the various costs of financial services and the meaning of annual percentage rates. Practices among the industry to use a variety of descriptions of fees and charges and non-disclosure of fees in terms of annual percentage rates only contribute to consumers’ financial illiteracy.

While it is not clear what impact improving financial literacy would have on use of the AFS overall, improving economic and financial literacy on the part of all consumers is arguably a critical component of a well-functioning modern democracy. If consumers better understand financial and economic ideas, they can provide an important counterweight to the significant economic clout currently enjoyed by financial institutions. At a minimum it will foster citizens who are much more capable of making informed decisions about their personal financial situations and AFS services.

## *5.2 Recommendations - Financial Literacy*

- **Provincial disclosure of cost of credit legislation should be enacted or updated** to require payday lenders and cheque cashing outlets to post and hand out (at outlets) schedules which include plain language explanations of all the fees and charges associated with payday loans. The description of the

[115] *Disclosure of Charges (Banks) Regulations,* SOR/92-324.

fees and charges should be expressed in annual percentage rates along side the dollar amounts.

- **Credit counselling services** should be actively supported and maintained as publicly funded programs by provincial and federal governments.[116]

- **Increase Availability and Access to Professional Financial Advice**
Consumers have also indicated that they have a need and a desire for access to professional financial advice about managing their personal financial situations.[117] Banks and other financial institutions need to do more to make personal financial advice available to their customers. For example, the National Endowment for Financial Education in the U.S. has recently co-ordinated a pro bono financial planning initiative to provide financial advice and planning advice to low-income Americans. This initiative included participation by institutes of public accountants and financial planners.[118] Equivalent Canadian institutes should be strongly encouraged to commence similar programs.

- **Consumer Education and Information about the AFS**
The recently formed federal agency, the Financial Consumer Agency of Canada, whose mandate includes providing consumer education about financial matters should publish information about the AFS and payday loans, in particular, comparing the APRs of payday loans with alternatives. It should also inform consumers about consumer protection measures relevant to the AFS.

Any or all of these measures would enable consumers to better evaluate services such as cheque cashing and payday loans in terms of more cost-effective options. As the proliferation of direct deposit continues to eat away at the cheque cashing side aspect their business, the AFS industry will attempt to advertise aggressively to emphasis the payday loan component of their business.

However, assisting consumer literacy is only one component of the overall picture. Legislative and regulatory mechanisms are needed to address the substance of industry practices both in the mainstream and alternative sectors.

---

[116] Unfortunately, some governments are moving in the opposite direction. The province of B.C. has recently eliminated its debtor assistance branch. [Source: M. Kane, "Don't Axe Debtor Assistance, Victoria Urged: The Existing Program Costs Little and Helps Many, its Defenders Argue" *Vancouver Sun* (7 March 2002) F5.]
[117] Canadian Bankers Association, *supra* note 106 at 8.
[118] National Endowment for Financial Education, *Nefe Digest* (September/October 2002) at 1.

## 5.3 Legislative/Regulatory Responses

Despite economists' views of the rational or quasi-rational exchange, which characterises the interaction of consumers with the marketplace, governments intervene in markets to correct inequities or prohibit behaviours which society judges as being morally or wrong. The federal usury law was designed to combat loan sharking, deemed as a societal wrong.[119]

When all fees and interest are taken into account, payday-lending companies are clearly contravening the federal usury law in the *Criminal Code.* Regulators, however, have been reluctant to intervene in this area. Understanding this reluctance requires looking at the larger context, both with respect to the 'reach' of the provision itself and the regulatory practices of federal and provincial governments with respect to the mainstream financial sector.

Federally incorporated financial institutions are subject to minimal government regulation concerning their customer practices. The federal government regulates the customer account practices of federally regulated banks with respect to disclosure of bank charges, interest on deposit accounts and the cost of borrowing. The nature and amount of those charges is not subject to regulation. It is also important to note that the usury provision in the *Criminal Code*, section 347, specifically excludes overdraft charges by banks or credit unions, thus allowing overdraft charges to exceed an APR of 60%.

The closure of branch locations by major banks is another area where a passive response by government has likely contributed to the growth of the alternative financial services sector. Many of the areas in which branch closures have taken place are locations that are already poorly served by financial institutions and which may provide an opening for payday lenders to enter the resulting gap in financial services.

Federal and most provincial governments have also done little to encourage better services for credit-dependent Canadians. Neither the federal or provincial governments have required the banking or credit union industry to engage in small loan lending to individuals or to ensure that small-volume customers have access to lines of credit or overdraft protection. Federal and provincial governments have also paid minimal attention to ensure access to basic banking services such as opening of personal deposit accounts and cheque cashing services for non-bank customers.

Quebec provides an interesting exception. The credit-union movement has recently set up pilot projects across the province, in which small loans (i.e. $500)

[119] See *Garland* v. *Consumers' Gas*, *supra* note 46 at para. 25.

will be made available to low-income persons at rates of interest, which are below prime.[120] The existence of credit unions has also significantly delayed the growth of payday lenders and cheque cashing services in Quebec. The strong presence of credit unions in Quebec has traditionally meant greater access by low-income persons to bank accounts. Ramsay noted that only 2.5% of adults in Quebec with incomes under $25,000 did not have bank accounts, compared to 10.4% in the rest of Canada.[121]

However, credit union practices may be changing and the prohibition may not be having the same effect on the industry, as a survey of MoneyMart's website reveals 16 locations in the City of Montreal alone.

The federal government's position of minimal regulation of the mainstream financial sector does not create a strong rationale for it to target solely the practices of the alternative financial sector. This fact may explain governments' 'inertia' with respect to prosecution of payday lenders who are clearly in violation of the *Criminal Code.*

Another important reason for this inertia may be the impact of the provision on the commercial marketplace. Section 347 has been applied to some commercial loan practices. Critics suggest that the extremely broad reach of the provision is unsuitable for most commercial loan transactions. Such transactions may include new commercial ventures, which are inherently risky, making it logical that lenders should take a high percentage of such loans. The provision also 'captures' commercial activities where both parties anticipate a substantial profit or increase in the value of an asset being financed by the loan transaction and the lender seeks to capture a fixed amount of that profit.[122] These critics view the provision as a major deterrent to economic development and the operation of commercial markets.

In light of this background, the next section explores legislative and/or regulatory options open to policy makers in relation to the AFS.

## *5.4 Options*

- **Enforce section 347 of the C*riminal Code***

The decision of the Supreme Court in *Garland* resulted a broad interpretation of section 347 of the *Criminal Code*, lending strong support for an argument that the fees and charges attached to payday loans bring such loans within the definition of a "criminal interest rate". As discussed above, recent lower court decisions

[120] D. Macdonald, "Debt Treadmill" *The [Montreal] Gazette* (13 October 2001) C1.
[121] Ramsay, *supra* note 11 at 2.
[122] Waldron, M.A., "Section 347 of the *Criminal Code*: "A Deeply Problematic Law"" (Paper prepared for the Uniform Law Conference of Canada Annual Meeting, 2002) at 2-6.

concerning payday lenders have disallowed the associated fees and charges attached to a payday loan, holding that they come within the definition of section 347. They have also clearly reinforced the public policy rationale behind the adoption of section 347, which was rooted in the recognition of the inequality of bargaining power inherent in short-term loan transactions.

The federal government and the provincial Attorneys General clearly have judicial precedents to support prosecution of payday lenders under the *Criminal Code*. Such an application could have a significant effect in severely reducing or even eliminating the industry. For the reasons identified above, these prosecutions have not been pursued, which have led some critics to call for the elimination of the provision.

One danger of entering into active prosecution before enacting any changes in the current practices by the mainstream financial services sector would be that the short-term loan option would be eliminated without ensuring that there are any alternatives in place for those consumers in urgent need of credit.

There is also an argument that the continued presence of the provision, although not enforced, provides one of the few levers that governments have over the industry.

However, it may also prevent any meaningful regulation of the industry. The provision as it stands renders the payday loan contract illegal, perhaps inhibiting provinces or territories from enacting legislation to regulate the industry.

- **Amend section 347 of the *Criminal Code***

Critics have suggested amending section 347 to resolve the dilemma of finding the appropriate balance between the need to protect consumers engaging in expensive and high risk short-term loan transactions and the need of the commercial community to have the freedom to engage in commercial loan transactions that may involve high interest rates. This could be accomplished by exempting from prosecution loans made by a lending company regulated under applicable provincial legislation.[123] This would encourage provinces to regulate the industry, as the payday loan contract would no longer be illegal.

However, such an amendment is premised upon there being applicable provincial legislation in place across the country. This is a significant hurdle, as it not clear that all provinces/territories have a desire to regulate the industry. It also requires federal-provincial co-operation and co-ordination.

The other concern raised by this approach is that it does not ensure that consumer will be protected from the excessively high fees and charges of the

[123] *Ibid.* at 23.

AFS. Exempting payday lenders from the application of section 347 without any assurance that provincial legislation will be enacted that would set significant limits on the fees attached to payday loans, will only further jeopardise consumers engaged with the AFS, by removing the industry from any form of interest rate oversight.

The perspective revealed by some of the adherents of amending this provision (and indirectly by the inaction of governments on this issue) is ambivalence about extremely high interest rates and a related assumption that payday lenders may fulfil a legitimate market need:

> …payday lenders are not usually considered the type of lender that loan sharking provisions are meant to prosecute. In fact, they may provide a needed service for some parts of the credit market. The solution to their activities is probably not criminal prosecution, but regulation under provincial statutes with licensing requirements and reporting rules.[124]

This argument fails to consider the public policy objectives behind section 347, to protect the public from exorbitantly high interest rates and from the inequality of bargaining power that in usually inherent in these short-term loan transactions.

This argument also fails to appreciate the significant economic gap between the situation of those with the financial ability to engage in commercial loan transactions and consumers using payday loans because their paycheques do not meet their day-to-day needs. The other key element missing from the above perspective is an acknowledgement that the presence of the AFS is evidence of the failure of the mainstream financial sector to reasonably serve the basic financial needs of a significant segment of the consumer market.

- **Industry self regulation**

The federal government has chosen to allow federal banks to monitor their practices in a number of areas. Although it is arguable how effective self-regulation has been, its emergence required the presence of a strong industry association, the Canadian Bankers Association. In contrast, a few very large players, and number of very small players constitute the payday lending industry. There is currently no AFS industry association in Canada, unlike the U.S.

There is, however, a more pragmatic reason that would inhibit the success of self-regulation. In the complete absence of any strong indication by the federal or provincial governments of concern over the practices and fees of the payday loan industry, the industry has no incentive to enter into any kind of self-regulation or voluntary code of conduct

[124] *Ibid.* at 22-23.

- **Provinces and territories should update regulatory framework to ensure consumer protection statutes capture the industry**

There is no uniformity between provincial/territorial jurisdictions with respect to aspects of consumer protection legislation that have applicability to the AFS. The Uniform Law Conference of Canada has enacted uniform disclosure of cost of credit legislation. This legislation, or a variation of it, has been adopted in only a few provinces: Saskatchewan, British Columbia, Nova Scotia and Ontario.

In Ontario, the applicable disclosure provisions have been located in the *Consumer Protection Act* and there are specific provisions relating specifically to disclosure of interest rates by short-term lenders. For some unknown reason, however, these provisions have not yet been proclaimed, so are not in force.[125]

Most provinces have adopted trade practices legislation or unconscionable transaction relief acts. This legislation could be used to protect consumers from deceptive and unfair practices engaged in by the AFS.

Eliminating the inconsistent patchwork of consumer protection directed to the AFS would be one important step in protecting consumers from the risks associated with the AFS.

- **Enact legislation to specifically regulate payday lenders**

Saskatchewan's *Trust and Loan Companies Act* provides an example of licensing legislation, which may apply to payday lenders. This legislation does not contain any statutory provisions specifically applicable to payday lenders, but its definition of "financing corporations" covered under the act is applicable to payday lenders. Such legislation gives the power to attach conditions to those licenses which may include ceilings on fees to comply with the criminal interest rate, restrictions on fees charged for payday loans and other services, and loan limits. .

Quebec, New Brunswick, Newfoundland and Nova Scotia also have licensing regimes under consumer protection statutes that require moneylenders to register with the relevant ministry. These various pieces of legislation also give the power to impose terms and conditions upon registration, but there are no terms and conditions yet defined in the acts or regulations that would have direct impact on the problems created raised by payday loans.

In the U.S. a national consumer information and legal advocacy agency, the National Consumer Law Center[126], has created a model act called the "Deferred

[125] *Consumer Protection Act*, R.S.O. 1990, c. C.31,
[126] National Consumer Law Center, online at http://www.consumerlaw.org/

Deposit Loan Act”. The model act sets out a licensing regime that is somewhat similar to the Saskatchewan Act. However, the model act is targeted specifically to payday lenders and sets out mandatory terms and conditions attached to licenses.

The act describes a series of prerequisites which must be met before licensing as well as required acts which include: minimum terms for loans, a maximum amount for a payday loan, the ability for the borrower to make partial payments on the loan, and permitted charges attached to loans with a limit on fees and ceilings on interest rates.

The act also sets out required disclosures which include: information pamphlets explaining the consumers rights and responsibilities in a payday loan transaction, a loan document itemising the fees and interest charges, posting requirements for those disclosures, disclosing the corresponding annual percentage rate associated with the fees and charges. It also describes prohibited acts, which may include rollovers of existing loans and use of one payday loan to pay off another.

