ISSUES + INSIGHTS

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Payday Lending and Auto Title Lending: Who Borrows and Why?

Payday and auto title loans threaten the economic security of some individuals, families and communities. The presence of loan stores combined with the absence of banks in these communities makes it tempting for mothers and fathers with economic need to take out an initial loan. The structure of the payday and auto title loans often then creates further economic instability for individuals, families and communities of color with low-incomes.

Recognizing both parents' commitment to their children and the flow of resources in many low-income families and communities, this paper explores how payday and auto title loans work, who uses them, and why. The ways in which these and related industries develop, adapt, expand, and impact communities is also considered. A current project of the Center for Family Policy and Practice focuses on the economic security of families of color with low incomes in four specific states. Therefore, much of this article's analysis of payday and auto title loans focuses on Georgia, Louisiana, Mississippi and Wisconsin.

How do payday and auto title loans work?

Payday lending, auto title lending, check-cashing outlets, money transmitters, pawnshops, refund anticipation loans, and rent-to-own stores all operate outside of federally insured banks (and FDIC regulations). Sometimes these are referred to as alternative financial services providers (AFSPs). Payday lending was virtually unheard of in the 1980s and then flourished as the wages of many workers declined and fewer jobs were available. Credit, in various forms, was increasingly made available and more people became dependent on it to meet everyday expenses.

Payday and auto title loans are not subject to the same consumer protections as bank loans. Payday loans are often less than $500, and because they are expected to carry over to the next paycheck, they are typically 14- or 30-day loans that include initial fees (which some states cap and others do not) and that generally involve a state's maximum allowed annual percentage rate (APR) for a small dollar loan which ranges from 300% to more than 1,000% (credit.com, 2014). Payday lenders typically require documentation of income which may include a paystub (no more than 30 days old), government benefits award letter, tax return showing self-employment income, business contracts showing future self-employment, an agreement showing alimony, evidence of child support or maintenance currently being paid or a transmittal letter of pension being paid. Beyond showing some form of current income, lenders do not assess borrowers' ability to repay (This may change, however. See Consumer Financial Protection Bureau proposed rules). Additionally, people taking out payday loans leave a post-dated check with the lender so the money can be withdrawn from the person's account when the loan is due. While the payday industry markets their products as short term loans, borrowers end up taking out multiple loans and are indebted for an average of five months per year (Pew, 2012). Typically, loans are renewed eight times (Coleman and Davis, 2016). A Georgetown University study found that 85% of borrowers took out three or more loans in one year and nearly 25% took out 14 or more (Matthis, 2011). Payday loans do not amortize, so if not paid in full at the due date, subsequent regular payments only cover interest and fees and not principal. Clearly, payday loans have much more impact than just "getting you to the next paycheck."

Auto title loans work differently. They are structured so that a person who borrowers typically gives the lender the clear title to the vehicle and often an extra set of keys in exchange for the agreed upon loan dollar value. A typical practice is to mount a GPS tracking device on the borrower's vehicle to expedite the lender's repossession of the vehicle if the loan payments are not made by the specified date. Auto title loan fees are generally larger than payday loans and also have triple digit interest rates and a term of 30 days. Pew (2015) indicates that more than two million people utilize auto title loans annually. These loans are structured to be unaffordable and the borrower's ability to repay is not considered when granting the loan. (This may also change. See CFPB proposed rules.) They are completely asset-based. When a person who borrows is unable to pay off the loan on top of her/his other expenses, the options are to: 1) pay only the fee and extend or renew the loan, 2) take out a new loan shortly after paying the old one, or 3) face repossession of the vehicle. Some research indicates that as many as 71% of the title loan customers have their vehicles repossessed (Martin and Adams, 2012). Repossession has particularly negative impacts because people who borrow commonly use the vehicle to travel to school or work (80%), or to medical appointments (95%) and/or to buy food and other household goods (98%) (Pew, 2015). Of the less-than-ideal options, borrowers often choose renewal and typically renew the loan eight times (Montezemolo, 2013).

