ACORN Canada
Uniting Communities for Justice

ACORN Policy Position: Fair Banking

Introduction

This document outlines the banking problem that is preventing low and moderate income Canadians from achieving economic justice. A number of policy recommendations are presented which would result in fairer banking and help to combat predatory lending.

What is ACORN Canada?

ACORN Canada, the Association of Community Organizations for Reform Now, was founded in 2004. We are a grassroots organization that has rapidly grown into one of the country's most effective voices for low and moderate income Canadians. With over 102,000 members in 22 neighbourhood chapters across the country, our central purpose is to effectively represent and champion the interests of Canada's low and moderate income citizens on the critical issues of social and economic justice.

Background

Millions of Canadians are unbanked (3%), or underbanked (15%)[1], leaving them financially excluded and forcing them to rely on the services of fringe financial lenders. The obvious disadvantages of being unbanked - without a bank account - are clear. Yet in addition, almost five million Canadians are underbanked - for example, with access to a bank account but no access to basic credit, unable to afford sky-high NSF fees or high interest rates linked to products for low income borrowers, or physically excluded due to branch closures in low income neighbourhoods.

Where the big banks fail to meet the needs of low and moderate income Canadians, there are a wealth of predatory lenders ready to step in and prey on this marginalized group. For example, there are an estimated 1,500 payday loan outlets across Canada[2]. Although these outlets remain outnumbered by bank branches, they are primarily concentrated in low income neighbourhoods, while banks are closing branches at an increasing rate. The number of bank branches in Canada has declined by 22% since 1990[3]. While payday lenders are targeting low income earners, moderate income earners are being preyed on by lenders offering higher value loan products, such as instalment and title loans.

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[1] Fantauzzi, J, *Predatory Lending: A Survey of High Interest Alternative Financial Service Users* (2016) <http://www.acorncanada.org/predatory-lending-report>
[2] Ibid.
[3] Anderson, J, Why Canada Needs Postal Banking (2013) <https://www.acorncanada.org/resource/why-canada-needs-postal-banking>

If you can't afford it, the options for credit are seemingly limitless. In addition to payday loans, low and moderate income borrowers are turning to many other forms of fringe lending in response to the exclusion imposed on them by mainstream financial lenders, such as instalment loans, title loans, rent-to-own outlets, cheque-cashing outlets, tax refund services, and more. It appears there is no shortage of predatory lenders willing to offer credit to low income earners at exorbitant rates.

Consequences

Low and moderate income earners are being pushed into using fringe financial services, as they are becoming further excluded by mainstream financial institutions. Many are getting caught in debt traps, forced to continuously extend their high interest credit, or take more loans, just to pay the previous loan. Marginalizing low and moderate income members by failing to meet their needs and forcing them to use predatory lenders further entrenches poverty in our communities and impacts a number of human rights. People cannot exercise their right an adequate standard of living when they cannot feed their families due to exorbitant interest rates leaving them in a vicious cycle of debt. This is the reality faced by many low and moderate income ACORN members.

Fringe Lending

Some of the most heavily utilized forms of fringe lending include:

Payday Loans
Payday loans are unsecured, short-term loans of up to $1500, paid back from next pay cheque, usually within 2-4 weeks of the initial loan, to a maximum of 62 days. Annual rates can vary from 390% - 650% depending on the province, far beyond the 60% rate allowed under the Criminal Code.

Instalment Loans
A loan which is repaid in equal instalments at regular intervals. Often high interest (over 35% but less than 60%). Usually, installment loans are repaid over long periods and are for significantly higher amounts than payday loans. The lender can attach additional costs such as insurance and fees which increase the interest rate beyond the rate allowed under the Criminal Code.

Rent-to-Own
Weekly or monthly payments are made in exchange for use of an item. If the borrower wants to buy the item, payments continue until it is paid off. The lender owns the item until it is paid in full. Lender often attaches high fees, interest and/or insurance to the loan.

