ACORN CANADA

SUMMARY

Fair Credit

Enhancing access to low-cost/short-term credit options among low- and moderate-income consumers.

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ACORN Canada is a national community union of low- and moderate-income people.

Executive Summary 2023

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Introduction

ACORN Canada undertook a national study to generate evidence on the availability of and awareness about short-term, low-cost credit options among financial consumers who face specific vulnerabilities in accessing fair credit alternatives. The study also produces more information about the low-cost credit options that people can access when they are facing a financial emergency.

ACORN has conducted several studies in the past which show that lack of financial inclusion is forcing many low- and moderate-income people to borrow money from fringe lenders at exorbitant interest rates. However, there is insufficient evidence with respect to the kind of low-cost credit options available to consumers, if low-to-moderate income and financially vulnerable people are aware of those options and the barriers people face in accessing them.

Overall, the study concludes that there is a very limited number of low cost or fair credit options for low- and moderate-income people, and of those that do exist, the scale of who can access them is very limited. This is based on a review of the literature as well as the results of a survey that ACORN conducted with its members.

The report covers three specific aspects:

- Scan of the nature and extent of the household high-cost debt in Canada.
- Scan of low-to-medium cost credit options in Canada and certain other jurisdictions.
- Findings of the national online survey administered to ACORN members nationally

Methodology

The study comprised a mix of primary and secondary data collection. The initial phase comprised of a scan of existing literature to understand the nature and extent of debt among Canadian households as well as low-to-medium credit options available by banks/other institutions. The second phase included two national focus groups and a national online survey to ACORN members nationally. An online survey was sent to all contacts that exist in the ACORN database nationally between February and March 2023. It was sent in both the official languages - French and English. A total of 623 responses were received.

ACORN has 24 neighbourhood chapters in 10 cities across the country. The provinces where ACORN has established chapters include Alberta, BC, Nova Scotia, New Brunswick and Ontario. Hence, the responses that were received are mostly from these provinces, the highest from Ontario, given ACORN's history of work in the province since 2004.

For the purpose of this research, the following categories were adopted to define the different types of credit (specifically Annual Percentage Rate or APR).

- Low: 0-9%
- Moderate: 10 -20%
- Medium: 21 - 30%
- High: 31-45%
- Extremely high: More than 45%

Findings from the scan of nature and extent of household debt in Canada

- The household debt among Canadians is rising especially with changes in the larger economic scenario, including the continued effects of the pandemic and the current record inflation. For example, FCAC surveys show that many more people are borrowing money, including from high-cost lenders.
- Low- and moderate-income people largely carry unsecured forms of debt which are usually installment loans, payday loans etc. and not mortgage debt.
- Lack of and inadequate access to traditional banking institutions and/or products is forcing many low- and moderate-income consumers to rely on fringe (often called alternative financial services) lenders that charge exorbitant interest rates.

Latest studies indicate that many Canadian households are extremely vulnerable or financially on the edge. While many households are not financially resilient, the percentage is especially high among low-to-moderate income households and certain other populations such as indigenous communities, single parents and those experiencing significant income volatility

Findings from the scan of nature and extent of household debt in Canada

A scan of existing low-cost credit options was conducted. At the national level, the two products include the My Money product that was launched by Canada Post and TD bank and Desjardins Accord D financing which is offered by Desjardins. While the Canada Post product stands discontinued, Desjardins product has a limited reach as it requires the individual to have a chequing account and a credit card from Desjardins. Further, most other locally available products marketed as payday loan alternatives are offered by credit unions which are available in a limited geographical area. Some provinces or cities have rent banks that help lower income tenants who have fallen behind on rent. But as Spotton Visano (2018) argues, the financial alternatives that exist today are a patchwork of solutions and will have limited impact because of being ad hoc.

Findings from the national survey

Many low-to-moderate income consumers are financially on the edge.

- More than half of the respondents cannot cover one month's worth of expenses.
- Around 40% of respondents would fall into debt in case they had to make an unexpected expenditure today of $500.
- 70% of respondents are currently in debt.
- 40% of respondents experienced severe financial hardship because of the pandemic and/or inflation.
- More than half of the respondents had to borrow money in the past 12 months.
- Out of those who said they had to borrow money, the largest proportion of people used their credit card (36%), followed by family member/friend (18%) or the bank (17%). Almost 22% had to go to a payday or an installment lender.
- 30% of respondents needed to borrow money very often or monthly. Only 16% of respondents mentioned that they never needed to borrow money.

Very few medium-low-cost credit options exist.