There is an argument that the existence of section 347 prevents provinces/territories from being able to enact payday loan legislation because these businesses are engaged in illegal contracts. However, Saskatchewan has already enacted legislation that is applicable to payday lenders, although there are no provisions specifically directed to that industry. It is difficult to know, therefore, why the presence of section 347 is a bar to such legislation. Presumably this legislation could impose licensing conditions, which could commence with ceilings on the fees and charges attached to payday loans to bring them within the legal interest rate.

A decision to criminally prosecute this practice without ensuring alternative sources of credit are available by mainstream financial services, may eliminate the industry, but would not serve the needs of those consumers who are turning to the AFS due to urgent need for credit.

A decision to amend the criminal interest rate provision to exempt the payday loan industry, without ensuring that all provinces/territories would ‘buy in’ to regulation of this industry with respect to its fees and charges and the risk element entailed in loan rollovers, could severely harm consumers, by removing any legislative oversight, however dormant.

However, this does not mean that governments should do nothing in the absence of criminal prosecution or amendment of section 347. Payday lenders are engaged in an extremely lucrative business, targeted to financially vulnerable consumers, and charging fees attached to those services that are exorbitantly high.

A combination of mainstream and AFS-targeted legislative and regulatory measures needs to be put in place at the federal and provincial/territorial level. These measures would ensure that the AFS is licensed under mandatory conditions, that consumer protection measures with respect to disclosure and fair practices are in place and directly applicable to the AFS, and that mainstream financial institutions offer credit services targeted to financially vulnerable consumers at reasonable prices.

## *5.5 Recommendations*

- **Mainstream Financial Institutions to Improve/Expand Services**

  The federal and provincial/territorial governments should actively encourage financial institutions to engage in small-loan lending at reasonable rates and offer lines of credit and overdraft protection to small-volume customers.

  The federal government and provincial/territorial governments should enact legislative changes to ensure easier access for modest and low-income consumers to basic banking services such as personal deposit accounts and cheque cashing services for non-bank customers.

  The federal government has indicated its intention to improve access to basic banking services as a result of Bill C-8, which introduced a series of changes to financial services legislation as well as establishing the Financial Consumer Agency of Canada. The federal government is urged to carry through legislative changes that will improve access to basic banking services.

  Initiatives in any or all of these areas could have a significant impact upon whether consumers turn to alternative financial services.

- **Ensure Provincial and Territorial Consumer Protection Framework Applies to the AFS**

  It is well beyond the scope of this report, but a comprehensive inventory and analysis of the existing consumer protection framework in provinces and territories should be undertaken to assess the extent to which existing legislation is currently applicable to the AFS. This would include consumer protection statutes and regulations, cost of credit disclosure legislation, and unconscionable transactions and trade practices legislation.

This information would then enable federal and provincial/territorial regulators to update the current consumer protection framework with respect to disclosure and unfair or unconscionable practices to be directly applicable to the AFS.

- **License the AFS**

  Improving the existing disclosure of information and unfair practices legislation can only be part of the solution, because it does not address the core practices that have raised the concerns outlined in this report, such as the high and disguised fees attached to payday loans and the loan rollover phenomenon. Therefore, a licensing regime should also be put in place that would attach conditions to licenses, such as limits on fees and charges, and provide for an active monitoring function of these licensees.

  The Saskatchewan's *Trust and Loan Corporations Act* provides a model for legislation which may apply to payday lenders by giving powers to license payday lenders and attach conditions to those licenses. A stronger alternative would be legislation specifically targeted to the AFS with mandatory licensing conditions which would clearly set out that the fees and charges attached to payday loans fall within the usury provision and therefore must be below the 60% limit.

  The Uniform Law Conference of Canada should enact a model statute, similar to the U.S. "Deferred Deposit Loan Act". This model act would provide an example of comprehensive legislation that would ensure mandatory controls on the AFS to eliminate usurious fees and charges and prevent rollovers of payday loans.

## *5.6 Conclusion*

As a final cautionary note, it is important to place all of these recommendations within the broader socio-economic context. Fundamental reasons for growth of the AFS include our significant dependence upon and increasing tolerance of credit, the increasingly high debt-to-income ratios of average and low-income Canadians, and the stagnating incomes of average and low-income Canadians who constitute the bottom 75% of Canadian families.

All of these factors will continue to drive consumers toward the AFS, notwithstanding any amount of regulation, until and unless the underlying economic conditions that have created this dependence on credit for growing numbers of Canadian consumers change.

## Bibliography

*Affordable Payday Loans* v. *Harrison*, [2002] A.J. No. 824, online: QL (ABPC)

Bruch, C. "Taking the Pay Out of Payday Loans: Putting an End to the Usurious and Unconscionable Interest Rates Charged by Payday Lenders" (2001) 69 U. of Cincinnati Law Review 1257

*Business Practices Act,* R.S.O. 1990, c. B. 17, s. 2

Canadian Bankers Association and Canadian Foundation for Economic Education. *Survey of Canadians' Economic and Financial Understanding* (December 1997)

Canadian Council on Social Development. *The Personal Security Index, 2002: After September 11th*

*C.A.P.S. International Inc.* v. *Kotello*, [2002] M.J. No. 205

*Cash Store (Advance Finance Co.)* v. *Lajoie,* [2002] A.J. No. 780, online: QL (CJ)

Caskey, J. "Payday Lending" (2001) 12(2) The Journal of the Association for Financial Counselling and Planning Education 1

Consumer Federation of America and U.S. Public Interest Research Group. "Rent-A-Bank Payday Lending: How Banks Help Payday Lenders Evade State Consumer Protections" (November 2001)

*Consumer Protection Act*, R.S.O. 1990, c. C.31

*Cost of Borrowing (Banks) Regulations,* SOR/2001-101

*Cost of Credit Disclosure Act*, R.S.S. 1978, c. 21

*Criminal Code,* R.S.C. 1985, c. C-46

*Dean's Cash Connection Ltd.* v. *Nelson-Wiger,* [2001] A.J. No. 246, online: QL (CJ)

*Disclosure of Charges (Banks) Regulations,* SOR/92-324

*Disclosure of Interest (Banks) Regulations,* SOR/92-321

Dollar Financial Group, Inc. *Annual Report to the Securities and Exchange Commission for the Fiscal Year Ended June 30, 2001*

Drysdale, L. and K. Keest. "The Two-Tiered Consumer Financial Services Marketplace: The Fringe Banking System and Its Challenge to Current Thinking About the Role of Usury Laws in Today's Society" (2000) 51 South Carolina Law Review 589

Duggan, T. "Access to Credit in the Alternative Consumer Credit Market: An Australian Comparison" (2001) 35 Canadian Business Law Journal 402

Ekos Research Associates Inc. Public Opinion Research Relating to the Financial Services Sector (Ottawa: The Task Force on the Future of the Canadian Financial Services Sector, 1998)

Elliehausen, G. and E.C. Lawrence. "Payday Advance Credit in America: An Analysis of Customer Demand" (Credit Research Center, Georgetown University: April 2001)

Foust, D. "Easy Money" *Business Week* (24 April 2000) 108

Fox, J.A. "The Debt Cycle: Using Payday Loans to Make Ends Meet". Paper prepared for NEFE/CFA Forum, February 28, 2002

*Garland* v. *Consumers' Gas Co,* [1998] 3 S.C.R. 112

Jackson, B. "Can't Rent?  Payday Shop Files to Buy a Charter" *American Banker* (9 July 2002)

Kane, M. "Don't Axe Debtor Assistance, Victoria Urged: The Existing Program Costs Little and Helps Many, its Defenders Argue" *Vancouver Sun* (7 March 2002) F5

Kari, S. "Street Smart" *Report on Business Magazine* (April 2000) 100

Keest, K. "Credit in the Alternative Financial Sector: The U.S. Experience" 35 Canadian Business Law Journal (2001) 409

Kilborn, P. "New Lenders with Huge Fees Thrive on Workers with Debts" *The New York Times* (18 June, 1999) A1

Koerner, B.I. "Preying on Payday" (May 2001) 26 *Mother Jones* 19

Lawson, P. *Eliminating Phonelessness in Canada: Possible Approaches 2d ed.* (Ottawa: Public Interest Advocacy Centre, 2002)

"Legislators Review Payday Lending Practices" (2000) 26 *State Legislatures* 9

Lydersen, K. "Payday Profiteers: Payday Lenders Target the Working Poor" *Multinational Monitor* (October 2001) 9

Lynch, M. "Legal loan sharking or essential service? The great "payday loan" controversy" *Reason* (April 2002) at 38

Macdonald, D. "Debt Treadmill" *The [Montreal] Gazette* (13 October 2001) C1

Menzies, D. "Waiting for payday" *Financial Post (National Post)* (22 September, 2001) D4

Minister of Industry, News Release, "Consumer Ministers Take Action to Improve Consumer Protection in the Evolving Marketplace" (25 May 2001)

*National Bank Act* 12 U.S.C. § 85 (1994)

National Endowment for Financial Education. *Nefe Digest* (September/October 2002)

Queensland Office of Fair Trading. *Payday Lending – A Report to the Minister for Fair Trading* (August 2000)

*Racketeering Influenced and Corrupt Organizations Act* 18 U.S.C.S. § 1961 n.1 (1991)

Ramsay, I. "Access to Credit in the Alternative Consumer Credit Market". Paper prepared for the Office of Consumer Affairs, Industry Canada and the Ministry of the Attorney General, British Columbia February 1, 2000

Reid, H. *A Garland for Consumers: Will the Garland Case Provide Safeguards for Vulnerable Consumers?* (Ottawa: Public Interest Advocacy Centre, 2000)

Reosti, J. "Why Republic First Still Likes Tax, Payday Loans" *American Banker* (2 July 2002)

*Small Loans Act,* R.S.C. 1970, c. S-11

Statistics Canada, *The Daily* (18 July 2002)

Stephens Inc. "The Developing "Payday Advance" Business", (September 28, 1999)

———. "The Emerging Business of Deferred Presentment (Payday Advance)" (April 1, 1999)

*The Trust and Loan Corporations Act*, R.S.S. 1997, c. T-22.2

*Truth in Lending Act* 15 U.S.C. §§ 1601-1693r (1994)

Waldron, M.A. "Section 347 of the *Criminal Code*: "A Deeply Problematic Law"". Paper prepared for the Uniform Law Conference of Canada Annual Meeting, 2002

Weissbourd, R. *Banking on Technology: Expanding Financial Markets and Economic Opportunity* (June 2002)

Wilson, D. *Payday Lending in Victoria – A Research Report* (Melbourne: Consumer Law Centre Victoria Ltd, 2002)

# Appendix A: Household Survey Questionnaire

## Alternative Finance Sector Survey
## September-October 2001

RESPONDENT ______________________________________________

TELEPHONE # ____________________ DATE: ____________________

POSTAL CODE ______________________________________________

INTERVIEWER ______________________________________________

SUPERVISOR _______________________________________________

TIME START: ___________ STOP: _______________= ________ MINS

Hello, my name is _____________ of Forum Research, a market research firm. We are doing a survey today on sources of financing.

A. How many people over the age of 15 live in your household in total?

| | |
|---|---|
| One only | 1 |
| Two | 2 |
| Three | 3 |
| Four | 4 |
| Five | 5 |
| Six | 6 |
| Seven or more | 7 |

B. Have you or has anyone in your household 15 years or older ever gotten a cash advance or credit from any of the following sources in the past three years? **(READ LIST. CIRCLE ALL THAT APPLY)**

| | |
|---|---|
| A payday lending company (like Money Mart, Stop 'n' Cash or Financial Stop, where you are are advanced cash against your paycheque) | 1 |
| A pawnshop, where you are are advanced cash against personal items left as security | 2 |

| | |
|---|---|
| A cheque cashing outlet (like Money Mart or Cash Stop) | 3 |
| A cash advance on a credit card (excluding normal credit card purchases) | 4 |
| A debt consolidation loan from a finance company (like Avco Financial or HFC) | 5 |
| NONE OF THE ABOVE | 0 |

**IF "NONE OF THE ABOVE", THANK AND TERMINATE. ALL OTHERS CONTINUE**

**ASK TO SPEAK TO THE PERSON IN THE HOUSEHOLD WHO QUALIFIES. IF MORE THAN ONE, ASK FOR THE ONE WHO IS AVAILABLE. RE-INTRODUCE YOURSELF IF NERCESSARY.**

PAYDAY LENDING

**IF ANY "PAYDAY LENDING" (CODE 1 AT Q. A), ASK Q. 1. ALL OTHERS SKIP TO Q. 2.**

1a. The last time you obtained a payday advance, which company did you use? **(DO NOT READ LIST. CIRCLE OR WRITE IN VERBATIM)**

| | |
|---|---|
| Money Mart | 1 |
| Cash Stop | 2 |
| Stop 'n' Cash | 4 |
| Financial Stop | 5 |
| UniCash | 6 |

OTHER (SPECIFY) ________________________________

1b. How often have you used payday advances in the past three years?

