STOP THE PAYDAY LOAN DEBT TRAP

www.fairlendingmn.org

Frequently Asked Questions

What is a payday loan?

Payday loans are small-dollar, high-interest loans requiring full payback on the borrower's next payday. They typically carry triple-digit annual interest rates, are due in full on a borrower's next payday, require direct access to a borrower's bank account, and are made with little or no regard for a borrower's ability to repay the loan. Because of these features, borrowers often cannot both repay the payday loan *and* meet their other obligations without having to quickly re-borrow.

Why do people use payday loans? Why repeatedly?

Payday lenders claim that payday loans are for unexpected emergency expenses, but the reality is that nearly 70% of payday borrowers first used payday loans to cover ordinary, expected expenses.[1] As such, a triple-digit interest payday loan is not a solution for meeting ongoing bills. In Minnesota, the typical payday loan borrower takes out ten loans per year. By the end of twenty weeks, an individual will pay $397.90 in charges for a typical $380 payday loan. Payday loans don't solve financial pressures; they make it worse.

Why is the APR so high on a payday loan?

Minnesota law allows a typical $380, two-week payday loan to cost as much as $40, which translates to a 273% APR. In addition to high costs, state law currently provides no protections against the debt trap, or any standards to ensure that borrowers can repay the loan without re-borrowing.

Why cap the number of loans?

Minnesotans for Fair Lending believes that all people deserve access to fair, small-dollar, emergency credit when it is needed. But exploiting financial stress to ensnare a borrower into a long-term debt trap is unacceptable. Limiting the

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[1] Pew Charitable Trusts. *Who Borrows, Where They Borrow, and Why*. 2012.

number of loans to a maximum of four loans a year[2] prevents this debt trap and ensures that payday loans function as they are marketed. Limiting the number of loans prevents the abusive debt cycle while still allowing payday loans to be available.

How does repeat lending work?
Repeat lending is based on a succession of new loans, but it does not generate new resources for the borrower. Rather, each new loan is just another opportunity to charge more fees for the same loan amount. Each loan is issued separately, with the balance due on the borrower's next payday. Borrowers often need the next loan because paying off the previous loan made it harder to pay the month's bills. This is the debt trap. In most cases, after 10 loans, the fees paid by the borrower will exceed the original loan amount.

But I don't want to take credit away from people who need it.
Establishing a limit of four loans per year offers emergency loans without creating the debt trap that makes borrowers worse off. After North Carolina banned payday lending, former borrowers said they were better off without payday loans, and, instead, worked with their creditors, lowered their expenses, used healthier loan options, sought assistance from family and friends, and avoided falling into a worsening debt trap.[3]

What is a typical payday loan APR in Minnesota?
A typical $380, two-week payday loan carries an APR of 273%.[4] This is more than what is permitted under the Payday Lending Law (which was designed to regulate all payday lenders) because three of the largest payday lenders in the state operate under a loophole in our law. We believe the loophole should be closed and the same rules be applied to all payday lenders in the state. The APR on smaller loan amounts are even higher. Loophole lenders charge 600-700% APR on a $100 loan.

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[2] This is modeled after guidelines established by the FDIC for state-chartered banks because being trapped in repetitive triple-digit payday loans is harmful to consumers and the financial institution.
[3] 22 states ban or limit payday lending and the dire predictions of the industry have not materialized.
[4] Payday America is authorized under the loophole to charge a $30 loan fee and a $50 annual fee. Depending on the size of the loan, Payday America charges either a $25 or $30 fee and some portion of the annual fee per loan.