Title Loans
A loan secured against a vehicle as collateral. The borrower pays a fee and gives the lender their car title in return for a loan. Car title loans are usually short term loans and often have high interest rates. If the borrower cannot repay the loan, the lender may repossess their vehicle.

Problem

A survey released by ACORN and the Canadian Centre for Policy Alternatives (CCPA) in late 2016, highlights a clear failing by mainstream financial institutions to provide appropriate products that meet the needs of low income consumers. Only 4.7% of respondents indicated that they prefer to use high interest financial providers over mainstream financial institutions[4]. The reasons that people turn to fringe lenders include: no overdraft protection with their bank, no access to a credit card, or the location of the fringe lender as a reason for using their services. This echoes a 2016 Financial Consumer Agency of Canada (FCAC) study, which found that 74% of respondents said that payday loans were the best available option[5]. Many did not have the option to borrow from a bank or credit union. In addition, the study found that 60% of payday loan borrowers do not have a credit card and 88% do not have access to a line of credit.

Both studies also found that borrowers are turning to these services out of necessity. For example, ACORN's predatory lending survey found that approximately 72% of respondents utilized fringe financial institution only in a time of need, for example, to buy food, pay housing costs or bills, or to alleviate poverty[6]. The FCAC study indicated that 41% of respondents used payday loans for necessary costs such as utility bills[7]. Unsurprisingly, given these figures, Statistics Canada found that low income earners are twice as likely to use payday loans[8]. These figures indicate that people are not surviving on their salaries or social assistance, and rely on fringe lending to fill the gaps. The ACORN/CCPA study found that people in employment were the second largest group accessing high interest products. This is supported by The Conference Board of Canada, who indicate that payday loan users are more likely than average to be in full time employment[9]. Issues here are two-fold:

[4] Fantauzzi, J, *Predatory Lending*
[5] Financial Consumer Agency of Canada, *Payday Loans Market Trends* (2016) <https://www.canada.ca/en/financial-consumer-agency/programs/research/payday-loans-market-trends.html>
[6] Fantauzzi, J, *Predatory Lending*
[7] Financial Consumer Agency of Canada, *Payday Loans Market Trends*
[8] Pyper, W, *Payday Loans* (2007) <http://www.statcan.gc.ca/pub/75-001-x/10407/9617-eng.pdf>
[9] The Canadian Conference Board of Canada, *Filling the Gap. Canada's Payday Lenders (2016)* <http://canadiancfa.com/wp-content/uploads/2016/11/cboc-filling-the-gap_final-nov-2016.pdf>

employed, low-income Canadians are not earning enough to fulfil their basic needs; and mainstream financial institutions are not providing them with necessary products, so the gap is being filled by high-interest lenders who often charge predatory rates. Fringe lenders are forthcoming about the fact that this group of low income earners is their target market. In fact, Dollar Financial Corporation, owner of Canada's largest payday lender Money Mart, even has a name for this target customer. 'ALICE' - asset limited, income constrained, employed[10]. The reality is that mainstream financial institutions are not meeting the needs of low and moderate income earners so fringe lenders, often charging predatory rates, are bridging the gap.
An additional issue adding to the struggles of low and moderate income earners is the fact that the model of many forms of predatory lending relies on consumers getting caught in a cycle of debt, in order for the companies to profit. An Ernst and Young report indicated that the cost of servicing a repeat payday loan borrower is much lower than that of servicing a new customer[11]. Evidently, it is in the interest of these lenders to attract repeat business. Many provinces have laws preventing lenders providing payday loans to borrowers while they have a loan outstanding with the same company. However, there is nothing to prevent a borrower going to another company to take out a payday loan. ACORN has witnessed a high frequency of borrowers taking a loan from Company A to repay Company B, getting caught in a vicious cycle of debt with negative outcomes for health, wellbeing and quality of life.

Fringe lending is only expected to grow. The FCAC has indicated that payday loan use has doubled in recent years[12]. At the same time, the number of people considered 'working poor' in Canada continues to rise, with Living Wage Canada indicating that 70% of those in poverty are in employment[13] - a perfect match for the predatory lenders looking for customers who fit their ALICE descriptors.