- When asked what you do first during a tough financial situation, only 7% of respondents go to the bank. Around 31% of them use a credit card closely followed by 29% who approach their family/friend. One in ten respondents said they either go to a payday or an installment lender.
- A vast majority i.e. 87% of respondents said that they were not aware of any medium or low interest credit options (annual interest less than 30%) or other sources of emergency funds for people with a low or moderate income who can't access credit from the major banks (it excludes credit cards and lines of credit from mainstream banks/credit unions).
- The two medium-to-low-cost credit options available nationally that people seem to be somewhat aware of/have used in the past include the Canada Post-TD My Money product (the product has now been discontinued) and Desjardins. The only other local credit product that a few people had used/were aware about included the Vancity Fair and Fast Loan offered by a Credit Union in BC.
- 22% of respondents were able to access rent bank/rent grant/other rent support programs and out of these, 41% of them were able to benefit from them.

Low-to-moderate income consumers are forced to borrow credit from predatory lenders.

- Around 20% of respondents had to take out a high-cost loan such as a payday loan/installment loan or other high-cost loan with annual interest rate over 30% in the last 12 months.
- Almost one-third of respondents had to take out a high-cost loan very often i.e. every month in the last year, another 18% said that they had to take out such a loan often in the past 12 months.
- The top reason for taking out a high-cost loan was to meet everyday living expenses such as rent, groceries etc. Other reasons but far less common ones included car repairs (20%), medical expenses (19%), pet expenses (11%) and to improve credit score (10%).
- A third of the respondents said that their loans got refinanced multiple times while 20% of them mentioned it being refinanced at least once. Refinancing is a common tactic employed by predatory lenders to ensure people are in the debt trap forever.
- Impacts people reported as a result of them making all or most loan payments on time included not being able to buy basic necessities (66%), followed by inability to pay a different bill (48%), reduced amount of savings for retirement (40%), skipping a needed medical appointment (29%) and incurring overdraft fees (26%).
- Consequences reported by the respondents if they could NOT make all or most of the loan payments on time included stress, anxiety and depression (80%), closely followed by getting in to even more debt (72%), adverse effect on the credit score (67%) and having to file a consumer proposal/ bankruptcy (11%).
- Around 60% of respondents were highly unsatisfied with the high-cost loan. Very few people rated their experience as satisfactory or highly satisfactory.

Limited access to traditional banking institutions/products

- Around 40% of respondents said that banks/credit union products were "not helpful at all" in times of financial hardship.
- Around 19% of respondents were members of a credit union. A quarter of the respondents who are a member of a credit union used a low-cost credit option from them.
- With respect to banking products such as line of credit, small loan, credit card, overdraft protection, removing holds on cheques, no fee accounts, and whether they received them, the number of people who received any of these banking products was found to be invariably lower than those who applied for it. The difference was especially pronounced in case of small loans, overdraft protection and credit card - all of which can be extremely helpful in case of a financial crisis.
- Main reasons for not using regular banking/financial services were a previous rejection from the bank (46%), feeling judged when going to the bank (30%), lack of trust in the banks or because banks have withdrawn from the account without their knowledge (24%); and the fact that banks are unfriendly and make respondents nervous (22%).

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Policy recommendations

- Support fair lending alternatives
- Enhance financial inclusion
- Lower the criminal rate of interest of predatory loans

Policy recommendations

Based on the findings of this study, the following are policy measures that the federal government could consider for enhancing the access to fair credit.

1 Support fair lending alternatives:

- The federal government must create a federally funded Fair Credit Benefit so that all low-income people have access to low-cost credit options in case of an emergency.
- The federal government should support postal banking and other low-cost alternatives. Canada Post's infrastructure can be leveraged to ensure that low-income people have access to low-cost loans in case of financial emergencies.

2 Enhance financial inclusion:

One of the key reasons why so many people have to rely on predatory lenders is that they are underbanked. ACORN continues to advocate for fair and affordable banking options from Canada's mainstream banks.

- ACORN repeats its call for the federal government to lower the NSF fee from $48 to $10.
- The federal government should eliminate overdraft fees and the banks should provide overdfraft protection to all customers.

3 Lower the criminal rate of interest of predatory loans.

- As promised in the Federal Budget 2023, the federal government must immediately lower the criminal interest rate of installment loans from 47% APR (60% Effective Annual Rate, EAR) to 35% APR (42% EAR). This interest cap should include all associated fees and costs such as insurance.
- The interest rate should be further lowered to 30% or 20% plus Bank of Canada rate or whichever is lower.
- The federal government needs to enforce the regulations and make contesting violations accessible to borrowers. Currently, it is nearly impossible for any borrower to challenge a predatory lender or take them to court if they are being ripped off.

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