



Canadian Payday  
Loan Association

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Association canadienne  
des prêteurs sur salaire

## **Canadian Payday Loan Association**

**Response to Payday Loan Business Regulation Proposal  
Discussion Paper**

**Dated April 21, 2008**

**Submitted to:**

**Service Alberta**

## **PURPOSE:**

The purpose of this paper is to provide Service Alberta with views of the Canadian Payday Loan Association on questions raised in the Payday Loan Business Regulation Proposal Discussion Paper dated March-April, 2008.

## **CANADIAN PAYDAY LOAN ASSOCIATION**

The Canadian Payday Loan Association was created in January, 2004 by industry leaders with the mandate to:

- a) consult with and encourage government to develop and enact reasonable regulation to protect consumers while allowing for a viable competitive industry, and
- (b) in the absence of regulation by governments, to develop a code of best business practices to be practiced by its membership which would inform and protect the consumer in relation to payday loan products.

The Canadian Payday Loan Association (“CPLA”) has consulted extensively with every province across Canada and has provided input and advice on the development of all legislation and regulations. The CPLA has participated fully in Utility Board Hearings in the Provinces of Manitoba and Nova Scotia and we have provided to the Federal and Provincial Governments the best and most complete information on the payday loan industry including who provides payday loans, how they are provided, who uses them and why.

The information provided includes:

- The 2004 Ernst & Young study on the cost of payday lenders across Canada to provide payday loans;
- Survey by Environics entitled Understanding Consumers of Canada’s Payday Loan Industry which included a survey of a 1,000 Canadians from the general population and 1,000 payday loan users across Canada.
- A study by Deloitte Touche of the cost of private (non-public) companies in the Province of Manitoba to provide payday loans.
- A study of Deloitte Touche of private (non-public) payday lenders in Nova Scotia.
- A report of Dr. Lawrence Gould of the University of Manitoba analyzing the cost to provide payday loans.

- Five separate surveys by Pollara of payday loan borrowers in the Provinces of Nova Scotia and New Brunswick, Manitoba, Ontario, Saskatchewan and British Columbia.
- The CPLA survey of the number and location of all the payday loan operations across Canada.
- The CPLA has created the independent Office of Ethics and Integrity Commission to ensure compliance with the CPLA's Code of Best Business Practices and deal with complaints made by consumers with respect to both members and non-members of the CPLA. Information on the types and numbers of complaints regarding payday loans can be found in reports filed on the website of the Independence, Compliance and Ethics Commission at [www.cplaethicscommission.ca](http://www.cplaethicscommission.ca).

All of the materials referred to above are available from the CPLA to the Province.

## **GENERAL PRINCIPLES OF REGULATION**

We understand that the goals of the government in bringing forward legislation to regulate of the industry to be as follows:

- Reasonable consumer protection
- Allow for a viable industry
- Workable rules for industry and government

Introducing regulations that license lenders, standardize disclosure, set fee caps that allow for a viable competitive industry and prohibit rollovers will have a significant impact on the operations of many lenders in Alberta and goes far to improving consumer protection. We believe the government should tread carefully and introduce reasonable regulations. There are significant dangers and unintended consequences to over regulating the industry, particularly the beginning stages of regulation.

Government will have made significant strides. If however the government feels further regulation is required it can be done so in the future after assessing first steps.

## **Part A – Licensing of Payday Lenders**

### **Question 1: Should the Alberta Government regulate the payday loan industry and, if so, how?**

The CPLA believes the Province of Alberta should regulate the industry with federally approved legislation. This would require each payday loan company operating in Alberta to be licensed. The benefit of licensing is that the government will be aware of each payday lender operating in the Province and will be better able to monitor compliance and ensure consistency from lender to lender across the Province. Furthermore, obtaining the designation of exemption of payday loans from section 347 of the *Criminal Code* allows the provincial government to set maximum rate caps which is not available through either other option. Obtaining the exemption will also ensure regulatory certainty for loan providers operating in the Province. With regulatory certainty, more larger and stable operators will enter the market which will ensure competition with delivery of the lowest cost and best services to the consumer.