Adding insult to injury, the six main banks in Canada - TD, BMO, RBC, Scotia, CIBC and National Bank – generated $35 billion in profits in 2015[14]. Meanwhile, many Canadians struggle with non-sufficient funds (NSF) fees of $45, high interest rates and no access to emergency credit or overdraft protection for low income earners. Banking is expensive for low and moderate income people. It makes economical sense to take a payday loan of $100 and pay up to $25 in interest (depending on the province) to stop a cheque from bouncing,

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[10] Ibid.
[11] Ernst & Young. 2004.The Cost of Providing Payday Loans in Canada. Tax Policy Services Group.
[12] Financial Consumer Agency of Canada, *Payday Loans Market Trends*
[13] Lefroncois, A, Canada's Working Poor and Precarious Employment (2015) <http://www.livingwagecanada.ca/index.php/blog/canadas-working-poor-and-precarious-employment/>
[14] CBC News, Canada's Big Banks Earn $35B in Profits for 2015 (2015) <http://www.cbc.ca/news/business/bank-profits-rise-1.3348661>

when the alternative is a $45 NSF fee. Banks are failing low and moderate income Canadians.

In summary, Canada's banking problem can be defined as follows:

- Low and moderate income earners are unable to meet their basic needs;
- Mainstream financial institutions - while making big profits - do not offer adequate products for, and often exclude, low and moderate income earners;
- Fringe financial lenders target this excluded group, offering high interest products, often at predatory rates;
- Many low and moderate income borrowers get caught in a debt trap: taking a loan which they cannot afford, so they are forced to extend the loan or take out another loan to pay the original loan.

ACORN's Experience

ACORN has developed several reports exploring the detriment caused by predatory lending. In addition, anecdotal evidence of the struggles of low and moderate income earners is gathered from daily conversations that frontline staff have with ACORN's low membership. Some examples of relevant work include:

- Predatory Lending: The Shark Report: http://bit.ly/1K144qY
- Predatory Lending: A Survey of High Interest Alternative Financial Service Users: http://bit.ly/2tpBqzV
- Regulation of Payday Lending in Canada: http://bit.ly/2tloJFV
- Protecting Canadians' Interest: Reining in the Payday Lending Industry: http://bit.ly/2tltE9q
- Survey of Payday Loan Users in Toronto and Vancouver: http://bit.ly/2tYSZDY

ACORN has also been a stakeholder in provincial government consultations on payday lending legislation in Ontario and BC. ACORN's submission to Ontario's Strengthening Consumer Financial Protection consultation is available at: http://bit.ly/2sRYkOR

Solutions

ACORN's low and moderate income members have highlighted a clear gap where the financial needs of low and moderate income people are not being met by mainstream financial institutions. Coupled with stricter regulations on predatory lending, ACORN members also call for the creation of alternative products for low and moderate income borrowers, so they are not forced to rely on fringe lenders who charge exorbitant rates and exploit vulnerable borrowers. From ACORN's predatory lending survey results, the majority of respondents (63%) indicated that they thought it was 'very important' for banks to offer products for lown and moderate income people, such as overdraft protection and small loans [15]. Given that most respondents of the ACORN and FCAC studies admitted only using the services of fringe lenders because their bank or credit unions would not provide credit[16 17], it is apparent that the creation of affordable loan products geared towards low and moderate income earners could result in a reduction in the number of people forced to rely the services of predatory lenders.

Good practice is already happening in Canada. Vancity's Fair and Fast Loans take the circumstances of the borrower into consideration, offering fast access to low cost loans that fill the gap created by mainstream banking, and provide an alternative to payday lending[18]. Vancity also offers extended repayment periods, allowing borrowers to take the time they need to stabilize financially. Another example is Causeway's Community Financial Fund, a pilot partnership between the Causeway Work Centre and three Ottawa credit unions, offering low cost loans to help people escape the debt traps caused by payday loans[19]. Loans have been approved for up to $5000, helping to tackle the issue of instalment loans and other types of alternative lending. However, these services are limited, and as such can only reach a small percentage of the low and moderate income earners who are impacted by predatory lending. Mainstream financial institutions need to support and learn from these initiatives to fill the gap that fringe lenders are occupying.