______________________________

**WRITE IN # OF TIMES**

Once only 1 → **SKIP TO Q1d.**

1c. How often have you gotten a payday advance more than one paycheque in a row? Would you say you do this…**(READ LIST. CIRCLE ONE ONLY)**…?

| | |
|---|---|
| Frequently | 3 |
| Sometimes | 2 |
| Rarely | 1 |

| | | |
|---|---|---|
| *or* | Never | 0 |

1d. Have you ever had difficulty paying off a payday advance on time?

| | |
|---|---|
| Yes | 1 |
| No | 2 → **SKIP TO Qf** |

1e. Have any of the following occurred as a result of having difficulty paying off this payday advance? **(READ LIST. CIRCLE ALL THAT APPLY. ROTATE ORDER OF STATEMENTS STARTING AT THE "X")**

| | |
|---|---|
| Harassing telephone calls to my home | 1 |
| Harassing telephone calls to my work | 2 |
| Payday loans company cashed the cheque I left as security for my advance | 3 |
| Incurred NSF charges on my cheque | 4 |
| NONE OF THESE | 0 |

For the next couple of questions, please think only about the last time you used a payday advance loan

1f. Where did you hear or learn about **(READ COMPANY FROM Q1a. DO NOT READ LIST. CIRCLE ALL THAT APPLY OR WRITE IN VERBATIM)**?

| | |
|---|---|
| TV/radio advertising | 1 |
| Posters/billboards/transit ads | 2 |
| Newspaper/magazine advertising | 3 |
| Advertising (unspecified) | 4 |
| Friends/relatives | 5 |
| Word of mouth | 6 |
| Saw outlet/sign on the street | 7 |
| OTHER (SPECIFY) | ______________________ |

1g. Which of the following reasons best describes the purpose for which you got this payday advance? **(READ LIST. ROTATE ORDER, STARTING AT THE "X". CIRCLE ALL THAT APPLY). PROBE:** What other reasons? Any other reasons?

| | |
|---|---|
| To cover day-to-day expenses | 1 |
| To pay the rent | 2 |
| To pay utilities | 3 |
| To pay other bills, loans or debts | 4 |
| For an emergency like illness or car repair | 5 |

| | |
|---|---|
| For recreation | 6 |
| For a major purchase | 7 |
| To avoid bouncing a cheque | 8 |
| OTHER (SPECIFY) | ____________ |

1h. How important was each of the following factors in your decision to go to **(READ COMPANY FROM Q1a)** for a payday advance? Would you say it was very important, somewhat important, not very important or not at all important that…**(READ EACH FACTOR IN TURN. CIRCLE ONE NUMBER FOR EACH. RORATE ORDER OF STATEMENTS STARTING AT THE "X")**

| | **Very** | **Some-what** | **Not very** | **Not at all** |
|---|---|---|---|---|
| It was close to where I live or work | 4 | 3 | 2 | 1 |
| I compared prices, it has best rates | 4 | 3 | 2 | 1 |
| The staff is friendly and helpful | 4 | 3 | 2 | 1 |
| It was the only place that would give me cash | 4 | 3 | 2 | 1 |
| The service is confidential | 4 | 3 | 2 | 1 |
| The atmosphere is friendly and welcoming | 4 | 3 | 2 | 1 |

1j. What was the amount of this payday advance?

____________________

**WRITE IN $ AMOUNT**

1k. As far as you know, how much did this payday advance cost you in fees and interest? **(WRITE IN <u>EITHER</u> DOLLAR AMOUNT OR PERCENT, DEPENDING ON RESPONDENT'S ANSWER)**

____________________ ____________________

**WRITE IN $ AMOUNT** ***<u>OR</u>*** **WRITE IN %**

| | |
|---|---|
| DON'T KNOW | 1 |

1l. How satisfied are you overall with the service you received from this payday advance company? Were you…**(READ LIST. CIRCLE ONE)**

| | | |
|---|---|---|
| | Very satisfied | 4 |
| | Somewhat satisfied | 3 |
| | Not very satisfied | 2 |
| *<u>or</u>* | Not at all satisfied | 1 |

1m. How would you rate your satisfaction with **(READ COMPANY FROM Q1a)** for the following? Would you say you are very satisfied, somewhat satisfied, not very satisfied or not at all satisfied with them for…**(READ EACH FACTOR IN TURN. CIRCLE ONE NUMBER FOR EACH. ROTATE ORDER OF STATEMENTS STARTING WITH "X")**…?

| | Very | Some-what | Not very | Not at all |
|---|---|---|---|---|
| Having the lowest rates | 4 | 3 | 2 | 1 |
| Explaining the cost of advances clearly | 4 | 3 | 2 | 1 |
| Friendliness of the staff | 4 | 3 | 2 | 1 |
| Ease of paperwork | 4 | 3 | 2 | 1 |
| Offering convenient location | 4 | 3 | 2 | 1 |
| Offering convenient hours | 4 | 3 | 2 | 1 |

1n. How likely are you to use payday advances in the future? Would you say you are…**(READ LIST. CIRCLE ONE)**…to do so?

| | | |
|---|---|---|
| | Very likely | 4 |
| | Somewhat likely | 3 |
| | Not very likely | 2 |
| *or* | Not at all likely | 1 |

1o. If you were unable to get the cash you needed from a payday lender, because that provider was not available in your area, what other source would you turn to for the cash you need? **(DO NOT READ LIST. CIRCLE ALL THAT APPLY)**

| | |
|---|---|
| A pawnshop | 2 |
| A cheque cashing outlet | 3 |
| A credit card advance | 4 |
| A finance company loan | 5 |
| Family or friends | 6 |
| Loansharks | 7 |
| A bank or trust company | 8 |
| Would do without the money | 9 |
| OTHER (SPECIFY) | ____________________ |

**NOW SKIP TO Q. 6**

**PAWNSHOP**

**IF NO "PAYDAY LENDING" CIRCLED (CODE 1 AT Q. A), BUT "PAWNHOP " IS CIRCLED (CODE 2 AT Q. A) ASK Q2. OTHERS SKIP TO Q3.)**

2a. **NO Q2A**

2b. How often have you used pawnshops in the past three years?

____________________
WRITE IN # OF TIMES

| | |
|---|---|
| Once only | 1 |

2c. NO Q2C

2d. Have you ever had difficulty paying off a pawnshop loan on time?

| | |
|---|---|
| Yes | 1 |
| No | 2 → SKIP TO Q2f |

2e. Have any of the following occurred as a result of having difficulty paying off this pawnshop loan? **(READ LIST. ROTATE ORDER OF MENTION STARTING AT THE "X". CIRCLE ALL THAT APPLY)**

| | |
|---|---|
| Harassing telephone calls to my home | 1 |
| Harassing telephone calls to my work | 2 |
| Pawnshop sold my property | 5 |
| NONE OF THESE | 0 |

For the next couple of questions, please think only about the last time you used a pawnshop

2f. Where did you hear or learn about the pawnshop you used? **(DO NOT READ LIST. CIRCLE ALL THAT APPLY)**

| | |
|---|---|
| TV/radio advertising | 1 |
| Posters/billboards/transit ads | 2 |
| Newspaper/magazine advertising | 3 |
| Advertising (unspecified) | 4 |
| Friends/relatives | 5 |
| Word of mouth | 6 |
| Saw outlet/sign on the street | 7 |
| OTHER (SPECIFY) | ____________________ |

2g. Which of the following reasons best describes the purpose for which you got cash from a pawnshop? **(READ LIST. ROTATE ORDER STARTING AT THE "X". CIRCLE ALL THAT APPLY). PROBE:** What other reasons? Any other reasons?

| | |
|---|---|
| To cover day-to-day expenses | 1 |
| To pay the rent | 2 |

| | |
|---|---|
| To pay utilities | 3 |
| To pay other bills, loans or debts | 4 |
| For an emergency like illness or car repair | 5 |
| For recreation | 6 |
| For a major purchase | 7 |
| To avoid bouncing a cheque | 8 |
| OTHER (SPECIFY) | ____________________ |

2h. How important was each of the following factors in your decision to go to a pawnshop for cash? Would you say it was very important, somewhat important, not very important or not at all important that…**(READ EACH FACTOR IN TURN. CIRCLE ONE NUMBER FOR EACH. ROTATE ORDER OF FACTORS STARTING AT THE "X")**

| | **Very** | **Some-what** | **Not very** | **Not at all** |
|---|---|---|---|---|
| It was close to where I live or work | 4 | 3 | 2 | 1 |
| I compared prices, it has best rates | 4 | 3 | 2 | 1 |
| The staff is friendly and helpful | 4 | 3 | 2 | 1 |
| It was the only place that would give me cash | 4 | 3 | 2 | 1 |
| The service is confidential | 4 | 3 | 2 | 1 |
| The atmosphere is friendly and welcoming | 4 | 3 | 2 | 1 |

2j. What was the amount of the cash you got?

____________________________

**WRITE IN $ AMOUNT**

2k. **NO Q2K.**

2l. How satisfied are you overall with the service you received from this pawnshop? Were you…**(READ LIST. CIRCLE ONE)**

| | | |
|---|---|---|
| | Very satisfied | 4 |
| | Somewhat satisfied | 3 |
| | Not very satisfied | 2 |
| *or* | Not at all satisfied | 1 |

2m. How would you rate your satisfaction with this pawnshop for the following? Would you say you are very satisfied, somewhat satisfied, not very satisfied or not at all satisfied with them for…**(READ EACH FACTOR IN TURN. CIRCLE ONE NUMBER FOR EACH. ROTATE ORDER OF STATEMENTS, STARTING WITH "X")**…?

| | Very | Some-what | Not very | Not at all |
|---|---|---|---|---|
| Having the lowest rates | 4 | 3 | 2 | 1 |
| Explaining the cost of advances clearly | 4 | 3 | 2 | 1 |
| Friendliness of the staff | 4 | 3 | 2 | 1 |
| Ease of paperwork | 4 | 3 | 2 | 1 |
| Offering convenient location | 4 | 3 | 2 | 1 |
| Offering convenient hours | 4 | 3 | 2 | 1 |

2n. How likely are you to use pawnshops in the future? Would you say you are…**(READ LIST. CIRCLE ONE)**…to do so?

| | | |
|---|---|---|
| | Very likely | 4 |
| | Somewhat likely | 3 |
| | Not very likely | 2 |
| *or* | Not at all likely | 1 |

2o. If you were unable to get the cash you needed from a pawnshop, because there were none in your area, what other source would you turn to for the cash you need? **(DO NOT READ LIST. CIRCLE ALL THAT APPLY)**

| | |
|---|---|
| A payday loan | 1 |
| A cheque cashing outlet | 3 |
| A credit card advance | 4 |
| A finance company loan | 5 |
| Family or friends | 6 |
| Loansharks | 7 |
| A bank or trust company | 8 |
| Would do without the money | 9 |
| OTHER (SPECIFY) | ______________________ |

**NOW SKIP TO Q. 6**

**CHEQUE CASHING**

**IF NO "PAYDAY LENDING" (CODE 1 AT QA) OR "PAWNSHOPS" (CODE 2 AT QA) CIRCLED, BUT "CHEQUE CASHING" (CODE 3 AT QA) IS CIRCLED, ASK Q. 3. ALL OTHER SKIP TO Q 4.**

3a. The last time you used a cheque cashing company, which company did you use? **(DO NOT READ LIST. CIRCLE OR WRITE IN VERBATIM)**

| | |
|---|---|
| Money Mart | 1 |

| | |
|---|---|
| Cash Stop | 2 |
| Stop 'n' Cash | 4 |
| Financial Stop | 5 |
| UniCash | 6 |
| OTHER (SPECIFY) ______________________ | |

3b. How often have you used cheque-cashing services in the past three years?

______________________
**WRITE IN # OF TIMES**

Once only 1 → **SKIP TO Q3f.**

3c. How often have you used cheque-cashing outlets for more than one paycheque in a row? Would you say you do this…**(READ LIST. CIRCLE ONE ONLY)**…?

| | | |
|---|---|---|
| | Frequently | 3 |
| | Sometimes | 2 |
| | Rarely | 1 |
| *or* | Never | 0 |

3d. **NO Q3D.**

3e. **NO Q3E.**

For the next couple of questions, please think only about the last time you used a cheque cashing company.

3f. Where did you hear or learn about **(READ COMPANY FROM Q3a. DO NOT READ LIST. CIRCLE ALL THAT APPLY OR WRITE IN VERBATIM)**?

| | |
|---|---|
| TV/radio advertising | 1 |
| Posters/billboards/transit ads | 2 |
| Newspaper/magazine advertising | 3 |
| Advertising (unspecified) | 4 |
| Friends/relatives | 5 |
| Word of mouth | 6 |
| Saw outlet/sign on the street | 7 |
| OTHER (SPECIFY) | ______________ |

3g. Which of the following reasons best describes the purpose for which you got this cash? **(READ LIST, ROTATE ORDER STARTING AT THE "X". CIRCLE ALL THAT APPLY). PROBE:** What other reasons? Any other reasons?

| | |
|---|---|
| To cover day-to-day expenses | 1 |
| To pay the rent | 2 |
| To pay utilities | 3 |
| To pay other bills, loans or debts | 4 |
| For an emergency like illness or car repair | 5 |
| For recreation | 6 |
| For a major purchase | 7 |
| To avoid bouncing a cheque | 8 |
| OTHER (SPECIFY) | ____________________ |

3h. How important was each of the following factors in your decision to go to **(READ COMPANY FROM Q3a)** to cash your cheque? Would you say it was very important, somewhat important, not very important or not at all important that…**(READ EACH FACTOR IN TURN. CIRCLE ONE NUMBER FOR EACH)**

| | **Very** | **Some-what** | **Not very** | **Not at all** |
|---|---|---|---|---|
| It was close to where I live or work | 4 | 3 | 2 | 1 |
| I compared prices, it has best rates | 4 | 3 | 2 | 1 |
| The staff is friendly and helpful | 4 | 3 | 2 | 1 |
| It was the only place that would give me cash | 4 | 3 | 2 | 1 |
| The service is confidential | 4 | 3 | 2 | 1 |
| The atmosphere is friendly and welcoming | 4 | 3 | 2 | 1 |
| No hold was put on my cheque | 4 | 3 | 2 | 1 |

3j. What was the amount of the cheque you cashed?