In addition to high interest rates, the payday loan industry collects more than $3,400,000,000 per year in fees alone (National People's Action, 2012). According to Senator Elizabeth Warren (D-MA) the average person taking out a payday loan spends $2412 annually in fees and interest (Color of Wealth, 2016). Across the nation, there are more payday loan stores than McDonald's, and in some communities, more payday lenders than Starbucks. The auto title loan industry grants 2 million loans annually worth $1,900,000,000 and it is estimated that borrowers pay $4,300,000,000 in fees alone (Montezemolo, 2013). People who take out an auto title loan are spending more than twice as much on fees and interest as they are receiving in loan dollars. By 2015, auto title loans were available in 25 states, and approximately 3% of adults across the nation had used them. Payday loans are more pervasive and are available in 46 states, prohibited only in Georgia, New York, New Jersey, and Arkansas (Pay Day Loan Consumer Information, 2016). As of 2013, approximately 5% of households in the nation had utilized payday loans (FDIC, 2013).

Who are the people taking out payday and auto title loans?

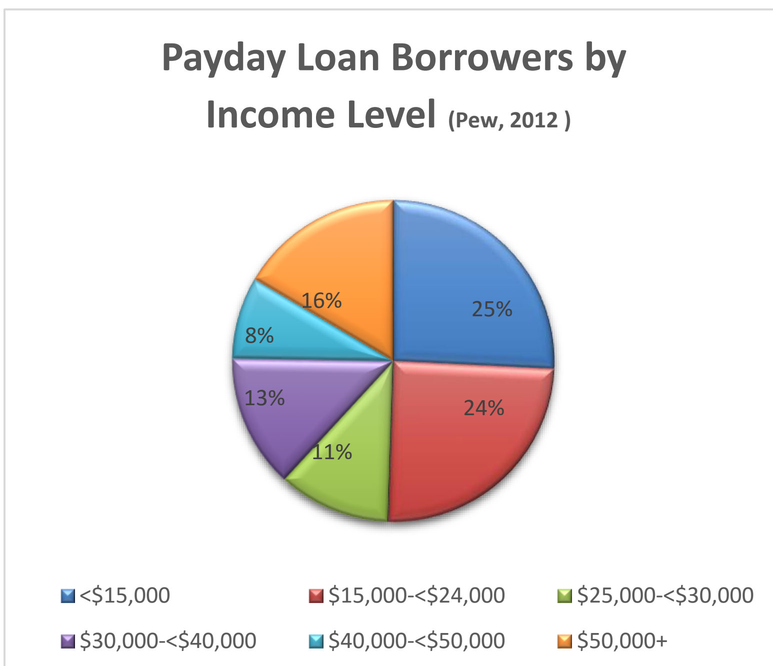
Information available about the borrowers is limited and looks within, but not across demographic categories. Therefore, our understanding of who actually borrows fits only into single demographic categories and we know that people do not.

Household Type

Among those included in the 2013 FDIC Survey of Unbanked and Underbanked Households, unmarried female headed households most commonly identified as payday loan borrowers at 9% and individual males and unmarried male-headed households follow, each at 7%. (Unmarried female- and unmarried male- headed households are defined as including two or more people related by birth, marriage, or adoption and residing together, along with any unrelated people who may also reside in the household. Single mothers, as well as single fathers are included in this category.) Married couples are the least likely to become payday loan borrowers at 3% (FDIC, 2013). The same survey indicates that nationwide, 5% of all respondents have taken out a payday loan. It is not stated where a noncustodial parent who utilizes payday or auto title loans fits into the data. Presumably, these fathers and mothers fit into the categories of unmarried male or female headed households. This indicates that single mothers and fathers are more likely to utilize payday loans than married couples or single women. Pew (2012) supports this interpretation by indicating that people who are separated or divorced are 103% more likely to have used a payday loan than people who are married.

Income

While individuals of all income levels utilize these payday and auto title loans, nearly half of all users earn less than $25,000 (FDIC, 2013; Pew, 2012). Of payday borrowers, 25% earn less than $15,000 and 24% earn between $15,000 and $25,000 (Pew, 2012). In the realm of auto title loans, Pew (2015) indicates that 20% of borrowers earn less than $15,000 annually and 22% earn between $15,000 and $24,999 annually. The Center for Responsible Lending has reported that auto title loan borrowers earning $25,000 per year cannot afford to repay the average loan amount of $1,042—even with a "free" loan with no fee—in a one-



month loan term. Therefore, the auto title loan industry has the effect of pushing at least 42% of its borrowers into economic insecurity.