To maintain the status quo limits the ability of the government to introduce regulations to protect the consumer. To regulate the industry without federally approved legislation leaves the provincial government in the awkward position of regulating transactions that allegedly contravene the Criminal Code. Furthermore there would be no limit on the amount of fees charged to consumers.

### **Question 2(A): Should the province require payday lenders to post a bond or other security in order to qualify for a license?**

The CPLA does not believe there should be a requirement for payday lenders to post a bond or other form of security. Unlike debt collection agencies and travel agencies who receive money from consumers, payday lenders are in the business of lending their own money to borrowers.

Lenders do not hold any amount of borrower's money. In fact, multiple borrowers hold a large amount of the lender's money.

While it is conceivable that there could be circumstances where a borrower has been overcharged or excess amounts have been taken from bank accounts, the likelihood of this happening or the magnitude of loss should it occur does not justify requirements of a letter of credit or a bond.

If a lender overcharges in breach of the Regulation, the lender could have their license revoked which would have serious economic consequences. Furthermore, the lender will have significant amount of loans advanced to borrowers throughout the province of Alberta. The amount of those loans will far exceed any potential liability and can stand a security to ensure performance of an obligation under the Regulations.

There is a significant precedent with licensing regimes of payday lenders in the Provinces of Saskatchewan and Nova Scotia. The Province of Saskatchewan has the option of

requiring a bond but this is on a per company basis, not on a per outlet basis. Their experience would indicate that there is no need for a bond.

The Regulations will already bring significant change to the industry and protections to consumers. There is no obvious demonstrated need for such a provision. In the future, if the Minister feels this is not sufficient, the bonding requirement can be reviewed. If this is revisited, we would recommend any future regulation provide that a net worth test be established and where the test is not met, only then have a bonding requirement imposed

**Question 2(B): Should the province restrict the fees that payday lenders can charge to a client who defaults on a loan?**

Yes, the CPLA believes there should be a restriction.

We believe there are two areas that the government should be aware of when setting the maximum default charge allowed. Firstly, reimbursement for the administrative time, charges, cost and expense incurred by the lender when the payday loan customer defaults on repayment of the loan; and secondly interest that is charged on the amount outstanding from the date of default until date of payment.

The CPLA Code of Best Business Practices provides that “a Member may not charge a penalty or NSF fee that exceeds an amount set from time to time by the Association”. The Association sets the fee to cover reasonable costs that are incurred by the lender as a result of default including costs charged to the lender by the bank for a return cheque or pre-authorized debit however the Association limits the maximum fee to be not greater than the NSF fees charged by a major bank. The Association currently set the amount at \$40.00 which is the amount charged by the Canadian Imperial Bank of Commerce. Payday lenders incur no less costs than other lenders in collecting arrears and we believe therefore the maximum charge inclusive of NSF fees that may be levied on default exclusive of interest should not be less than \$40.00.

In addition, a lender should be able to charge interest on the amount of the loan at a rate within currently permitted limits until repayment.

**Question 2(C): Should the province ban the practice of “discounting” where the payday lender gives the client less money than what’s stated on the loan agreement and treats the difference as a fee?**

We believe that this can adequately addressed by properly defining “fees” paid in connection with a loan. If the definition includes fees that must be paid to obtain the loan whether paid before or after obtaining the advance and fees are stated as a percentage of the net funds received by the consumer upon completion of the transaction this should be sufficient.

**Question 2(D): Should the province ban “rollover” loans where the payday lender gives the client another loan to pay for the initial loan and charges them a fee?**

Yes. It is a condition of membership of the CPLA that a member not provide rollovers. This should be applicable to all lenders.