____________________
**WRITE IN $ AMOUNT**

3 k. As far as you know, how much did it cost you in fees and interest to cash this cheque? **(WRITE IN EITHER DOLLAR AMOUNT OR PERCENT, DEPENDING ON RESPONDENT'S ANSWER)**

____________________ ____________________
**WRITE IN $ AMOUNT** ***OR*** **WRITE IN %**

DON'T KNOW 1

3l. How satisfied are you overall with the service you received from this cheque cashing company? Were you…**(READ LIST. CIRCLE ONE)**

| | | |
|---|---|---|
| | Very satisfied | 4 |
| | Somewhat satisfied | 3 |
| | Not very satisfied | 2 |
| *or* | Not at all satisfied | 1 |

3m. How would you rate your satisfaction with **(READ COMPANY FROM Q3a)** for the following? Would you say you are very satisfied, somewhat satisfied, not very satisfied or not at all satisfied with them for…**(READ EACH FACTOR IN TURN. CIRCLE ONE NUMBER FOR EACH. ROTATE ORDER OF STATEMENTS, STARTING WITH "X")**…?

| | **Very** | **Some-what** | **Not very** | **Not at all** |
|---|---|---|---|---|
| Having the lowest rates | 4 | 3 | 2 | 1 |
| Explaining the cost clearly | 4 | 3 | 2 | 1 |
| Friendliness of the staff | 4 | 3 | 2 | 1 |
| Ease of paperwork | 4 | 3 | 2 | 1 |
| Offering convenient location | 4 | 3 | 2 | 1 |
| Offering convenient hours | 4 | 3 | 2 | 1 |

3n. How likely are you to use cheque cashing in the future? Would you say you are…**(READ LIST. CIRCLE ONE)**…to do so?

| | | |
|---|---|---|
| | Very likely | 4 |
| | Somewhat likely | 3 |
| | Not very likely | 2 |
| *or* | Not at all likely | 1 |

3o. If you were unable to get the cash you needed at a cheque cashing outlet, because none existed in your area, what other source would you turn to for the cash you need? **(DO NOT READ LIST. CIRCLE ALL THAT APPLY)**

| | |
|---|---|
| A payday loan | 1 |
| A pawnshop | 2 |
| A credit card advance | 4 |
| A finance company loan | 5 |
| Family or friends | 6 |
| Loansharks | 7 |
| A bank or trust company | 8 |
| Would do without the money | 9 |
| OTHER (SPECIFY) | ____________________ |

NOW SKIP TO Q. 6

CREDIT CARD CASH ADVANCE

IF NO "PAYDAY LENDING" (CODE 1 AT QA) OR "PAWNSHOP" (CODE 2 AT QA) OR "CHEQUE CASHING" (CODE 3 AT QA) CIRCLED, BUT "CREDIT CARD CASH ADVANCE" (CODE 4 AT QA) IS CIRCLED, ASK Q 4. ALL OTHERS SKIP TO Q5.

4a. The last time you obtained a credit card cash advance, which company did you use? (DO NOT READ LIST. CIRCLE OR WRITE IN VERBATIM)

| | |
|---|---|
| MasterCard | 7 |
| Visa | 8 |
| American Express | 9 |
| Gas card | 10 |
| Store or retail card | 11 |
| OTHER (SPECIFY) ________________ | |

4b. How often have you used credit card cash advances in the past three years?

________________
WRITE IN # OF TIMES

| | | |
|---|---|---|
| Once only | 1 | → SKIP TO Q4d. |

4c. How often have you gotten a credit card cash advance to pay off your credit card bill? Would you say you do this…(READ LIST. CIRCLE ONE ONLY)…?

| | | |
|---|---|---|
| | Frequently | 3 |
| | Sometimes | 2 |
| | Rarely | 1 |
| *or* | Never | 0 |

4d. Have you ever had difficulty paying off a credit card bill on time?

| | | |
|---|---|---|
| Yes | 1 | |
| No | 2 | → SKIP TO Q4f |

4e. Have any of the following occurred as a result of having difficulty paying off your credit card bill? (READ LIST. ROTATE ORDER STARTING AT THE "X". CIRCLE ALL THAT APPLY)

| | |
|---|---|
| Harassing telephone calls to my home | 1 |
| Harassing telephone calls to my work | 2 |

| | |
|---|---|
| Credit privileges were withdrawn | 6 |
| Credit rating was downgraded | 7 |
| Paycheque was garnisheed | 8 |
| NONE OF THESE | 0 |

For the next couple of questions, please think only about the last time you used a credit card cash advance

4f. NO Q4F.

4g. Which of the following reasons best describes the purpose for which you got this credit card cash advance? **(READ LIST. ROTATE ORDER STARTING AT THE "X". CIRCLE ALL THAT APPLY). PROBE:** What other reasons? Any other reasons?

| | |
|---|---|
| To cover day-to-day expenses | 1 |
| To pay the rent | 2 |
| To pay utilities | 3 |
| To pay other bills, loans or debts | 4 |
| For an emergency like illness or car repair | 5 |
| For recreation | 6 |
| For a major purchase | 7 |
| To avoid bouncing a cheque | 8 |
| OTHER (SPECIFY) | ______________________ |

4h. How important was each of the following factors in your decision to get a credit card cash advance? Would you say it was very important, somewhat important, not very important or not at all important that…**(READ EACH FACTOR IN TURN. ROTATE ORDER STARTING AT THE "X". CIRCLE ONE NUMBER FOR EACH)**

| | **Very** | **Some-what** | **Not very** | **Not at all** |
|---|---|---|---|---|
| I compared prices, it has best rates | 4 | 3 | 2 | 1 |
| It was the only place that would give me cash | 4 | 3 | 2 | 1 |
| Service is confidential | 4 | 3 | 2 | 1 |

4j. What was the amount of this credit card cash advance?

______________________________
**WRITE IN $ AMOUNT**

4 k. As far as you know, how much did this credit card advance cost you in fees and interest? **(WRITE IN <u>EITHER</u> DOLLAR AMOUNT OR PERCENT, DEPENDING ON RESPONDENT'S ANSWER)**

______________________ ______________________

WRITE IN $ AMOUNT *OR* WRITE IN %

| | |
|---|---|
| DON'T KNOW | 1 |

4l. How satisfied are you overall with the service you received from this credit card company? Were you…**(READ LIST. CIRCLE ONE)**

| | | |
|---|---|---|
| | Very satisfied | 4 |
| | Somewhat satisfied | 3 |
| | Not very satisfied | 2 |
| *or* | Not at all satisfied | 1 |

4m. How would you rate your satisfaction with **(READ CARD ISSUER FROM Q4a)** for the following? Would you say you are very satisfied, somewhat satisfied, not very satisfied or not at all satisfied with them for…**(READ EACH FACTOR IN TURN. CIRCLE ONE NUMBER FOR EACH. ROTATE ORDER OF STATEMENTS, STARTING WITH "X")**…?

| | **Very** | **Some-what** | **Not very** | **Not at all** |
|---|---|---|---|---|
| Having the lowest rates | 4 | 3 | 2 | 1 |
| Explaining the cost of advances clearly | 4 | 3 | 2 | 1 |
| Offering an appropriate credit limit | 4 | 3 | 2 | 1 |
| Ease of paperwork | 4 | 3 | 2 | 1 |

4n. How likely are you to credit card cash advances in the future? Would you say you are…**(READ LIST. CIRCLE ONE)**…to do so?

| | | |
|---|---|---|
| | Very likely | 4 |
| | Somewhat likely | 3 |
| | Not very likely | 2 |
| *or* | Not at all likely | 1 |

4o. If you were unable to get the cash you needed from a credit card advance because you did not have a credit card, what other source would you turn to for the cash you need? **(DO NOT READ LIST. CIRCLE ALL THAT APPLY)**

| | |
|---|---|
| A payday loan | 1 |
| A pawnshop | 2 |
| A cheque cashing outlet | 3 |
| A finance company loan | 5 |

| | |
|---|---|
| Family or friends | 6 |
| Loansharks | 7 |
| A bank or trust company | 8 |
| Would do without the money | 9 |
| OTHER (SPECIFY) | ____________ |

**NOW SKIP TO Q. 6**

**DEBT CONSOLIDATION LOAN**

**IF NO "PAYDAY LENDING" (CODE 1 AT QA) OR "PAWNSHOP" (CODE 2 AT QA) OR "CHEQUE CASHING" (CODE 3 AT QA) OR "CREDIT CARD ADVANCE" (CODE 4 AT QA) CIRCLED, BUT "DEBT CONSOLIDATION" (CODE 5 AT QA) IS CIRCLED, ASK Q5.**

5a. The last time you obtained a debt consolidation loan from a finance company, which company did you use? **(DO NOT READ LIST. CIRCLE OR WRITE IN VERBATIM)**

| | |
|---|---|
| Household Finance or HFC | 12 |
| Avco Financial | 13 |
| Beneficial Finance | 14 |
| OTHER (SPECIFY) ____________________ | |

5b. How often have you used gotten a debt consolidation loan in the past three years?

____________________

**WRITE IN # OF TIMES**

| | |
|---|---|
| Once only | 1 → **SKIP TO Q5d.** |

5c. How often have you gotten a debt consolidation loan to pay off a previous debt consolidation loan? Would you say you do this…**(READ LIST. CIRCLE ONE ONLY)**…?

| | | |
|---|---|---|
| | Frequently | 3 |
| | Sometimes | 2 |
| | Rarely | 1 |
| *or* | Never | 0 |

5d. Have you ever had difficulty making payments on a debt consolidation loan on time?

| | |
|---|---|
| Yes | 1 |
| No | 2 → **SKIP TO Q5f** |

5e. Have any of the following occurred as a result of having difficulty making payments on a debt consolidation loan? **(READ LIST. ROTATE ORDER STARTING AT THE "X". CIRCLE ALL THAT APPLY)**

| | | |
|---|---|---|
| Harassing telephone calls to my home | 1 | |
| Harassing telephone calls to my work | 2 | |
| Credit privileges were withdrawn | | 6 |
| Credit rating was downgraded | | 7 |
| Paycheque was garnisheed | | 8 |
| NONE OF THESE | | 0 |

For the next couple of questions, please think only about the last time you used a debt consolidation loan

5f. Where did you hear or learn about **(READ COMPANY FROM Q5a. DO NOT READ LIST. CIRCLE ALL THAT APPLY OR WRITE IN VERBATIM)**?

| | |
|---|---|
| TV/radio advertising | 1 |
| Posters/billboards/transit ads | 2 |
| Newspaper/magazine advertising | 3 |
| Advertising (unspecified) | 4 |
| Friends/relatives | 5 |
| Word of mouth | 6 |
| Saw outlet/sign on the street | 7 |
| OTHER (SPECIFY) | ____________________ |

5g. **NO Q5G.**

5h. How important was each of the following factors in your decision to go to **(READ COMPANY FROM Q5a)** for a debt consolidation loan? Would you say it was very important, somewhat important, not very important or not at all important that…**(READ EACH FACTOR IN TURN. ROTATE ORDER STARTING AT THE "X". CIRCLE ONE NUMBER FOR EACH)**

| | **Very** | **Some-what** | **Not very** | **Not at all** |
|---|---|---|---|---|
| Close to where I live or work | 4 | 3 | 2 | 1 |
| I compared prices, it has best rates | 4 | 3 | 2 | 1 |
| Staff is friendly and helpful | 4 | 3 | 2 | 1 |
| It was the only place that would give me cash | 4 | 3 | 2 | 1 |
| Service is confidential | 4 | 3 | 2 | 1 |
| Atmosphere is friendly and welcoming | 4 | 3 | 2 | 1 |

5j. What was the amount of this debt consolidation loan?

