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May 16, 2013

Mr. H. M. Singh
Secretary and Executive Director
Manitoba Public Utilities Board
Room 400, 330 Portage Avenue
Winnipeg, MB R3C 0C4

Dear Mr. Singh:

RE: Payday Lending Review under Section 164 of the Consumer Protection Act

Introduction

On behalf of CAC Manitoba and Winnipeg Harvest, we are pleased to provide the following information for the consideration of the Public Utilities Board:

A Profile of Canadian Payday Loan Customers prepared by Dr. Wayne Simpson and Ms Dana Bazarkulova;

Payday Lending Literature Review prepared by Dr. Jerry Buckland and Ms Elizabeth Buckland;

Regulation of the Payday Lending Industry – Are the Rate Caps Reasonable? prepared by Dr. Chris Robinson;

Report on Mystery Shopping Payday Lending and Payday Lending-Like Outlets in Winnipeg prepared under the supervision of Dr. Jerry Buckland;

Report on Exit Interviews of Payday Lending and Payday Lending-Like Outlets in Winnipeg prepared under the supervision of Dr. Jerry Buckland and with the assistance of Dr. Wayne Simpson;

A mapping perspective of the historical development of the Winnipeg payday lending industry prepared under the supervision of Dr. Jerry Buckland.

The Experts

The information provided by Winnipeg Harvest and CAC Manitoba was prepared under the leadership of a number of experts. Their curriculum vitae are provided in the attachments but brief summaries are provided below.

Dr. Jerry Buckland (CV 7)

Dr. Buckland is an economist with a particular expertise in financial exclusion, fringe financial services and developmental economics. He was qualified as an expert witness on matters relating to financial exclusion and fringe financial services in prior PUB proceedings relating to government cheque cashing and payday lending. He has authored numerous peer reviewed articles as well as book chapters and one book on matters relating to financial exclusion and fringe financial services.[1]

Dr. Chris Robinson (CV 8)

Dr. Robinson hold a PhD in finance and is a certified financial planner and chartered accountant. He was qualified as an expert in finance by the PUB in the previous payday lending proceeding. He is the author of reports for Industry Canada and Acorn regarding the payday lending industry. Dr. Robinson is the recipient of a number of best paper awards on subjects such as personal finance.

Dr. Wayne Simpson (CV 9)

Dr. Simpson is an economist with particular expertise in econometrics and micro-economics. He has been qualified as an expert witness in statistical analysis in PUB proceedings relating to payday lending and in econometrics and micro-economics for the purpose of providing evidence relating to the risks faced by Manitoba Public Insurance. Dr. Simpson is the co-author of "Examining Evidence of Financial & Credit Exclusion in Canada from 1999-2005," *Journal of Socio-Economcs* vol. 38, 2009, 966-976.

Dana Bazarkulova (Professor and PhD Candidate) (CV 10)

Ms Bazarkulova is an economist with particular expertise in econometrics and micro-economics. Her teaching experience includes microeconomics, money and banking and mathematical methods.

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1 For examples of his work, please see *Hard Choices: Financial Exclusion and Fringe Banks in Inner-city Canada, 'The Changing Structure of Inner-city Retail Banking: Examining Bank Branch and Payday Loan Outlet Locations in Winnipeg, 1980-2009,'* Canadian Journal of Urban Research, *'Banking on the Margin in Canada,'* Economic Development Quarterly, *'Two-Tier Banking: The Rise of Fringe Banks in Winnipeg's Inner-city,'* Canadian Journal of Urban Research.

Overview of the Evidence Filed

A Profile of Canadian Payday Loan Customers[2]

Dr. Simpson and Ms Bazarkulova explore the profile of Canadian payday loan customers based on 2009 data. They note that almost half of the payday loan customers surveyed used the service at least three times during the last 12 months. Frequent users tended to have lower family incomes than less frequent payday loan users.

Dr. Simpson and Ms Bazarkulova conclude that lower household income, lower assets, employment, lower education, younger age, unmarried individuals,and financial responsibility for children each increase the probability of having taken out a payday loan and increase the probability of repeat use of payday lenders.

Payday Lending Literature Review

The Bucklands examine recent US and Canadian academic literature exploring the payday loan controversy. They observe that payday loan operations in the US now outnumber Starbucks and McDonald's combined. A recent survey from The Pew Charitable Trust concludes that:

> [Payday loans] are a highly controversial form of credit, as borrowers find fast relief but often struggle for months to repay obligations marketed as lasting only weeks. While proponents argue that payday lending is a vital way to help underserved people solve temporary cash-flow problems, opponents claim that the practice preys on overburdened people with expensive debt that is usually impossible to retire on the borrower's next payday (Pew Charitable Trust, 2012, p.4).

The Bucklands cite American data showing that the primary profit driver of the industry comes from "churning" repeat borrowers and suggesting that these clients are being harmed by what may become an unmanageable cycle of debt. They also reference an intriguing US study suggesting that consumers were "helped by a maximum amount that could be borrowed, a lower interest rate on the payday loan, and shorter term that the loan could be carried."

In terms of the relationship between banking services and fringe financial services in Canada, the Bucklands references analysis suggesting that mainstream financial institutions have migrated to the suburbs with the void being at least partially filled by so-called fringe financial institutions especially payday lender. They cite Winnipeg research concluding that payday lenders with their small loans, check-cashing and bill payment service have become the only banking option for low-income people in some neighbourhoods.