In the industry stakeholder meeting held by the provincial government on April 1, 2008 each attendee was asked to provide the government with a description of a “rollover”. The definition of the CPLA is as follows:

*“A rollover includes (a) an extension of a loan for a fee (not including interest and (b) the granting of a new loan where part or all of the proceeds of the loan are used to pay out an existing loan.*

**Question 2(E): Should the province set a maximum amount that a payday loan business can lend to a client as a percentage of the client’s net income.**

The CPLA believes that there should be no restriction on the percentage of the Borrower’s next paycheque that can be loaned or if there is a restriction it should be a high percentage. While lenders often advertise the maximum percentage of the Borrower’s next paycheque that may be loaned, in practice a lender makes a separate credit decision with every borrower that applies for a loan and our members advise us that in a majority of cases a borrower will not qualify for the maximum amount that could be loaned and/or the amount the borrower is seeking to borrow is less than the amount for which the borrower is approved.

Market forces work well in this respect and we do not believe intervention by regulation is necessary. Lenders must be very careful in advancing credit and making correct credit decisions if they want to remain in business. There is strong motivation not to lend to a borrower more than can reasonably expect to repay. On the other hand, if a borrower needs to borrow \$600.00 for a car repair, legislation prohibiting a lender from lending the borrower more than \$400.00 will merely force a borrower to seek the additional funds elsewhere. In drafting regulations it is important for the government to remember that it is the Borrower that makes the decision how much he or she wants to borrow, not the lender.

Lenders, like all financial institutions, are in a business to make a profit, not lose money. Excess lending results in loan losses. A lender’s objective is not to lend more money than a borrower can repay.

The Manitoba Public Utilities Board issued an order that stated that a lender could not charge fees exceeding more than six (6%) percent of the amount of the loan for loans in excess of thirty (30%) percent of net pay. Based on the financial information provided to them by all parties they were aware that no lender could provide loans for six (6%) percent on a financially viable basis and the effect of the order would be to cap the amount of the loans at thirty (30%) percent of net pay. The CPLA fundamentally disagree with this decision and we feel it is bad for consumers.

Based on the average net paycheck of someone being paid bi-weekly, they have by law prohibited a person earning \$40,000.00 from obtaining a loan in excess of \$345.00.

They have done this notwithstanding the fact that there is no evidence that there is any correlation between the rate of default and the size of the loan in relation to income. If a consumer requires funds for an unexpected expense and they are prohibited from getting all of those funds from a payday lender, the need does not go away. They will be forced to seek those funds elsewhere whether it is through a title loan, pawnshop or other source.

The fact of the matter is this industry has grown in response to consumer demand. It is a service the consumer wants and it is the consumer that decides how much he or she needs to borrow (up to a maximum of what the lender is prepared to lend).

**Question 2(F): Should the province require payday lenders to use contracts written with easy-to-understand language.**

The CPLA believes that it is not unreasonable for a regulator to ensure the loan agreements of licensed lenders do not contain deceptive or misleading language.

**Question 2(G): Should the province allow borrowers a “cooling off” period during which they can cancel the loan and return the money without any interest, fees or penalty.**

Yes. The Code of Best Business Practices of the CPLA requires that members have a cooling off period to the end of the next business day to allow a borrower to rescind the loan transaction. We believe this allows the borrower sufficient time to make such a decision.

**Question 2(H): If a payday loan business is found to violate Alberta’s regulations, should the province allow the client to only pay back the amount of the loan with no interest or fees?**

Yes.

**Question 3: Should the Alberta government set a maximum amount that payday lenders can charge a client.**

Yes, we believe that the government should set a maximum amount that payday lenders can charge a consumer. It should be a “maximum” or “ceiling” which will allow providers to offer the product at a price lower than the maximum in a competitive environment which will account for variations in geography and creditworthiness of individuals.

All stakeholders, both industry and consumer advocates, agree that a monopoly is not in the public interest and it is important to have a competitive payday lending market.