Across the FDIC's income groups, the highest use rates are typically in the category of $15,000-$30,000. This is not true in Mississippi where 12% of people in the less than $15,000 category have used payday loans and only 7% in the $15,000-$30,000 (FDIC, 2013).

Clearly, single parents (custodial and non-custodial) with low incomes are frequent users of payday and auto title loans.

Race/ethnicity

Analysis of the race and ethnicity of people who use payday and auto title loans suggests that disproportionate use is associated with disproportionately high access to wealth-stripping loans and limited access to bank loans with stronger consumer protections. Pew (2012) determined that African Americans are 103% more like to use a payday loan than whites. Nationwide, people who identify as Asian or White are least likely to take out payday and auto title loans and people who identify as Black or American Indian/Alaskan are most likely to be drawn into the loans. This is especially true in Mississippi, where the rate of payday loan use among Blacks is 12%, which is significantly higher than the overall rate of use nationally (5%) and higher than the nationwide rate of use among African Americans (10%).

Percentage of People Nationwide That Use Loans by Race/Ethnicity

(FDIC, 2013)

	Payday Loan	Auto Title Loan
Black	10%	4%
American Indian/Alaskan	8%	5%
Hawaiian/Pacific Islander	6%	3%
Hispanic	5%	3%
White non-Black non-Hispanic	4%	2%
Asian	1%	1%

Overall in the US, the highest use of auto title loans is among American Indians/Alaskans at 5% (FDIC, 2013). Use of the loans among Blacks is much higher in Georgia and Mississippi than it is nationally. In Mississippi, 11% of Blacks utilized auto title loans and in Georgia the rate was 7%. Nationwide, use by Blacks is just 4%, which is still twice the nationwide usage rate of Whites. Interestingly, in Wisconsin, the highest rate of auto-title-loan use reported was for Hispanics at 7%, followed by Blacks at 4%. It is unclear why Wisconsin would differ from other states, but the current political climate and national policies on immigration clearly create incentives for many undocumented Latinos to avoid utilizing formal US institutions like the banking system. Auto title loans that don't require a bank account may be the only feasible option for many.

Education Level and Employment Status
Education level also correlates with use of these banking alternatives. The use of both payday and auto title loans drops dramatically with the completion of a college degree. Similarly, Pew (2012) found that 89% of borrowers do not have college degrees.

Nationwide Use of Auto Title and Payday Loans by Education Level

	Payday	Auto Title
No high school degree	5.2%	3.9%
High school degree	5.1%	2.9%
Some college	6.6%	3.2%
College degree	2.2%	1.6%

(FDIC, 2013)

Borrowers are also twice as likely to be unemployed than employed (FDIC, 2013). We do not have the complex analysis that looks across these categories to fully understand who the borrowers are, but since borrowers use these loans to meet everyday expenses, many single parents with low income who are unemployed and do not have a college degree are likely to rely on payday and auto title loans to provide for their children.

While overall data about use does not look across groups, it is clear that ~25% of payday and auto title loan borrowers earn less than $15,000 annually and about another 25% earn between $15,000 and $30,000 annually. Single parents (custodial and noncustodial) are frequent users. Almost all borrowers have less than a college degree and borrowers are twice as likely as those who do not borrow to be unemployed. And finally, people of color are more likely to be borrowers than white people. It would be easy to end the story here and reasonable to think of people who utilize payday or auto title loans as financially irresponsible or just going through "tough times." While either or both of those may be true, the story of why people become borrowers is not that simple.

What factors create the conditions that lead single parents, people with low incomes, people of color, and people with less formal schooling to become payday and auto-title loan borrowers?
While payday lending is a fairly new practice and auto title lending is even newer, these industries have boomed. The data available is limited and sometimes inconsistent. Factors include the state and neighborhood in which one lives, access to banks, and the presence and accessibility of payday and auto title lenders. That said, there is evidence indicating that certain factors help ensure that certain people become payday and auto-title loan customers.