_____________________________
**WRITE IN $ AMOUNT**

5 k. As far as you know, how much did this debt consolidation loan cost you in fees and interest? **(WRITE IN <u>EITHER</u> DOLLAR AMOUNT OR PERCENT, DEPENDING ON RESPONDENT'S ANSWER)**

______________________      ______________________
**WRITE IN $ AMOUNT** ***<u>OR</u>*** **WRITE IN %**

| | |
|---|---|
| DON'T KNOW | 1 |

5l. How satisfied are you overall with the service you received from this finance company? Were you…**(READ LIST. CIRCLE ONE)**

| | | |
|---|---|---|
| | Very satisfied | 4 |
| | Somewhat satisfied | 3 |
| | Not very satisfied | 2 |
| *<u>or</u>* | Not at all satisfied | 1 |

5m. How would you rate your satisfaction with **(READ COMPANY FROM Q5a)** for the following? Would you say you are very satisfied, somewhat satisfied, not very satisfied or not at all satisfied with them for…**(READ EACH FACTOR IN TURN. CIRCLE ONE NUMBER FOR EACH. ROTATE ORDER OF STATEMENTS, STARTING WITH "X")**…?

| | Very | Some-what | Not very | Not at all |
|---|---|---|---|---|
| Having the lowest rates | 4 | 3 | 2 | 1 |
| Explaining the cost of loans clearly | 4 | 3 | 2 | 1 |
| Friendliness of the staff | 4 | 3 | 2 | 1 |
| Ease of paperwork | 4 | 3 | 2 | 1 |
| Offering convenient location | 4 | 3 | 2 | 1 |
| Offering convenient hours | 4 | 3 | 2 | 1 |

5n. How likely are you to use a finance company for a debt consolidation loan in the future? Would you say you are…**(READ LIST. CIRCLE ONE)**…to do so?

| | | |
|---|---|---|
| | Very likely | 4 |
| | Somewhat likely | 3 |
| | Not very likely | 2 |
| *<u>or</u>* | Not at all likely | 1 |

5o. If you were unable to get the cash you needed from a finance company, because none existed in your area, what other source would you turn to for the cash you need? **(DO NOT READ LIST. CIRCLE ALL THAT APPLY)**

| | |
|---|---|
| A payday loan | 1 |
| A pawnshop | 2 |
| A cheque cashing outlet | 3 |
| A credit card advance | 4 |
| Family or friends | 6 |
| Loansharks | 7 |
| A bank or trust company | 8 |
| Would do without the money | 9 |
| OTHER (SPECIFY) | ____________________ |

**OTHER DATA (ASK ALL)**

6a. How would you describe the debt you are carrying, from all sources, compared to your normal debt? Would you say your current debt load is…**(READ LIST. CIRCLE ONE ONLY)**…?

| | | |
|---|---|---|
| | Much higher than normal | 5 |
| | Higher than normal | 4 |
| | About normal | 3 |
| | Lower than normal | 2 |
| <u>*or*</u> | Much lower than normal | 1 |

6b. How knowledgeable are you about financial matters and managing debt? Would you say you are…**(READ LIST. CIRCLE ONE ONLY)**…about finances and managing debt?

| | | |
|---|---|---|
| | Very knowledgeable | 4 |
| | Somewhat knowledgeable | 3 |
| | Not very knowledgeable | 2 |
| <u>*or*</u> | Not at all knowledgeable | 1 |

6c. How good would you say your credit rating is right now? Would you say it is…**(READ LIST. CIRCLE ONE ONLY)**…?

| | | |
|---|---|---|
| | Very good | 1 |
| | Good | 2 |
| | Fair | 3 |
| | Poor | 4 |
| <u>*or*</u> | Very poor, or R-9 | 5 |

6d. About how much cash do you have left over at the end of an average pay period? Would you say you have…**(READ LIST. CIRCLE ONE ONLY)**…?

| | |
|---|---|
| More than enough for my needs | 5 |
| A little more than enough for my needs | 4 |
| Just barely enough for my needs | 3 |
| Not quite enough for my needs | 2 |
| Not nearly enough for my needs | 1 |

6e. Please tell me about any other sources of financing or credit you use. Do you currently have any of the following? **(READ LIST. ROTATE ORDERSTARTING AT THE "X". CIRCLE ALL THAT APPLY)**

| | |
|---|---|
| A bank account | 1 |
| A personal loan | 2 |
| A mortgage | 3 |
| A car loan | 4 |
| A car lease | 5 |
| A credit card | 6 |

6f. In general, how satisfied are you with the service you get from banks and trust companies? Would you say you are…**(READ LIST. CIRCLE ONE ONLY)**…?

| | | |
|---|---|---|
| | Very satisfied | 4 |
| | Somewhat satisfied | 3 |
| | Not very satisfied | 2 |
| *or* | Not at all satisfied | 1 |

**DEMOGRAPHICS**

**(READ)** The following questions will be used for classification only, that is, to group people with similar characteristics.

7 **RECORD GENDER.**

| | |
|---|---|
| Male | 1 |
| Female | 2 |

8a. How many people in total live in your household? **(CIRCLE ONE ONLY)**

| | |
|---|---|
| One only | 1 → **SKIP TO Q.9** |

| | |
|---|---|
| Two | 2 |
| Three | 3 |
| Four | 4 |
| Five or more | 5 |

8b. How many are children under 18 years of age? **(CIRCLE ONE ONLY)**

| | | |
|---|---|---|
| NONE | 0 | → **SKIP TO Q. 9** |
| One | 1 | |
| Two | 2 | |
| Three or more | 3 | |

8b. How many are children under 15 years of age? **(CIRCLE ONE ONLY)**

| | |
|---|---|
| NONE | 0 |
| One | 1 |
| Two | 2 |
| Three or more | 3 |

9a. How many vehicles are there in your household? **(CIRCLE ONE ONLY)**

| | |
|---|---|
| One only | 1 |
| Two | 2 |
| Three | 3 |
| Four or more | 4 |
| NONE | X |

9b. Does the head of this household own or rent this home?

| | |
|---|---|
| Own | 1 |
| Rent | 2 |
| OTHER (SPECIFY) ____________ | |

10a Are you working or not working?

| | | |
|---|---|---|
| Working | 1 | |
| Not working | 2 | → **SKIP TO Q 10c** |

10b What is your occupation, that is, what kind of work do you do?

______________________________________________ **NOW SKIP TO Q. 11**

10c Are you … **(READ LIST. CIRCLE ONE ONLY)**…?

| | | |
|---|---|---|
| | Retired | 1 |
| | A student | 2 |
| | A full-time homemaker | 3 |
| *or* | not currently employed | 4 |

11. What is the highest level of education you have completed? **(DO NOT READ LIST. CIRCLE ONE ONLY)**

| | |
|---|---|
| Some/completed primary school | 1 |
| Some/completed secondary school | 2 |
| Some/completed community college | 3 |
| Some/completed university | 4 |
| Some/completed postgraduate degree | 5 |

12. Which of the following best describes your marital status? **(READ LIST. CIRCLE ONE ONLY)**

| | |
|---|---|
| Married or living common-law | 1 |
| Separated or divorced | 2 |
| Single, never married | 3 |
| Widowed/widower | 4 |

13. Please tell me if you are…**(READ LIST. CIRCLE ONE ONLY.)**.

| | |
|---|---|
| 15 to 20 years | 1 |
| 20 to 24 years | 2 |
| 25 to 29 years | 3 |
| 30 to 34 years | 4 |
| 35 to 44 years | 5 |
| 45 to 54 years | 6 |
| 55 years or more | 7 |

14. And finally, which of the following categories best describes the annual household income before taxes? **(READ LIST. CIRCLE ONE ONLY)**

| | |
|---|---|
| Under $20,000 | 1 |

| | |
|---|---|
| $20,000 to $39,000 | 2 |
| $40,000 to $59,000 | 3 |
| $60,000 to $79,000 | 4 |
| $80,000 to $99,000 | 5 |
| $100,000 or more | 6 |

Thank you very much for your cooperation.

# Appendix B: Margins of Error on Household Survey

Overall incidence of usage data, based on the random sample of 4206 contacts, are accurate to within less than 1%, either way, nineteen out of twenty times. This means that, if all Canadians were polled, their answers would be within plus 1% or minus 1% of the answers shown here, nineteen out of twenty times asking the identical question.

Data presented on the sample of 202 in-depth interviews are accurate to within at least 7%, either way, 19 times out of 20.

Margins of error at various sample sizes and observed percentages are shown below:

| Sample Size | Observed Percent | Margins of Error |
|---|---|---|
| 4000 (Total contacts) | 50% | ±1.6% |
| | 5% or 95% | ±0.7% |
| | 3% or 97% | ±0.5% |
| | 2% or 98% | ±0.4% |
| 202 (Total in-depths) | 50% | ±7% |
| | 25% or 75% | ±6% |
| | 10% or 90% | ±5% |
| 57 (Total payday loan) | 50% | ±14% |
| | 25% or 75% | ±12% |
| | 10% or 90% | ±9% |

## Appendix C: Focus Group Report

# Alternative Financial Services in Canada: Findings from Focus Groups

*Discussion Paper*

*September 2001*


**Michael Grant**

Grant Insights

31 Fairfield Road
Toronto, Ontario
M4P 1S9

Phone: (416) 481-1694
Fax: (416) 481-8767
www.grantinsights.com ♦ michael@grantinsights.com

## Table of Contents

# Alternative Financial Services in Canada: Findings from Focus Groups

## 1.0 Introduction

The so-called Alternative Financial Services (AFS) sector has experienced considerable growth in North America in the last decade. This sector includes a wide variety of cheque cashing facilities and sub-prime lenders, including payday lending and pawnbrokers. Some commentators also include tax discounting companies, finance companies and rent-to-own companies. Although this broader definition of the industry is considered in this report, the main focus of the report is cheque cashing and payday lending organizations, the most recognizable in Canada being Money Marts.[127]

There is a concern among consumer advocates that cheque cashing and payday lending operations use ethically dubious practices to take advantage of consumers who have no reasonable alternative sources for credit. These practices are thought to violate federal usury legislation and provincial consumer protection statutes. Yet enforcement has been spotty. This is partly because the Crown has been reluctant to pursue these cases, but also because the industry has been successful in riding the fine line between blatant violation of laws and merely ethically questionable business practices.

Most of the literature in this field has been generated out of the United States with particular reference to inter-state differences in regulatory environments. In addition, legal and economic treatises that attempt to establish the issues surrounding the industry are commonplace. By their nature, these reports tend to be somewhat conceptual and deductive in their reasoning. However, in many ways, the industry violates many precepts of logical, well-functioning markets. Moreover, these studies occasionally lack balance; they are either clearly against the industry to begin with or they take an industry perspective that inevitably glosses over ethical rough spots.

This discussion paper endeavors to make a unique contribution to the literature on cheque cashing and payday lending as it applies to Canada. It is based entirely on the views of Canadian users of the AFS sector, as well as an interview with someone who had worked within the industry. Although the report does not claim to be statistically representative of the sector, it has the virtue of being focused on the Canadian experience and of relating directly the experience of those who have actually used the services. These discussions exposed nuances that are difficult to reveal with either theoretical research or household surveys.

[127] From this point forward the AFS will refer primarily to cheque cashing and payday lending organizations. Money Mart is the brand name for the National Money Mart Cheque Cashing Company, which is a wholly owned subsidiary of Pennsylvania-based Dollar Financial Group Inc.

There remains, however, a need for a larger scale household survey to validate the themes discussed in this paper. Therefore this paper will form the basis for a large-scale, statistically valid household survey that will be conducted during the Fall of 2001. This discussion paper is merely one of four contributions into the Public Interest Advocacy Centre's (PIAC's) final report on the AFS. In addition to this paper and the findings of the household survey, an extensive literature review and consultations with concerned organizations will be reflected in the final report that is slated for release in Spring 2002.

## 1.1 Overview of the Paper

The paper begins with a review of the methodology. This is followed by a brief description of the participants in 6 focus groups held across Canada in August 2001.

Before considering the findings of the focus groups, the paper reviews some insights offered by a former employee of a Money Mart on its business practices and customers. This industry view is juxtaposed with the experience of the focus group participants. Special attention is paid to the participants' use of various types of financial services. Then the report considers participants' attitudes toward different types of credit, which plays an important role in their usage of these services and in their attitudes toward government regulation. The report then goes into some detail on usage patterns and how these establish pathways to the AFS. It concludes with participants' views on the role of government regulation and some summary comments.

## 2.0 Methodology

This report is based on a qualitative interview methodology. This involves a number of group interviews (or focus groups) that bring together small (7 to 9) numbers of people to discuss their attitudes to and experience with various sorts of financial services, with particular emphasis on the AFS. Two focus groups were held in each of Toronto, Calgary and Vancouver (a total of 6) during August 2001. These focus groups were augmented by an interview with a former employee of Money Mart.

There are two structural parameters for the focus group: the recruitment screener that determines eligibility for participation and the discussion guide that provides a framework for the focus group conversation. These are provided in Appendices A and B.

Although our interest was primarily in cheque cashing and payday lending, two types of groups were recruited. One group consisted of people who satisfied the *weak* condition of having had used a finance company. The second group consisted of those who satisfied the *strong* condition of having used a cheque cashing or payday lending facility. This type of recruiting was done because the pathways that lead to the cheque cashing and payday lending organizations are of interest. More importantly, it was felt that a social stigma may be attached to cheque cashing and payday lending that may make some participants reluctant to come forward. This was indeed the case as a number of those who were recruited based on the weak condition also had direct experience of cheque cashing and, in a few instances, payday lending.

The discussion guide merely acts as a framework for the focus group. In practice, the discussion can be quite wide ranging and there is considerable interaction between the moderator (the present author) and the participants, and among the participants themselves. Group discussion can be very effective because people are gathered with those who have common experiences and participants can empathize with other participants' financial challenges.

The discussion guide (Appendix B) logically begins with usage and attitudes (U&A) towards various forms of financial services. The discussion at this point is supplemented through the use of a tally sheet that summarizes each participant's experience with different types of financial services. The discussion then delves further into the course of events that led to the use of the AFS, how people use it, how often they use it and their general impressions and experiences with the sector. The discussion then briefly explores other options for financing outside of the AFS and then considers the participants' views on roles for government regulation.

**Exhibit 1**
**Characteristics of the Focus Group Attendees**

**Total Attendees:** 47

## Gender

| | |
|---|---|
| Male | 26 |
| Female | 21 |

## Education

| | |
|---|---|
| Some High School | 2 |
| Completed High School | 16 |
| Some College | 16 |
| Some University | 4 |
| Completed College | 5 |
| Completed University | 4 |

## Annual Income Level

| | |
|---|---|
| <$10k | 1 |
| $10-19k | 4 |
| $20-29k | 11 |
| $30-39k | 17 |
| $40-49k | 6 |
| $50-59k | 6 |
| $70-79k | 1 |
| $80-89k | 1 |

Source: Grant Insights

## 3.0 Focus Group Participants

Exhibit 1 reviews some demographic information on the focus group attendees. Most of the participants had at least a high school education and lower to middle levels of income. There was rough gender balance in the groups.

## 4.0 Prelude to the Focus Group: The Disclosure Interviews

A weakness in the existing literature is that the motivations and practices of the industry are usually the source of speculation and there is rarely an attempt to juxtapose the industry business practices with the behaviours of the consumers.