Examples of steps taken by government to combat predatory lending can be found overseas. In Scotland, municipal government has partnered with credit unions to offer small, fast, low-interest loans to challenge the payday loan market. By securing government funding, credit unions have the opportunity to provide loans on a wider scale. Labelled 'The Wee Glasgow Loan' the product provides a straightforward online application and quick decision timeframe, allowing it to act as a viable alternative to payday loans. The loan product allows borrowers to pay back over longer periods of up to 12 months, giving them time to get back on their feet. Providers also incorporate financial education into the process, helping borrowers to address the root causes of their financial issues. The credit unions involved are in talks about rolling out the program across Scotland, which would likely require funding from the national government.

[15] Fantauzzi, J, *Predatory Lending*
[16] Ibid.
[17] Financial Consumer Agency of Canada, *Payday Loans Market Trends*
[18] Vancity, *Vancity Fair & Fast Loan*
<https://www.vancity.com/Loans/TypesOfLoans/FairAndFastLoan/>
[19] Causeway Work Centre, *Causeway Community Finance Fund Backgrounder*
<http://www.causewayworkcentre.org/wp-content/uploads/2013/09/CCFF-Launch-Backgrounder.pdf>

ACORN members also support postal banking, and believe that it presents opportunities to both fill a gap where banks and credit unions do not have branches, and also to provide products for low income earners that offer a genuine alternative to fringe lenders. Successful examples of postal banking include the Post Office bank in the UK, La Banque Postale in France, and Kiwibank in New Zealand.

Recommendations

Based on extensive research on predatory lending and the detriment it causes low and moderate income earners, ACORN has a number of policy recommendations that, if implemented, would make banking fairer:

- Mandate the banks to provide access to low interest credit for emergencies;

  Providing low interest access to credit would ensure that low and moderate income earners have options if they run into unexpected financial issues, so they are not forced to rely on fringe lenders charging excessive rates and fees.

- Mandate the banks to provide low interest overdraft protection;

  Low interest overdraft protection would allow low and moderate income earners to avoid missing payments or bouncing cheques, with the overdraft temporarily covering payments when there are not enough funds available, to be repaid with interest.

- Mandate the banks to provide no holds on checks;

  By placing holds on cheques, banks push low and moderate income earners to find access to credit elsewhere. Rather than wait for the cheque hold period to end, people who need access to the funds immediately will pay excessive rates and fees to cash the cheque at a cheque cashing outlets, or take a payday loan.

- Mandate the banks to lower NSF fees from $45 to $10;

  The current rate of $45 is excessive and causes many people to rely on predatory loans. It is cheaper to pay interest of up to $25 (depending on the province) on a $100 payday loan than bounce a $100 cheque and pay a $45 NSF fee.

- Create a fund to support alternatives to predatory lenders, such as postal banking and credit union credit products geared toward low and moderate income families;

By encouraging the creation of other products, the gap in financial services for low and moderate income people will be filled, saving many low and moderate income people from relying on predatory lending.

- Create a national anti-predatory lending strategy;

  Tackling predatory lending at a national level will provide the opportunity to address gaps in regulation and will allow the sharing of best practice across the country.

- Create a real time national tracking system (or database) to help stop rollover loans;

  A real-time database which keeps a record of payday, installment and title loans would ensure that borrowers are not taking out multiple loans with different lenders. This would help prevent rollover loans, where customers borrow from one lender to pay an existing lender, preventing customers from spiralling into debt traps.

- Amend the Criminal Code to lower the maximum interest rate from 60% to 30%.

  Lowering the maximum interest rate would make lending more affordable for low and moderate income borrowers, as it would prevent lenders charging excessive interest rates.