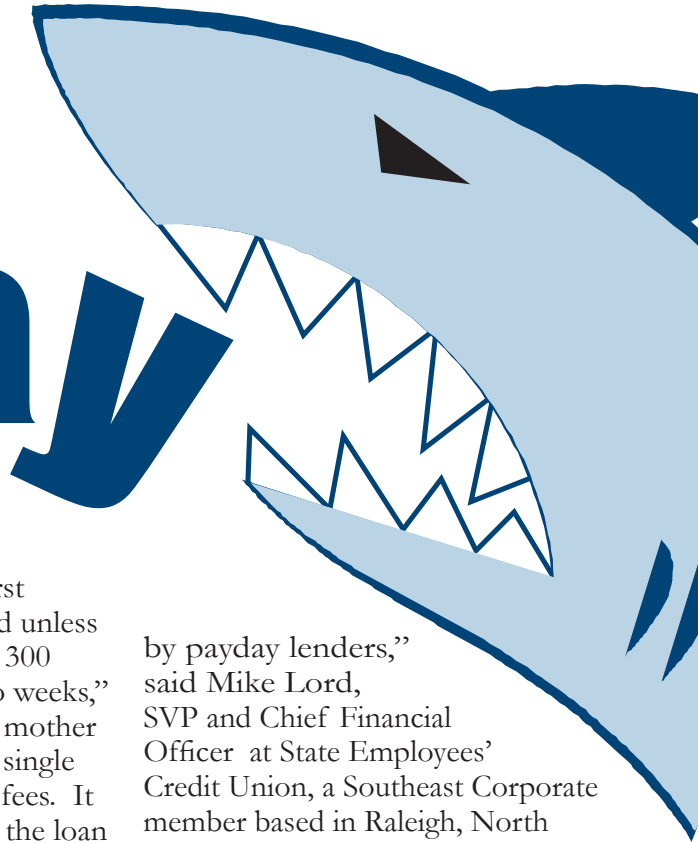


Credit Unions Create Alternatives to Payday Lending



Many credit union members are so cash-strapped that they're hitting up a store in a strip mall for a quick \$200 or \$300 payday loan. These folks will be the first to tell you that they know they're paying way too much to make ends meet.

A small but growing number of credit unions across the country, including members of Southeast Corporate, are developing alternatives to help members avoid falling prey to payday lenders. These credit union pioneers are tackling a tough issue, challenged by the National Credit Union Administration's (NCUA's) 18 percent interest-rate cap.

At one of Southeast Corporate's Annual Meetings, Mark Starr, CEO of Florida Credit Union, raised the issue with then NCUA Chairman Johnson. Starr told Chairman Johnson the NCUA should not interfere with how credit unions run their courtesy pay programs because it is an alternative to payday lenders. Starr's comment caused us to take a hard look at what our members are doing to address this difficult problem. We found some interesting results.

THE PROBLEM

"As soon as you get your first payday loan, you are trapped unless you know you will have the 300 extra dollars in the next two weeks," said Lisa Englekens a single mother who, with 35 rollovers of a single payday loan, paid \$1,254 in fees. It took her two years to repay the loan and get out of the debt trap. While these companies seem convenient and hassle-free, exorbitant fees due on payday force consumers to borrow again to make up for the extra expense. Thus the borrowing cycle continues.

Sandra Harris, a respected member of her community, hit on tough times and turned to payday lending. After several rollovers, Sandra's first loan was due in full. She couldn't pay it off, so she took a loan from a second lender. Frantically trying to manage her bills, Sandra eventually found herself with six simultaneous payday loans. She was paying more than \$600 per month in fees, none of which was applied to her debt. Sandra was evicted from her apartment and her car was repossessed.

"A few years ago we noticed that we frequently had big stacks of checks show up on pay days brought in

by payday lenders," said Mike Lord, SVP and Chief Financial Officer at State Employees' Credit Union, a Southeast Corporate member based in Raleigh, North Carolina. "Check cashers and payday lenders were abusing folks with worse than loan shark interest rates. It was obvious to us that many of our members were caught in a horrendous cycle."

THE INDUSTRY

Payday lending is a relatively new business that has grown explosively over the past decade. Many of the top U.S. banks measured by assets have helped fund the rise of payday lending by extending credit lines. "The big banks are profiting from a predatory financial industry," says Matthew Lee, Executive Director of Inner City Press/Fair Finance Watch, a New York-based organization that lobbies against predatory lending. "By partnering with payday lenders, they have enabled them to sprout like mushrooms all over the country."