To quote Scott Hannah before the Manitoba Public Utilities Board:

*“So we believe that the structure that has been proposed by the Association of \$20-\$23 per hundred, while it is a high cost – no question about that – it would allow competition within the industry, which we*

*believe is important, as opposed to setting the limit at such a low rate that you would have virtually a monopoly in the industry. We believe that it is important to have competition, innovation and allow market forces to prevail which would ensure the consumer would be able to access the lowest cost and the best service provider.*

*We believe that consumers would be better protected than by lowering the fees dramatically and perhaps driving the majority of reasonable business out of business and having that business go underground.”*

*“Government should not be seeking to regulate the industry like a utility. Government should seek to set a ceiling below which a competitive market can function, not the lowest possible charge that still allows a viable payday lending market if that means that it allows a monopoly or oligarchy in which only one or two operators to survive.”*

The reason that it is important to maintain a competitive market is as follows:

**1. Access for all consumers.**

The payday lending market is not homogeneous. Each lender has different risk assessment criteria. As a result, there are borrowers with poor credit history who are unable to obtain a loan when needed from some payday lenders but are able to obtain a loan from other payday lenders who do not have as strict a lending criterion. These companies have higher bad debt costs and therefore charge higher fees.

If the government sets a rate that is the “lowest charge possible” which still allows some payday lenders to operate, the higher cost operators will either change (restrict) their lending criteria or cease operations with the result that access to credit is denied to a portion of consumers (arguably those who need it most). These consumers will be forced to seek credit elsewhere such as obtaining a title loan or pledging goods at a pawn shop.

**2. Geographical Access.**

The CPLA is aware from talking to its members, that there are rural operators in smaller centres that charge higher amounts. Our members advise us that they must charge higher rates to remain viable. The reason is not that the costs to operate are higher in rural centres but rather the volume of transactions is lower.

Again, if the government sets the “lowest charge possible”, payday lenders will continue operate in the major centres but rural operators will be forced to close. This will exclude access by rural residents to credit.

Once regulation comes into effect there will more entrants into the market. At the same time clear disclosure rules will allow consumers to compare “apples to apples” and choose a lender on the basis of price. As consumers gain awareness, there will be aggressive competition among lenders on the basis of price. As an example of this, Advance America has already opened eight outlets in the City of Winnipeg and in

advance of regulation are charging interest only on their loans and offering a cashback bonus in order to capture market share. We have been advised that they have now opened outlets in Alberta. The result of this is that competition will set the lowest possible charge for each appropriate market and operators who were over charging will either reduce their fees or will no longer be able to survive.

## **FEE OPTIONS**

The Consultation Document sets out three potential options for setting maximum rates. The CPLA recommends Option 2: *Set a maximum fee as a percentage or dollar amount of the loan.* The CPLA is not in favour of Option 1: *No Maximum Fees* because without a maximum fee cap the province will be unable to obtain an exemption under s.347. The CPLA is not in favour of Option 3: *Set a maximum fee with a tiered system.*

The maximum cost of credit for payday lending should be a simple percentage of the amount loaned or “x dollars per hundred” for the term of the loan. For example, 23 percent which equates to \$23.00 for a loan of \$100.00 and \$69.00 for a loan of \$300.00. This is the best method for the following reasons:

### **(A) SIMPLICITY:**

A “dollar per one hundred” system is simple and easy for consumers to understand and will facilitate a comparison from lender to lender. Governments, including this province, are moving towards more disclosure, clear understandable disclosure and disclosure on a consistent basis. With the objective of having a simple comparable method, the introduction of tiered rates simply complicates calculations and works against the objective.

### **(B) BORROWERS PAY MORE FOR SMALLER LOANS**

A company will need to earn a certain amount of revenue to remain in operation. If the amount that can be charged for higher loans is reduced, it means the amount charged for smaller loans must be increased. Those with higher incomes are the borrowers that can qualify for higher loans and conversely, those with lower incomes will only qualify for smaller amounts. As a result, with a tiered rate, borrowers with lower incomes, who generally obtain smaller loans, are paying more for credit than those with higher incomes.