To address this weakness, a separate interview was conducted with a former manager of Money Mart in Vancouver. This manager had worked in a middle management capacity for two and half years in four stores in the Vancouver area. This main interview was supplemented by a telephone interview with a former teller of Money Mart who had worked in Toronto and Vancouver for 12 months in 2000-01. This secondary interview was used to confirm some of the findings of the main interview and is not reported separately.

Although the main interview cannot be considered the definitive view on Money Mart's business practices, it is considered preferable to no inside view. The interview was designed to focus on the factual operation of the business with limited impressionistic comments on the quality of the business. None the less, it should be noted that the manager was not bitter about his experience with Money Mart. On the contrary, he considered the Money Mart to be a very good, albeit low-paying, employer. He had a number of positive things to say about the company and overall believes that it provides a needed service. Although he left of his own accord to go to another higher paying employer, his overall job satisfaction with Money Mart was not low.

## 4.1 How Money Mart Makes Money

The most interesting thing about the disclosure interview is the light it sheds on the way Money Mart's pricing regime works and how it manages business risk.

Money Mart has two main (very related) lines of business: cheque cashing and payday lending. The cheque cashing business has been under stress in recent years due to the significant expansion in the use of direct deposit. Notwithstanding the apparently high price to cash cheques (2.9 per cent plus an item fee), the business depends on relatively large volumes to be economic. So the reduction in volumes from direct deposit has presented a challenge for Money Mart. Further, the cheque cashing business became constrained in its growth because it was primarily targeting young, lower-to-middle income males for its business.

In order to grow the business, there was a need to move into alternative financial services that would not be reliant on direct deposit and that would appeal to other types of customers, especially "grey collar" women. The best prospect for growth was considered to be payday lending or "payroll advance". This product was developed in the United States as a natural outgrowth of the cheque-cashing business and involves small loans that are secured through a personal cheque. It was introduced into Money Mart about 5 years ago and, in the words of the interviewee, has been "100-fold more successful" than cheque cashing. This is because its volumes are growing significantly (although still not as large as cheque cashing) but its pricing is much more lucrative than payday lending.

### 4.1.1 The Pricing and Revenue Generation Model

The reason that payday lending is so lucrative is because of the way it is priced. Many commentators have tended to focus on the relatively high cost of the loan itself, which can amount up to $25 dollars for a two-week loan of $100. But according to the interviewee, the main revenue streams are not associated with the loan itself but rather the fees related to the personal cheque that is used to secure the loan.

Money Mart has a graduated scale of item fees that reflect the general quality of different kinds of cheques. In this scheme, personal cheques are the most expensive to cash and attract an item fee of $12.99. In addition, a cheque that is irredeemable because of insufficient funds (NSF) attracts a NSF fee of 25 dollars. Money Mart's management system focuses on maximizing these additional fees.

In this regard, there are direct links between the cheque cashing pricing regime and the payday loan product. Theoretically, a customer can avoid fees by redeeming their cheque before the end of the term. Money Mart, however, encourages customers to allow it to simply cash the cheque. Although there is complete disclosure of these fees within the loan document, the customer usually "don't understand a word you're saying". In the loan document that deals with cheque cashing fees there is language suggesting that it is preferable for the customer to "choose the convenience" of allowing Money Mart to simply deposit their cheque when the term matures.

In addition, Money Mart tightly manages the window between when the loan matures and when the cheque can be redeemed. The whole premise of the payday loan is that cash is required before the next payday. Yet the cheque is written and deposited on the person's payday. Either the customer has to find another source of cash to redeem the cheque (unlikely) or he/she has to lie to Money Mart about when he/she is being paid thereby allowing time to redeem the cheque. Money Mart's information systems are set up to identify customers who consistently redeem their cheques before term which calls forth special efforts to determine whether the customer is being paid before the end of the term of the loan. Not surprisingly, the rate of cheque redemption is "very low".

NSF fees are another source of revenue. At 25 dollars these are significant and, once again, Money Mart has specific management systems around ensuring that a certain number of cheques "go NSF". However, the interviewee was unclear as to how Money Mart could manage this directly other than those efforts that were already in place to ensure high item fees. Undoubtedly the practice of discouraging redemption would lead to some NSF fees being charged.

## 4.2 Managing Risk

One might think that Money Mart would want to avoid NSF fees because these would be offset by higher collection costs. Although these costs are incurred, the interviewee suggested that Money Mart is in a good position to manage these costs effectively. To begin, the vast majority of collections are managed at the branch level through simple telephone calling. Teller staff is used to make collections during down periods in business. For the most part, the customers "have nowhere else to go" so are willing to work with Money Mart to clear their name. In the instances where collections do remain a problem, the practice of "scooping" (garnishment) of presented cheques is common.

In general, Money Mart is extremely shrewd in the way it structures its business to minimize risk. On the cheque cashing side, it ensures due diligence around the "three R's": right cheque, right person leading to recourse. This means that if Money Mart has taken sufficient steps to ensure the cheque is legitimate, and the right payee is presenting it, then it has legal recourse to ensure collection from the payor. This management system suggests that the costs to Money Mart of managing the risk of bad cheques may not be as high as the industry claims and that its bad debt is actually low, although how low remains unclear.

### 4.3 Potential Competitors

According to the interviewee, Money Mart "rides the fine line between revenue generation (on one side) and legality and morality (on the other)". Yet he describes the business as being "relatively unsophisticated" but nonetheless "highly profitable". All this begs the question as to why others do not enter the market, thereby bidding down the prices for these services. The interviewee speculated that the main reason is that Money Mart was one of the earliest entrants and has established a dominant position in a market that is still a "grey area" from a regulatory point of view. As such, new entrants may be reluctant to enter the market in a later stage for fear that regulations may greatly reduce the profitability of the business. The ambiguity of the regulatory situation and the existing market structure has created the conditions for a quasi-monopolistic structure that benefits Money Mart, both in terms of the prices it charges for its services and in minimizing costs due to bad debts.

## 5.0 Main Themes of the Focus Group Discussions

### 5.1 Overall Use of Credit

Participants were asked to fill out tally sheets to describe their use of various forms of financing. Chart 1 (overleaf) reviews usage for various forms of finance based on these tally sheets. Not surprising, given the selection criteria for the focus group, there is a high rate of usage of cheque cashing among the participants. Indeed, about 8 people that were recruited based on their use of finance companies had experience with cheque cashing and one of these people had also taken out a payday loan.

Most participants had interactions with mainline financial institutions but were not using them either because they were disqualified through their credit rating or they were dissatisfied with their services, even though these were widely acknowledged to be the cheapest forms for credit. There was a general distrust of banks. This did not seem to apply to credit unions in the same way although experience with these was not as extensive as with banks and other deposit-taking institutions.

Some forms of credit definitely had stigmas attached to them, but once this stigma had been overcome participants merely considered the source to be a normal part of their financial service use. For instance, non-users of cheque cashing and payday lending facilities were much more likely to consider these morally repugnant, ("they're just legalized loan sharks", "they are preying on the poor") than those that had actually used the service. This also applied to sources of cash like pawnshops, which many users considered to be a reasonable service to help them through cash emergencies. This was especially true in Calgary where participants could point to "hundreds" of pawnshops as an indication of the demand for their services. In the words of one: "no problem, if you have to pawn something it can't be that important to you".

## 5.2 Credit Cards: Paving the Way to the AFS

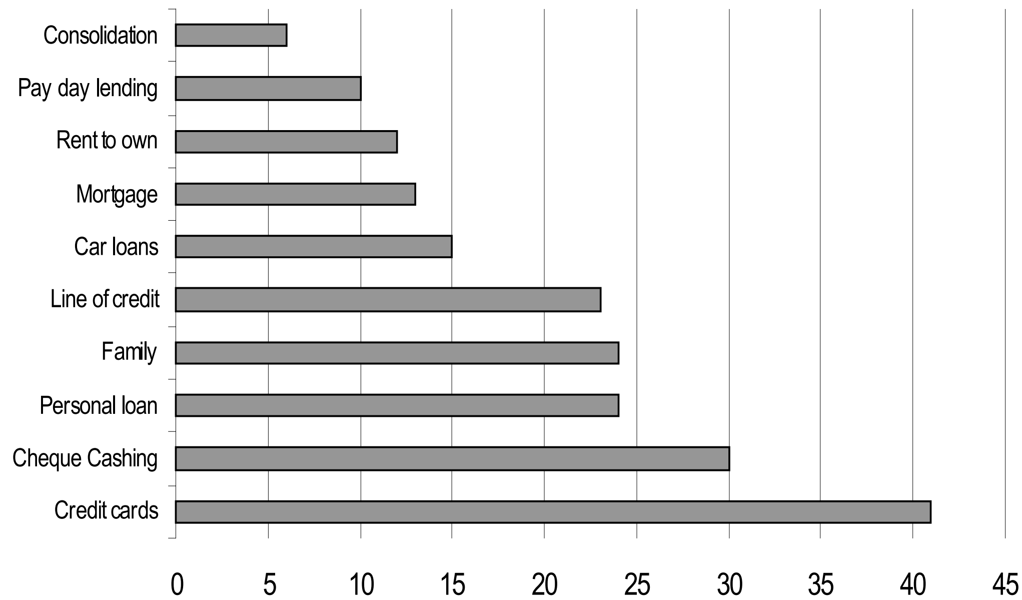
People were most familiar with credit cards and many times this was the product that ultimately led them to the AFS market. Participants were initially attracted to credit cards by their availability, incentive programs (like Air Miles or limited free credit) and the fact that they offer an easy way to establish a credit rating. It was also noted that credit cards are necessary for securing certain types of lending arrangements, like video and equipment rentals.

However, the idea of using a credit card to establish a credit rating was seen as a double-edged sword. Although participants recognized that credit cards are a cheap form of credit for those who exercise discipline in paying the monthly balance, for those who do not have this discipline, credit cards are trouble. "They are only good if you pay them off" was a typical sentiment expressed. So while credit cards are convenient, they are " a bit too convenient" for many people.

Many participants had started their initial cycle of debt through overuse of credit cards and this ultimately undermined their credit rating and limited their access to cheaper forms of credit. For these participants, credit cards were something to be feared with the credit card debt considerations overriding any cost effectiveness considerations (discussed further below).

In addition to aggressively marketing these cards, participants complained that credit card companies initiate increases in card limits without being requested by the cardholder. Not only did this create problems for those lacking the discipline to use the cards effectively, but it also created security concerns should the cards be lost or stolen. In general, these participants were not confident in their ability to take action to get incorrect charges to their credit cards reversed and this creates a source of anxiety when the credit card companies engineer unsolicited increases in credit limits.

**Chart 1**
**Use of Various Financing Options by Focus Group Participants (Number of Participants)**




Source: Grant Insights. Data collected from focus group tally sheets.

## 5.3 Retailer Extended Credit

Of course, retailer credit cards presented many of the same problems as bank credit cards, but there are also some unique issues. For example, retailer finance is often made available at the end of a purchasing decision. As such, some participants were overly focused on the goods at hand as opposed to the cost of financing the goods. For consumers that may lack a disciplined approach to credit, the enticement of the goods may cloud their judgment on financing.

This can be further exacerbated by the fact that the conversation about finance is usually held with a retail sales person whose main expertise lies in the goods being purchased. Usually a third party (a finance company) provides the finance in these transactions. These situations were ripe for miscommunication about financing terms. Several participants found that there were unforeseen charges and that the loan documents tended to be confusing. Indeed, this was more likely to occur with retailer-extended credit than with payday lending.

The same dynamic was at work with rent-to-own. The main consideration of the person was the need for a particular product. The conversation with the rent-to-own sales person is usually about the product itself and the 'easy' financing terms. It is only after the fact that people realized that this easy financing comes at a large cost. "I just fell in love with the sofa and I wanted to have it…I didn't realize how much it cost until months later" was how one Toronto participant described the process.

Yet most participants seemed to be aware that rent-to-own was not the best way to finance ownership and should be considered only for leasing. In Calgary, participants pointed to a recent promotion by IBM for "a computer for a dollar a day" as being an especially egregious example of rent-to-own. Other participants in Calgary and Vancouver compared rent-to-own to "leasing a car", which should only be done for short term needs or in cases where goods become quickly obsolete.

## 5.4 AttitudesToward AFS Services

Participants were asked to compare the costs of the various forms of credit detailed in their tally sheets (Exhibit 1). Participants in all three cities had difficulty distinguishing between the specific cost of various forms of credit. To the extent that differentiation did take place, it was done so in a dichotomous fashion: banks and credit unions are "cheap" (yet unavailable) and everything else is "expensive" (and "easy to get"). As an example, some participants confused the bi-weekly rate of a payday loan with the annual percentage rates (APR's) charged by credit cards and finance companies. These were both seen as being "expensive" but the extent of the expense did not seem to matter.

### 5.4.1 Volume of Credit Major Consideration in Total Cost

Views on the cost of credit were often coloured by attitudes toward other credit parameters, most notably the *volume* of credit, which for many people is of far greater concern than the *per dollar* (or unit) cost of credit. Many people at the focus groups had significant credit card debt that occasionally resulted in personal bankruptcy. To these people, the volume of credit is the source of great anxiety. In a perverse way, many of these people consider the payday lending companies to be less repugnant than the credit card companies. Although the cost of credit is "high", you "don't have this debt hanging over your head and just snowballing". So the real cost of credit is the volume of credit times the per dollar cost. Even if AFS credit is expensive, it is usually highly structured as opposed to open-ended. This constrains the volume of credit and, in the minds of some participants, leads to a lower total dollar cost of credit.