At the beginning of the 1990s, there were probably fewer than 200 payday loan offices nationally. By



Audrey Cerise, President and CEO of ASI FCU, was fed up with predatory lenders preying on credit union members.

mid-2001, that number had risen to about 10,000, many of which operate as large, multi-state chains. These businesses have become so successful that some of them are traded on the New York Stock Exchange.

Clearly, payday lending is profitable. According to Advance America, borrowers average at least nine loan transactions per year. The annual percentage rates on payday loans are frequently 400 percent or more. However, the true profitability of the industry depends on receiving high fees many times over for the same outstanding capital. Payday lenders seek to convert occasional users into chronic borrowers.

Arthur Jackson, a warehouse worker, and grandfather of seven, went to the same Advance America payday

shop for more than five years. His total interest paid is estimated at about \$5,000 for a loan of \$300. Advance America flipped the loan for Jackson over a hundred times, collecting interest of up to \$52.50 for each transaction, while extending him no new money.

Jackson is not the typical payday loan customer. Most tend to be younger than the general adult population and women slightly outnumber men. Most are from lower-middle to middle-income households. They have “maxed out” their credit cards and other lines of credit. Others do not have access to lower cost credit because they have severely impaired credit histories. Members of the military are also a prime target.

THE SOLUTION

Southeast Corporate members are

combating the problem on several fronts. Some are offering specialized lending products to help meet member needs and get them out of the payday lending trap. Other members are leading the fight by offering financial education and counseling to their members.

Specialized Lending Programs

One of our members, ASI Federal Credit Union in Harahan, LA, watched payday lending operations run rampant in the state and decided to do something about it.

“Most of our members who got involved with payday lenders fully expected to be able to pay off the lender but in reality were only able to pay on the loan, thus perpetuating their relationship with the payday lender,” said Audrey Cerise ASI President and CEO. “In some instances, they went from one payday lender to another, much like someone who is kiting with a checking account.”

So ASI created a host of alternatives to payday lending including: a Payday Lender ReBuilder Loan, an Asset Builder Loan, a Credit Enhancement Plan and a Stretch Plan.

The Stretch Plan is an open-ended line of credit offered with no credit check required. Loan amounts are between \$200 and \$500, and offered as overdraft protection up to the amount of the loan. Borrowers must maintain direct deposit and their accounts must have been open for at least three months. ASI charges a small per month fee plus an APR of 15 percent. According to ASI’s Community Development Specialist, Shannon Cian, “The Stretch Plan has been a very effective product for our members; they do not need to credit qualify, and with good behavior their line of

Payday Loan Growth Is Explosive

credit can be increased, or they may 'graduate' to other products. Since direct deposit is a requirement, it is virtually "fool proof" (meaning it's very difficult for a member to miss a payment). The Stretch Plan is also a great way for our members to establish or repair their credit, as we report payment histories to all credit reporting agencies. The Credit Enhancement Plan works in a similar manner."

With good behavior, however, ASI likes to graduate Stretch Plan members into the Asset Builder program. With this loan, the "fees" that members would normally be paying are instead placed in a holding account for the members' use once the loan is paid off. "We have had remarkable success stories where members have fallen on hard times or found themselves in crisis and frantically called the CEO, only to be told that they actually have this money in their savings accounts," said Cian.

ASI's newest program, the Payday Lender ReBuilder Loan, was set up under the auspices of a JP Morgan Chase/NFCDCU APPLE grant. Cerise praised the program. "The Payday Lender Rebuilder is our most successful program. It requires members to list all of their debts to payday lenders, and we pay them off in full. We then set up a term loan for the outstanding balance. This gives members an opportunity to get out of the payday cycle and make a smaller payment that fits into their budget." This consolidation loan can be up to \$3000. Borrowers are required to attend financial management classes presented by the credit union, must establish a savings account that is frozen until the loan is paid off and have to sign an agreement promising not to borrow from payday lenders throughout the term of the loan.



State Employees' Credit Union in North Carolina, has more than 53,000 members enrolled in its Salary Advance Program.