State context

There is little policy regulation at the federal level, but there have been a variety of regulatory efforts at the state level. These range from limiting APRs to banning payday lending outright. The chart below is based on usage and fees across states and highlights some of the differences.

Perhaps the most striking aspect of the table below is the APR of payday loans in each state. As noted earlier, the range is 300% to 1000%. The lowest end of that is well beyond typical credit rates, the credit mechanism commonly used by middle- and upper-income individuals. As the table below also suggests, the sheer number of payday loan stores is significant, and differs by state.

Overview of Payday Loan Usage and Annual Fees
(excerpted from Profiting from Poverty, 2012 and FDIC, 2013)

State	Households that have used payday loans*	Licensed Payday Lenders (2011)	Payday Loan APR Charged	Annual Fees from Payday Loans
Georgia	3.9%	*	*	*
Louisiana	6.5%	942	560%	$287,000,000
Mississippi	7.5%	938	574%	$267,009,242
Wisconsin	3.6%	436	574%	$96,800,000
US Totals	4.6%	17,630		$3,366,217,743

*As of 2004, Georgia law imposes stiff penalties for payday lending by non-banks and in-state banks, and is the first state law to expressly prohibit payday lenders from partnering with out-of-state banks to evade state usury limits.

While Georgia has banned payday lending, Louisiana, Mississippi and Wisconsin are considered "permissive" states which are "the least regulated and allow initial fees of 15% of the borrowed principal or higher" (Pew, 2012, p. 20). Often, states with the most payday loan stores also have the highest concentrations of credit-challenged residents. Mississippi and Louisiana are examples of that. Mississippi has approximately six times as many payday lending stores per capita as the national average and Louisiana has four times as many. This suggests that payday lenders may tend to locate in states where demand for their services is likely to be high because a significant portion of the population has weak or no credit scores and therefore, cannot access forms of credit with consumer protections (Prager, 2009, p. 15).

Auto title lending numbers tell a parallel story. Location and numbers matter. There are more than 8,000 title loan stores operating in 25 states and they fund close to $2 billion in loans annually (Pew, 2012). Georgia, Louisiana, Mississippi and Wisconsin are included in the 21 states with a "significant" presence of auto title lending (at least $4 million/year, not including refinances) (Center for Responsible Lending, 2015), which is connected to the annual dollar value of loans granted. Usage rates of auto title loans by residents of Georgia, Louisiana, Mississippi and Wisconsin exceed the national average and Mississippians use auto title loans at a rate of more than twice the national average. And in terms of the number of stores, the number of loans, and loan value, Georgia and Mississippi do about double the business of Louisiana and Wisconsin. It is especially noteworthy that Mississippi has more than three times as many auto title loan stores per 100,000 residents than Georgia, less than one-third the population, and nearly the same number of loans and loan values as Georgia.

An Overview of Auto Title Loan Usage
(adapted from Pew, 2015 and FDIC, 2013)

State	% of Residents That Have Used Auto Title Loans	Auto Title Lending Stores per 100,000 Residents	Population	Total # Loans	Value of Loans Granted Annually
Georgia	5	3.6	10,250,000	85,125	$88,700,250
Louisiana	4	4.0	4,670,000	40,860	$42,576,120
Mississippi	7	12	2,993,000	81,720	$85,152,240
Wisconsin	3	2.8	5,771,000	36,774	$38,318,508
US Totals	3	2.5		1,955,256	$1,932,023,417

Location. Location. Location: Access to Loans When Banks Aren't Prominent
The location of lenders within a neighborhood tells another piece of the story. Wealth-stripping lenders are much more prominent in neighborhoods where people have low incomes (especially in large urban areas) and in many of these areas, the number of payday loan stores outnumbers mainstream banks (Matthis, 2011). Although the Consumer Financial Protection Bureau (CFPB) recently proposed rules that would require some level of assessment of payday loan borrower's ability to pay, currently, neither payday loans nor auto title loans assess the borrower's ability to repay the loan and auto title loans do not require that a borrower have a bank account.

In other words, the presence and location of payday and auto title loan stores indicates that they are intended to be accessible and visible to people who have little or no access to or connection with traditional banking institutions.