### 5.4.2 Strict Terms of AFS Loans Viewed as a Virtue

Given their views on the importance of the volume of credit, some participants had come to see the strict terms of the AFS as "necessary medicine". Indeed this was considered to be a major benefit of payday loans: they are relatively small loans that add little to the volume of credit. When the volume of credit is a main consideration, the low volume/strict terms of the typical payday loan are actually seen as being a virtue.

### 5.4.3 Bank Holds Drive Cheque Cashing Business

Of importance to the participants was the fact that they could get their money right away from a cheque cashing institution. These are people who have both a very high need for cash and who are most likely to face holds on cheques by mainline financial institutions. These circumstances are tailor-made for the cheque cashing sector that specializes in satisfying the demand for cash while organizing their management systems around managing the risk of bad cheques.

### 5.4.4 Mainstream Movement to Fee-For-Service and AFS Prices

The hold issue combined with the movement of mainstream financial services to fee-for-service pricing makes cost comparisons more problematic. For example, a participant in Calgary noted that his bank would put constraints on his access to a recently deposited pay cheque, limiting this to $200. But the participants required "every dime" of his pay cheque. Although he could withdraw this over time, he would incur fees every time he made a withdrawal. Even though the bank service fees would definitely amount to less than the cheque cashing fees, to him cheque cashing was " about the same as the banks service fees", especially when you consider the extra time involved to get all of the money from his cheque. Similarly, the time cost of cashing a first cheque at Money Mart was seen as being " basically the same as opening a bank account".

### 5.4.5 The AFS as a "Value for Money" Service

In another vein, opinions on the cost of credit were heavily influenced by attitudes toward the level and convenience of service. As with most consumers, the participants recognized that a higher price was merely the cost of greater convenience. One Vancouver participant put it this way: "…when I go into the 7-Eleven I pay 6 bucks for box of cereal. But the place is open when I get out of work, so I pay it. Money Mart is just like that…you are paying for the convenience".

### 5.4.6 Views on Customer Service

Although bank hold periods are the main driver of the cheque cashing side of the business, users of cheque cashing also pointed out that the advantage of Money Mart's opening hours, with at least 1 branch in major municipal areas opened 24 hours. Many people worked in night shift jobs and were in the habit of stopping into Money Mart after work when other cheque cashing options were unavailable. Beyond this, users of Money Mart pointed to the general friendliness of the staff and the welcoming atmosphere compared to banks.

The interview with the former Money Mart manager revealed that a great deal of effort had been made by the company to “spruce-up” the stores and to make them more inviting to females. Those that had used payday lending pointed to the fact that Money Marts were “welcoming” and that “they want to give you the money”. This was contrasted with the banks that were considered to be more judgmental and questioning. Vancouver participants also felt that Money Marts had greater privacy than the banks and were suspicious that banks were using their information systems to target customers for increases in credit card limits. Overall, customer satisfaction among users of Money Mart in all the groups among users was high.

### 5.4.7 Finance Companies as Source of Business Finance

In some instances, finance companies had acted as a key source of capital to finance small businesses that ultimately led participants away from the AFS sector. In Calgary, three participants had successfully used finance companies in this way. So when posed the question of expense, one participant turned the question on its head: “…expensive in relationship to what? I don’t think it costs a lot if I can pay $2000 in interest but then make $3000 with the money I have borrowed”. Although this situation was not commonplace, it does point out that the sub-prime market may serve the function of extending credit to those who would otherwise not qualify for credit and that it rations it such a way to make the borrowers focus on the cost of credit. As another Calgary participant put it: “ I got into debt through credit cards while partying in university…those bastards at the finance company charged me an arm and a leg for that money but if I didn’t have it, I wouldn’t have started my business.”

## 5.5 Pathways to the AFS

All customers of the AFS share the characteristic of having a poor (or no) credit rating that limited their access to mainline credit. Most often this credit rating resulted through credit card use. But within this, there are two customer types: disciplined credit users and ill-disciplined credit users. Disciplined credit users tend to be older, have learned from their bad credit experiences and are much more wary about credit in general. Many have cut up their credit cards and will only use the AFS in genuine emergencies. They are aware that credit cards are best when they are paid off monthly and are more inclined to comparison shop for credit.

Ill-discipline credit users may have a poor credit rating or no credit rating. Some are not the least bit interested in establishing a credit rating and see their use of the AFS as being a manifestation of their desire not to conform. Others are merely coping with debt through a variety of means. They tend to cope by revolving credit between various facilities but do not really have a plan for putting their high credit needs behind them. These people tend to be younger and may be on the path to personal bankruptcy but have yet to experience that trauma.

They recognize that they pay a lot for credit but are much more likely to focus on the volume of credit as opposed to the dollar cost or annual percentage rate (APR) of interest.

Exhibit 2 and 3 outline the characteristics of cheque cashing and pay day lending use of the participants. These users come to cheque cashing and payday lending through two main pathways: straight to the AFS based on its perceived merits or through a poor credit rating.

### 5.5.1 Straight to the AFS

Some participants have come to cheque cashing and payday lending without having significant experience of other forms of retail financial services. These people tend to be younger people who have started using cheque-cashing services. They may have a bank account, but this is either dormant or rarely used. Many may not have established a credit rating or their credit rating is not an issue because they are not looking to borrow significant sums of money. In some cases, they value the "alternative" of the AFS because they see themselves living an alternative lifestyle. For instance, one Toronto participant proudly declared that he was using cheque cashing and payday lending for "recreation".

**Exhibit 2**
**Cheque Cashing Use**

| | |
|---|---|
| Numbers Using Cheque Cashing | 30 |
| Average Amount of Cheque Cashed | $ 450.00 |
| Minimum Amount | $ 50.00 |
| Maximum Amount | $1000.00 |
| **Cost of cashing cheque (n=26)** | |
| Those expressing cost as a percent | 15 |
| Those expressing as a dollar amount | 10 |
| Those expressing as both a per cent and dollar amt. | 1 |
| Average cost for those expressing as a per cent | 3 per cent |
| Average cost for those expressing as a per cent | $ 31.65 |

Source: Grant Insights. Data collected from tally sheets.

Like any financial services company, Money Mart endeavours to establish a loyalty relationship with its customers and, by all accounts, has had some success in doing this. These users tend to value the aforementioned convenience and service aspects of their relationship with Money Mart. Although they acknowledge that the initial steps of establishing this relationship can be very similar to a bank, in terms of filling in forms and the like, they do not really see any difference between this and a bank. They are far less likely to be aware of the cost of credit.

Within this group are people that could be best described as rational or quasi-rational users of cheque cashing and payday lending. These people operate in cash and have a high demand for converting cheques into cash immediately. Although the cost of credit may be high, the bank does not offer them an opportunity to get all their cash without both incurring transaction fees and wasting time. They are inclined to see their relationship with the cheque cashing and payday lending organizations in a positive light. This is because they are not entirely cognizant of the relative cost of the service and in fact see these strict, closed-ended arrangements as preferable to the relatively open-ended credit card arrangements that have resulted in many of their peers' carrying high debt. So within the context of their financial discipline and needs, and the current market structure, they are simply making a rational decision to use cheque cashing because of its features.

**Exhibit 3**
**Payday Lending Use**

| | |
|---|---|
| Numbers Using Payday Lending | 10 |
| Average Amount of Payday Loan (n=3) | $ 335.50 |
| Maximum Payday Loan | $ 700.00 |
| Minimum Payday Loan | $ 120.00 |
| **Cost of Payday Loan** | |
| Those expressing cost as a percent | 3 |
| Those expressing as a dollar amount | 7 |
| Average cost for those expressing as a per cent | 25 per cent |
| Average cost for those expressing as a dollar amt. | $ 85.00 |
| **Number that had rolled over a payday loan** | 2 |

Source: Grant Insights. Data collected from tally sheets.

### 5.5.2 Route R-9

Another major group of people will have had initial exposure to the AFS because of problems with mainstream credit, most likely via credit cards. Some of these people are using the AFS as a temporary measure to get through a difficult time. Others are in a situation of long term coping with no access to other sources of credit. They have incorporated the AFS into their financial coping but do not see anyway out in the foreseeable future.

This group is very aware of the dreaded “R-9” credit rating. They fully understand that the credit rating limits their financing options and leads to them paying more for finance. The “Straight to the AFS” group was more likely to express negative and dismissive sentiments toward the mainline financial institutions whereas this group was more likely to express dissatisfaction with the credit rating system. This manifested itself in two ways. First, they believe that the credit rating system is impenetrable meaning that extenuating circumstances or errors cannot be accounted for or corrected. This leads to the second concern; unsolicited increases in credit card limits expose them to credit card fraud that will affect their rating, which they believe they have very little power to correct.

All this can lead them to using the AFS. Although they may very well develop relationships with AFS institutions, they clearly understand that this costs them dearly and they would prefer to repair their credit rating and deal with mainstream financial institutions. Some of these people have a plan to make this happen but others see no way out and incorporate the AFS into their coping strategies.

### 5.6 AFS Usage Behaviours: “Crisis, What Crisis?”

One area of interest during the focus groups (and the forthcoming household survey) was the usage patterns of the participants. Some participants indicated that they would use payday loans to deal with crises, the main one being the possibility that a utility would be cut off because of non-payment of a bill. No one at the focus groups indicated that they were using payday loans to avoid NSF fees on outstanding cheques.

A more likely scenario was that a person had incorporated payday loans into a cycle of high cost credit that may include credit cards, finance companies and pawnshops. The manager of Money Mart indicated that he saw many of the same customers come in for payday loans during the course of a year and a number of participants indicated that they had drawn on payday loans more than once during the course of a year.

At this juncture, an important distinction should be made between rollovers (or consecutive use) of payday loans and periodic use of payday loans. Some commentators in the United States have expressed concern with payday loans being rolled over, thereby generating astronomical APR’s. A more likely scenario, based on the focus groups, is that payday loans are drawn on occasionally and incorporated into a cycle of payments. Although some participants had used payday loans several times during the year, there was no reporting of consecutive use of payday loans.

A common scenario is that a person may be short money for a minimum payment on a credit card and they may use the payday loan to make this payment and free up space on their credit card for other payments. They may also consider pawning items or use them to secure a small loan at a pawnshop. In fact, focus group participants were more likely to roll over a pawnshop loan than a payday loan because they may be emotionally attached to the collateral in some way. This is not really crisis use per se unless one considers the whole situation a crisis.

Any multiple use of payday loans during the course of the year will undoubtedly result in a very high annual cost of credit, especially given the prevalence of item fees and the possibility of NSF charges. However, this behaviour is somewhat different in kind from rolling over a payday loan. As such, advocates might be wise to consider the total usage during the year as opposed to merely rollover behaviour.

## 5.7 Disclosure and Information Issues

Most of the concern about disclosure and information issues related to retailer-extended credit, rent-to-own and the credit rating system. These issues have already been discussed in previous sections. The main relevant point here is that many people who use the AFS are insufficiently focused on the cost for disclosure rules to have a significant effect on their behaviour. With reference to a payday loan, one participant in Calgary noted "its two or three pages of gobbledygook…you don't read it because you just want to get the money".

In general, participants were not wildly impressed with the idea of improving disclosure. To the extent to which they thought it would make a difference was in terms of ensuring that no "extra fees" were added to leasing, retailer finance or rent-to-own contracts. But participants did not seem to have any issue with disclosure as it applied to cheque cashing and payday lending. They either knew that this was "expensive" or they didn't seem to care because they wanted the money.

## 5.8 Enforcement Issues

Another concern expressed in the US literature is about aggressive enforcement methods to collect debts in the AFS sector. One tactic is to threaten to deposit a cheque that the payday lending company thinks will likely "go NSF". But as seen earlier, there is no need for Money Mart to make any threats in this regard, they just go ahead and do it!

The interview with the former Money Mart manager indicated that there was little reason for Money Mart to become aggressive in their collection practices. To begin, the loan amounts were usually fairly small and not secured by personal property. It was more effective to have a teller telephone the person and work out an arrangement or have a discussion with the person the next time they came in, which more often than not they did. Money Mart's internal information system was effective at identifying repeat customers with outstanding debts. Notwithstanding this, and the fact that no one at the focus group had experienced poor treatment directly, some participants in Calgary indicated that they had overheard clerks being aggressive with customers over the telephone. Aggressive collection was more likely to be reported in relationship to finance companies who "can get quite nasty…. they'll harass you at work" in the words of a Calgary participant.

To the extent that there were threats leveled at the participants, these were more likely to be by utilities for unpaid bills in the form of removal of service. As mentioned, such threats may very well be an impetus to someone using a payday loan.

## 5.9 Alternatives to the AFS

Most people considered the payday lenders as the "end of the line" primarily because of their reputation for doling out very small and expensive loans. The only other alternatives to payday lending were family and friends and loan sharking.

The use of family as a source of money depended very much on a person's relationship with family members. For instance, one Toronto participant indicated that he always went to his mother for financing and this was a long-standing relationship. More commonly, people were concern that using family and friends as a source of money would compromise their relationship and violate their privacy. This was especially true for people who were using payday loans "recreationally" as they realized that they could not go to their family for this purpose. Also, some participants indicated that their family was in similar financial straits, so the idea of going to them to get money to pay the utility bill was a non-starter.

In general, people preferred arms-length relationships in borrowing, even if this cost them much more money. The exception would be young people who would occasionally use a parent to co-sign a loan with a bank or finance company.