### **(C) CONSUMERS WILL HAVE A MORE DIFFICULT TIME QUALIFYING FOR A PORTION OF THE LOAN.**

The net effect of having a different rate of return for different amounts lent means that the lender will have a different lending criteria for those amounts. With higher fees, a lender can have less restrictive lending criteria. With lower fees, a lender will have more restrictive criteria. If, for example a lender can charge 26% of a loan for the first \$300.00 and 20% for the next \$300.00, the lending criteria will be more restrictive for that portion of the loan over \$300.00. Take any example where a borrower required \$600.00 for a car repair. If the borrower qualified for a \$600.00 loan the cost would be \$138.00. However in many cases, based on credit history, a borrower may only qualify for a loan up to

\$300.00. The borrower requires \$600.00 for the repair and therefore is forced to go to two different lenders to obtain two small loans at the highest rate. The cost is \$156.00. If the rate was set at \$23.00 per hundred, the total cost of the loan would be \$138.00. As a result, a tiered rate hurts consumers.

**(D) ADJUSTMENT FOR INFLATION**

Cost of operation of any business increase over time. This is adjusted in part because the size of people's paychecks rise and the size of loans increase. With a tiered rate over time, the lender is unable to cover increases in cost due to inflation. This is what has happened with the Tax Rebate Discounting Act.

It has been argued that it does not cost more to make a large loan compared to a small loan. Of course, on a simplistic basis it is true to say that the fixed cost in terms of processing paper work for a loan does not cost a lender twice as much when it provides a loan of \$200.00 as it would for \$100.00. That is true of every retail business. If you go into a butcher shop and buy a pound of hamburger for \$3.00, the butcher does not charge \$4.00 for two pounds of hamburger because the time of the butcher to serve the customer is the same. There are many more factors that must be taken into consideration, some of which are set out below.

The CPLA recommends the rate cap be set as a percentage of the loan or "x dollars per hundred". We believe this price structure is supported by industry and a majority of consumer advocates across the country. It is supported by consumers as indicated by the Pollara studies (which can be found on the CPLA website [www.cpla-acps.ca](http://www.cpla-acps.ca)).

Scott Hannah of the Credit Counselling Society also stated before the Manitoba Public Utilities Board:

*"We have examined the report prepared by Lawrence Gould on behalf of the Canadian Payday Loan Association and his recommendations to set a flat fee per hundred dollars of payday loans. Having looked at the experience our clients who have come to us with financial difficulties as a result of payday loans, we support that avenue."*

When asked about his views on a layered rate versus a simple "dollar per hundred" rate before the Manitoba Public Utilities Board Professor Chris Robinson stated:

*"MR. ALLAN FORAN: And in these 25 recommendations you've attempted to simplify the fee structure to make it easier to implement and understand so that you now accept that a flat percentage fee for all borrowers is an acceptable fee structure. Is that correct?"*

*DR. CHRIS ROBINSON: Yes. And that has been a change in my thinking, and it was in fact the Board's questions about me that -- took me a while to think -- to recognize the issue, but then as we have all struggled with, even interpreting, through the mystery shopping what certain fees were, I've recognized the importance of -- of that. In terms of letting the costs to the*

*borrower flow where the borrower is creating the costs this is not the ideal structure. On the other hand the issue of simplification is important....And, I should add, I've completely abandoned, however, the really messy fee structure which I originally -- the -- you know, the interest plus fixed fee, plus this and that was solely because of recommendation -- because of the recognition that while I can understand how such things work, I don't think anybody else does out there who is actually borrowing on them. And I don't think they're necessary. I don't think they help anybody."*

Finally, with the simple system contemplated in Option 2, inspection and monitoring is much easier for government.

### **FURTHER COMMENTS**

We note that the Consultation Document makes reference to examples of rates in the United States. We would caution against reliance on these statistics. Not only are there marked differences between the states but there are many differences between Canada and the United States. Operating costs such as wages and employee benefits provided to workers and taxation rates are just a few of the differences that must be considered. The CPLA has done extensive studies of the cost of operation in Canada which we will be happy to provide when the Province address the issue of setting rate caps.

### **CONCLUSION**

Thank you for the opportunity to respond to the Consultation Document. The Consultation Document does not indicate how the Province will set maximum rates for payday loans or what factors it will take into consideration in setting rates. We look forward to working closely with the Province as these matters are defined. Rates and how they set are obviously of tremendous importance to the industry and our customers.