Cian says the program has helped the credit union realize how crucial it is to offer alternatives to payday lending. "The stories members have told of the pressures, anxiety, depression, and feelings of being trapped they experienced when stuck in the payday lending debt cycle were shocking and eye-opening," she said.

Credit unions that offer payday advances are discovering that these services can generate enough revenue to pay for themselves. At the same time, they offer significant savings for members and reinforce the message that the credit union is on their side. This message has not gone unnoticed. Among recommendations to consumers on how to avoid payday lending, both the Federal Trade Commission and the Center for Responsible Lending suggest, "try a small loan from a credit union." Neither mentions banks offering any relief.

State Employees' Credit Union (SECU) offers a Salary Advance

Loan that has a built in required savings component. The Salary Advance Loan (SALO) program is designed to help end members' monthly borrowing cycle by providing a low cost alternative to payday lending. The program includes an inexpensive, convenient loan along with a Salary Advance Cash Account to assist in saving for the future. Five percent of each loan advance is required to be placed in the cash account, and access is restricted. According to SECU's Mike Lord, "Many of these members have never had a savings account in their life. We find they feel proud and protective of their savings. The SALO share account is a safety valve for them. We want them to break the cycle."

Lord reports that the program has been very successful for his credit union and that it is profitable. He said, "With a loan rate of 12 percent APR, we are making money on the program." Automation has

helped SECU manage the program efficiently. “A few months ago I was in our call center just after state pay day,” said Lord. “We were flooded with calls for salary advance loans. We have since automated the process which has helped both our members and our staff. Members enrolled in the program can now make themselves a loan advance at any time of the day through our website, or via our automated voice response system. This has made the program more convenient for our members and more efficient for our staff.”

Financial Education & Counseling

Financial education and counseling are strong components of credit union efforts to serve members. Education is part of what is needed for credit unions to protect members who are most at risk of becoming the target of predatory lenders. Over 250 credit unions nationwide, serving over 15 million members, partner with a company called BALANCE, a financial fitness program.

Jax Federal Credit Union in Jacksonville, FL has been offering the BALANCE Program to members for quite awhile. Angie Coleman-Rao, Vice President of Marketing at the credit union said, “We refer a lot of members to Balance. They have helped members improve and build their credit. It’s been a good resource also when working with the needs of our SEGs (select employee groups).”

“We recently signed up for the Balance Program to give us an option for giving our members help,” said Mark Starr, President and CEO of Florida Credit Union in Gainesville, FL. “We had developed a financial counseling program that included classes in the past and experienced very limited success. The BALANCE Program will be

a more cost effective way to offer members help with a broader range of topics at no cost to them.” The education that BALANCE provides helps support salary advance and courtesy pay programs. Credit union members can get help developing a workable spending and savings plan, learn how to get out of debt, and obtain assistance with their credit report, as well as advice on building or repairing credit.

The BALANCE program is offered free of charge to a credit union’s members and provides its services in confidentiality. Credit unions are charged modest fees on a sliding



ASI’s Payday Lender ReBuilder Loan makes payments smaller to fit a member’s budget.

scale to participate in the Balance Program. For more information visit Balance at www.balancepro.org.

Southeast Corporate member, Florida Commerce Credit Union, offers the BALANCE program but has also developed something of its own. Florida Commerce has many SEG groups and works directly with employers offering PROsumer Lunch-N-Learn seminars. Members can choose from topics such as money management, debt management, and ID theft or the credit union will custom-design a

topic for the employer. On top of that, the credit union provides attendees with a free lunch!

OUR TURN

Credit Union executives have been expanding services among lower- and middle-income members and point out that making low-cost micro loans adheres to the credit union philosophy of people helping people. “There is certainly a need to assist members with short-term, low-interest-rate loan products,” said Lord. “Credit unions have always provided such loans. Creating alternatives to abusive payday lending is a challenge we

must meet for the sake of our members. There are many credit unions providing their members with these alternatives and they’re not losing money”

Shannon Cian of ASI sums things up well and states our challenge. “I feel that products such as the ones ASI and other credit unions have set up can be easily replicated by any credit union with a need or desire to do so. I

strongly recommend speaking with representatives from other credit unions that have already established such products and also listening to your specific member base. Due to credit unions having unique fields of membership, it is crucial to figure out what type of product will best suit the needs of your particular members. Now, more than ever, we need to put payday lenders out of business - and credit unions across the country can help provide the resources to do so.”

Education is a Key Component