No one had direct experience of loan sharking and no one suggested that they would be tempted to use a loan shark in the absence of payday lending. A more likely scenario would be that they would simply have to do without this source of funds, as people undoubtedly did before the introduction of payday loans. Loan sharking was seen as being something that was used by gamblers or drug addicts, people who were, apparently, underrepresented at the focus groups.

## 5.10 Role for Government

Participants were generally skeptical about the ability of government to improve the situation through increased regulation. As mentioned, non-users were more likely to see cheque cashing and payday lending organizations in a negative light but only a few thought that they should be regulated. For example one participant in Calgary, who was especially vociferous in her disgust for the payday lenders, suggested that she did not want to see them outlawed but rather regulated so that they could not lend to young people who were going to use the funds for recreational purposes.

People generally thought that more variety in financing options, even high-priced options, would work in their favour. To the extent that they wanted more government involvement, it was more likely to be in general regulation of the financial services sector as opposed to specifically the AFS sector. In this way the participants felt, for example, that all finance service charges should be regulated and that "hidden charges" should be banned.

## 6.0 Summary Comments

The focus groups revealed a complexity of experience that does not easily lead to straightforward prescriptions for regulating the AFS. On the one hand, cheque cashing and payday lending institutions profit from a group of customers who are in financial straits and others who are lacking in financial literacy. The companies' management systems for maximizing profits from these people are, at best, ethically suspect.

On the other hand, the pre-conditions leading to the use of the AFS very much grow out of other parts of the financial services sector (especially credit cards) and our consumer culture. Moreover, there are genuine needs that these customers have, in terms of convenience and customer service, that are addressed by companies such as Money Mart and that are not addressed by mainline financial institutions. Notwithstanding the moral repugnance of the industry to some, the customers themselves are actually quite satisfied with the services and do not want to see them outlawed.

These themes need to be explored in greater detail through a larger sample of customers to verify some of the findings reported here. Moreover, a larger sample will allow for more statistically representative findings for quantitative data such as usage volumes and costs. Addressing these information needs will be a key role of the large-scale household survey that is planned for the fall 2001.

## Appendix A: Recruiting Screener for Focus Groups

Grant Insights

**31 Fairfield Road**
**Toronto, Ontario**
**M4P 1S9**

Recruiting Screener
June 22, 2001

**RESPONDENT** ____________________________________________

**TELEPHONE #** __________________ **DATE:** ___________________

**POSTAL CODE** ___________________________________________

**INTERVIEWER** ___________________________________________

**SUPERVISOR** ____________________________________________

| | | | | | |
|---|---|---|---|---|---|
| **CITY:** | Toronto | 1 | **GROUP:** | 5:30PM | 1 |
| | Calgary | 2 | | 7:30PM | 2 |
| | Vancouver | 3 | | | |

Hello, my name is _______ of _________, a market research firm. We are conducting a research study on non-bank consumer credit and financing, and we are looking for people to take part in a focus group.

1. First of all, do you, or does anyone in your household work for any of the following types of companies? **(READ LIST. IF "YES" TO ANY, THANK AND TERMINATE)**

| | | |
|---|---|---|
| Market research | 1 | TERMINATE |
| Banking | 2 | TERMINATE |
| Finance company | 3 | TERMINATE |
| Cheque cashing company | 4 | TERMINATE |
| Tax rebating company | 5 | TERMINATE |
| The federal government | 6 | TERMINATE |
| Advertising or media | 7 | TERMINATE |
| NONE OF THE ABOVE | 0 → | CONTINUE |

2a. Have you ever taken part in a focus group discussion before?

| | | |
|---|---|---|
| Yes | 1 → | **CONTINUE** |
| No | 2 → | **SKIP TO Q. 3** |

2b. How long has it been since you last took part in a focus group? **(DO NOT READ LIST)**

| | | |
|---|---|---|
| 6 months or less | 1 → | **TERMINATE** |
| More than 6 months ago | 2 → | **CONTINUE** |

3. Would you feel uncomfortable freely expressing your opinions in a group of people?

| | | |
|---|---|---|
| Yes | 1 → | **TERMINATE** |
| No | 2 → | **CONTINUE** |

3. The focus groups we are recruiting will take place at 5:30 PM and 7:30 PM on…**(READ DATE)**…and participants will be paid an honorarium of $50 for attending. Are you available to take part in a focus group discussion on this date?

| | | |
|---|---|---|
| Yes | 1 → | **CONTINUE** |
| No | 2 → | **TERMINATE** |

4. We are recruiting people who have used alternative sources of consumer credit and financing other than banks or trust companies, whether for emergencies, or for short term cash needs. Have you ever borrowed money from or arranged financing through any of the following types of companies? **(READ LIST. CIRCLE ALL THAT APPLY)**

| | | |
|---|---|---|
| A finance company (like Household Finance or Avco Financial Services) | 1 | → **RECRUIT FOR 5:30 GROUP** |
| A cheque cashing outlet (like Money Mart or UniCash) | 2 | **RECRUIT FOR 7:30 GROUP** |
| A payday advance loan company (like Money Mart, Stop 'n' Cash or Financial Stop, where consumers are loaned money against their paycheques) | 3 | |
| A tax discounter (i.e. will advance you money on your tax return in return for a percentage of the total amount you are owed) | 4 | |
| NONE OF THE ABOVE | 0 | → **TERMINATE** |

5. Which of the following categories best describes your age group? **(READ LIST. CIRCLE ONE ONLY)**

| | | |
|---|---|---|
| Under 18 | 1 | → **TERMINATE** |
| 18 to 24 | 2 | |
| 25 to 34 | 3 | **RECRUIT A** |
| 35 to 54 | 4 | **GOOD MIX** |
| 55 or more | 6 | |

6. **RECORD GENDER. DO NOT ASK**

| | | |
|---|---|---|
| Male | 1 | **RECRUIT A** |

| | | |
|---|---|---|
| Female | 2 | **GOOD MIX** |

7a Are you working or not working?

| | | |
|---|---|---|
| Working | 1 | |
| Not working | 2 | → **SKIP TO Q 7c** |

7b What is your occupation, that is, what kind of work do you do?

________________________________________ **NOW SKIP TO Q. 8**

7c Are you … **(READ LIST. CIRCLE ONE ONLY)**…?

| | | |
|---|---|---|
| | Retired | 1 |
| | A student | 2 |
| | A full-time homemaker | 3 |
| *or* | not currently employed | 4 |

8 What is the highest level of education you have completed? **(DO NOT READ LIST. CIRCLE ONE ONLY)**

| | |
|---|---|
| Some/completed primary school | 1 |
| Some/completed secondary school | 2 |
| Some/completed community college | 3 |
| Some/completed university | 4 |
| Some/completed postgraduate degree | 5 |

9. Which of the following best describes your marital status? **(READ LIST. CIRCLE ONE ONLY)**

| | |
|---|---|
| Married or living common-law | 1 |
| Separated or divorced | 2 |
| Single, never married | 3 |
| Widowed/widower | 4 |

10. And finally, which of the following categories best describes your annual household income before taxes? **(READ LIST. CIRCLE ONE ONLY)**

| | |
|---|---|
| Under $10,000 | 1 |
| $10,000 to $19,000 | 2 |
| $20,000 to $29,000 | 3 |
| $30,000 to $39,000 | 4 |
| $40,000 to $49,000 | 5 |
| $50,000 to $79,000 | 6 |
| $80,000 to $99,000 | 7 |
| $100,000 or more | 8 |

**CONFIRM DETAILS AND RECRUIT FOR APPROPRIATE GROUP**

## Appendix B: Focus Group Discussion Guide

Grant Insights

**31 Fairfield Road**
**Toronto, Ontario**
**M4P 1S9**

*I. INTRODUCTION*

- Role of moderator
- No right or wrong answers
- Please do not self-censor
- What is said in the room stays in the room
- Taping for moderator's reference only (report)
- Confidentiality, don't talk to the next group coming in

*II. RESPONDENTS*

- Who has been to a group before, who hasn't (SHOW HANDS)

- Introductions around the table

    - First name
    - Household composition/family/kids
    - What do you do (occupation)

*III. AWARENESS OF FINANCING OPTIONS*

- Third Person *Awareness* of types of financing
    - Credit Card
    - Car loan
    - Mortgage
    - Personal loan
    - Line of credit
    - Loan consolidation
    - Hire purchase/rent to own
    - Car equity loan
    - Payday loan
    - OTHER VOLUNTEERED MENTIONS

- Probe for any not mentioned
- ***For each, discuss…***
  - Advantages/disadvantages
  - Perceptions of cost and specific rates
  - Perceived reasons for using each

## *IV. DESCRIBE YOUR CURRENT FINANCING BEHAVIOUR*

- First Person *Currently used* sources of
  - Credit Card
  - Car loan
  - Mortgage
  - Personal loan
  - Line of credit
  - Loan consolidation
  - Hire purchase/rent to own
  - Car equity loan
  - Payday loan ***(SEPARATE SHEET)***
  - OTHER VOLUNTEERED MENTIONS
- Probe for any not mentioned
- ***HAND OUT TALLY SHEETS TO NOTE MONTHLY PAYMENTS/RATE***
- CREDIT CARDS
  - Is a balance carried?
  - What is/are rates?
  - How do you know? Where do you get information on costs?
  - How much?
  - Payments?
  - Perceptions of credit card rates vs. bank loan rates
  - Perceptions of ease of use of card credit
  - Why card credit vs. other forms of credit?
- CAR LOAN
  - How much
  - How long
  - What is rate?
  - Payments

- MORTGAGE
  - How much
  - Payments
  - How long
  - What is rate
- PERSONAL LOAN
  - From whom?
  - For what?
  - How much
  - Payments
  - How long
  - What is rate
- LINE OF CREDIT
  - Reasons
  - From who
  - Collateral/guarantee
  - How much
  - How much used
  - Payments
  - What is rate*
- LOAN CONSOLIDATION
  - How many loans consolidated?
  - Who with
  - *Was loan/debt consulting used*
  - Reasons
  - New payments vs. old payments
  - What is rate
  - How do you know?  Where do you get information on costs?
- HIRE PURCHASE/RENT TO OWN
  - What/how much
  - Payments
  - How long

    - Reasons vs. purchase
    - What is rate

- ***PAYDAY LOAN***

    - Reasons
    - What did you use it for (emergency or regular payments)
        - Is this considered an alternative to bouncing a cheque and incurring fees for this?
    - With who?
    - How much?
        - Where did you get the information on how much it would cost?
    - Frequency? Is it rolled over? If not rolled over, do you use it regularly?
    - Payments?
    - How long?
    - Have you used more than one lender?

    - What is rate - daily/monthly/annual

- ***ASK RESPONDENTS LOOK AT SHEET AND CONSIDER TOTAL COST***

- How do you feel about the cost of credit..is it high or low?

- Is better financing rate available…..?

    - Banks/trusts
    - Finance companies
    - Credit unions
    - Neighbours/friends(PROBE GENTLY FOR LOANSHARKING)

- For each used…

    - Reasons
    - Advantages/disadvantages

- For each not used…

    - Why not
    - Advantages/disadvantages
    - Credit history with each

***V. CHEQUE CASHING (U&A)***

- Awareness/usage of cheque cashing
    - Frequency
    - Average amounts
- Outlets used/aware of
    - Cash Stop
    - Money Mart
    - Cash 'n' Go
    - OTHER
- Reasons (WRITE ON FLIPCHART - PROBE EACH MENTIONED)
    - Emergencies
    - Convenience
    - Timely
    - No bank account
    - Just moved/transient
- Advantages/disadvantages
- Awareness of rate
    - Daily
    - Monthly

      Annual
- Perceptions of fairness/unfairness (IF NOT MENTIONED)
- Are other sources of emergency/short-term cash available
    - Banks/trusts
    - Finance companies
    - Credit unions
    - Neighbours/friends (PROBE GENTLY FOR LOANSHARKING)
- For each not used…
    - Why not
    - Advantages/disadvantages
    - Credit history with each

## *VI. TAX REBATE DISCOUNTING*

- Awareness/usage of payday loans
    - Frequency
    - Average amounts
- Outlets used/aware of
    - H&R Block
    - BenTax
    - Others
- Reasons (WRITE ON FLIPCHART - PROBE EACH MENTIONED)
    - Convenience
    - Get cash fast
    - Timely
- Advantages/disadvantages
- Awareness of cost/rate
    - Daily
    - Monthly
    - Annual

## VII. ROLE OF GOVERNMENT

- Which financing sources are regulated (WRITE ON FLIPCHART)
    - Banks
    - Trust companies
    - Credit unions
    - Finance companies (like Avco or Household Finance)
    - Car leasing firms
    - Cheque cashing outlets
    - Payday loan companies
    - Car equity loan companies
    - Pawnshops
- Probe for any not mentioned

- For each mentioned…
  - How much are they regulated
  - Are rates regulated
  - Does regulation benefit company or consumer
  - Is regulation fair for the business
  - Is regulation fair for consumer
  - Is more regulation/oversight needed
  - Do they abuse current regulations
- Does the government have any role in regulating the alternative financing industry such as…?
  - Finance companies
  - Cheque cashing outlets
  - Payday loans companies
  - Car loan equity companies
  - Pawnshops
- Do consumers need protection from this industry?
- What type of information should the government insist that companies provide to help you make good decisions?
- Where do you look for information that helps you decide which company and financial services to use?
- Do you feel you have enough information or too much information right now?

### *IX. "BLUE SKY SESSION" (RESPONDENTS WRITE ON COMMENTS SECTION OF SCORE SHEET)*

- In a perfect world, what would the role of the government be in regulating the financing and loans industry and protecting the rights of both consumers and businesses?