2 *Payday Loans Consumer Profile based on the 2009 Canada Financial Capabilities Survey*

Research examined by the Bucklands suggests that "information disclosure and financial education surrounding the payday borrowing decision has a significant impact on whether that consumer takes out a payday loan. Getting a consumer to think more long term about adding up the costs of the loan over time reduces the frequency of payday borrowing."

The Bucklands concludes by identifying two key factors central to the payday lending debate:

- at present, there is no large-scale alternative to the payday lending for many low-income consumers who need cash to pay their bills and live their lives; and,
- there is evidence that in jurisdictions where clients are repeat borrowers, harm can result. This is because these payday clients repeatedly renew their payday loans and fall into an unmanageable cycle of debt and bankruptcy.

Regulation of the Payday Lending Industry – Are the Rate Caps Reasonable?

Dr. Robinson note that companies in a rate regulation proceeding ordinarily provide extensive audited financial information and allow access to their accounting systems through queries. He invites any payday loan company which takes issue with current Manitoba rate cap to provide several years of audited financial statements in support of their contention as well as information regarding their sales volumes.

Dr. Robinson revisits his evidence from the previous PUB proceeding in which he argued:

> A just and reasonable rate for a payday lender to charge is a rate that allows an efficient lender to recover costs and earn a reasonable profit but not an excess profit.

Dr. Robinson notes that the number of stores operated by larger payday loan operators such as Money Mart and Cash Money in 2013 are comparable to the number operated by the these two firms in 2009. Noting a decline in the number of stores in Manitoba, Dr. Robinson observes that:

> These numbers are consistent with the normal progression observed in most new industries. The opportunity for easy profits with high prices has vanished and efficiency becomes essential for survival. The large chains have economies of scale in advertising, oversight and systems that keep their costs per loan lower than independent stores.

In anticipation of claims that access to payday loans has diminished, Dr. Robinson observes that a "claim that rate caps have restricted availability of payday loans would have to be accompanied by comprehensive evidence that loan volume per store has declined and no such evidence is available."

In terms of the rate cap in Ontario, Dr. Robinson notes that:

> the introduction of a 21% rate cap in Ontario seems to have allowed more revenue than the major chains needed to remain profitable since they are now lowering rates below the cap.

Dr. Robinson concludes that the current rate cap of 17% of the principal amount of a payday loan is reasonable. He notes that a significant number of payday lenders continue to operate in Manitoba signalling that they can continue to earn a fair rate of return at that rate. He points out that the Ontario rate cap is 21% and two of the largest lenders are now offering some discounted prices to increase business. He draws the reasonable inference that the Ontario cap is too high and the Manitoba cap is probably appropriate.

Based on information provided in the prior proceeding, Dr. Robinson also observes that some US states have rate caps that effectively bar payday lenders while most of the rest have instituted rate caps of 13% - 19% with the commonest single cap being 15%. The major payday lending firms are generally profitable in Canada and the US, which he considers to be further evidence that the rate caps are not too low.

Report on Mystery Shopping Payday Lending and Payday Lending-Like Outlets in Winnipeg

Based on the mystery shopping evidence, the payday lending firms charged $17/$100 for their payday loans. Evidence was found of variation in the fees and policies related to defaults and extensions.

The payday-loan like products, or LOCs, charged higher fees including a brokerage fees and numerous associated charges. This makes them a comparatively more expensive product. These outlets appear to charge $24.50/$100 broker fee in addition to a 16 cents/$100/day for the basic loan. Other charges included a $5.00 MasterCard activation fee, $24.95 monthly fee and $2.25 per transaction. One staff person estimated that a loan of $100 would cost $75.[3] The multiple charges and fees associated with the LOCs made them confusing to understand.

Shoppers found that most payday lending outlets have a 7-day cooling off period before they can borrow another loan. Some outlets have provisions for delaying their payments requiring customers to call in advance of a default to make arrangements. The amounts involved in making the arrangements appear to be applied on a case by case basis and there is therefore a lack of transparency in the process.

The data indicated a general deficit in disclosure of product information especially regarding fees. There is a need for additional written information which the customer can take away to consider. The data also suggested that more effort needs to be made to ensure compliance

3 Report on Mystery Shopping, p. 2

to consumer privacy protection through the practices and policies of pay lending outlets.

A surprising result from the mystery shopping was that some payday lenders offer loans collateralized on income sources other than employment. This included entitlement cheques such as Child Tax Benefits. While some payday lenders have renamed their product to line of credit other lenders have broadened the type of collateralized income they rely on.

Exit Interviews of Payday lending customers

In total there were 56 surveys completed by people who had recent experience with a small loan from Cash Money, Money Mart and The Cash Store. Almost all customers claim to understand how the loan works as well as the fee components and total fees. However consumers reported less understanding of the fee components and total fees than the working of the loan.

A number of reasons were offered in support of the choice of payday lenders. Among the reasons cited were the welcoming environment, less time involved in getting a loan and ineligibility for a bank or credit card.

Historical Data and Maps

This exercise tracks the development of the payday lending industry in Winnipeg. It notes slow growth through the 1990s with rapid growth between 2001 and 2009. The number of outlets has declined since 2009. Roughly half the current number of outlets are in the inner city and roughly half in the suburbs. Taking into account Cash Store Financial outlets, the number of outlets present in Winnipeg in 2013 approximates the number available in 2005[4].

Conclusion

Winnipeg Harvest and CAC MB appreciate the opportunity to participate in this hearing. They will provide their recommendations after considering the evidence of other parties.

Yours truly,

BYRON WILLIAMS
DIRECTOR

BW/sk

cc. CAC Manitoba
Winnipeg Harvest

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4 The numbers presented in this analysis may differ from numbers presented elsewhere in part due to timing differences.