Location + Demographics
Without ready and reasonable access to the banking system and its consumer safeguards and the necessary relationship with those institutions, people who need access to cash are likely to choose a payday and/or auto title loan store in their neighborhood. An estimated 26% of all

American households representing 39 million adults are either unbanked or underbanked[1] (National People's Action, 2012) and that correlates with race and ethnicity in the United States. An estimated 54% of African Americans, 47% of Hispanics, and 42% of Native Americans fit into the unbanked or underbanked categories and only 20% of Whites fit those categories (FDIC, 2013). Among people who are underbanked or unbanked, 60% live in households where Spanish is the only language spoken and 51% are foreign born non-citizens (FDIC, 2013). This indicates that payday loan and auto title loans are more accessible loan options than traditional banks for people of color, Spanish-only speakers and/or people born outside the United States who are not citizens. In some communities, payday and auto title lending are the only options available.

Payday and auto title loans don't do business where there are banks and banks don't do much business where there are people of color, Spanish-only speakers and/or foreign-born non-citizens. Payday and auto title lenders are typically found in neighborhoods where people of color live who are struggling to make ends meet. For example, Mississippi had the highest concentration of licensed payday lenders in the nation (Center for Responsible Lending, 2013). In March 2014, the FDIC reported 823 bank branches in Mississippi and in August 2013, the Mississippi Department of Banking and Consumer Finance reported 898 payday loan stores. Of those, 97% (871) were located in zip codes with a median household income between $20,000 and $60,000 and all of the stores were located in areas with minority populations of more than 20%. These areas also suffer from high unemployment (Kurban, Diagne and Otabor, 2014).

Payday lenders are located in neighborhoods where people of color with low incomes live and where there are no banks. Yet, payday and auto title loans are visible and accessible, and therefore are utilized. Most borrowers use payday loans to cover ordinary living expenses, not unexpected emergencies which tells us that people simply aren't making enough money compared to their daily living needs (Safe Loans Coalition, 2016). The Pew Trust (2012) reports that 69% of borrowers used loan money to cover recurring expenses such as utilities, credit card bills, rent or mortgage payments, or food, and 16% dealt with unexpected expenses such as a car repair or emergency medical expense. It is unclear whether or not the fathers and mothers in that report use the loans for the recurring expense of child support payments or not. Yet, one can reasonably expect that the 69% of people taking out payday and auto title loans to cover recurring expenses will struggle to pay back the $2412 in fees and interest experienced by the average borrower. These are multi-billion dollar industries that are utilized by a small percentage of people in the United States. The numbers highlight the potential for the loans to undermine the economic security of people using them.

[1] The Federal Deposit Insurance Commission identifies a household as "unbanked" if they answered "no" to the question, "Do you or does anyone in your household currently have a checking or savings account?" Underbanked households are defined as those households that have a checking and/or a savings account and had used utilized an alternative financial services provider in the past 12 months.

Additionally, Louisiana ranks sixth in the nation in percentage of households reliant on alternative financial services providers (AFSPs) like payday and auto title lenders. The FDIC's 2013 Survey of Unbanked and Underbanked Households shows that in Louisiana, just 2% of people who are fully banked have ever used payday loans while 18% of people who are underbanked, and 7% of people who are unbanked, have ever used payday loans. The discrepancies hold among auto-title loan users as well. The same survey indicates that in Louisiana, the rate of auto-title loan use among fully banked people is 0.7%, while it it is 11.7% among people who are underbanked, and just 1.5% among unbanked people. Neighborhoods with payday and auto-title loan stores are on average 70% Black, with median household annual incomes of $16,562. Neighborhoods with banks, on the other hand, are on average 46% Black, with median household earnings of $24,137. Generally, researchers have determined that communities where people of color with low incomes live are attractive to alternative financial service providers because of "systematic neglect by traditional financial institutions" (Kurban, Diagne and Otabor, 2014, p. 9).

> In Louisiana, payday loan neighborhoods are on average 70% African American with a median household annual income of $16,562. Bank neighborhoods, on the other hand, are on average 46% African American with median household annual earnings of $24,137.

It is evident that payday and auto title lenders are setting up shop in low-income communities of color and banks are not. In other words, the stage is set to ensure that parents with low-incomes are "unbanked" and can readily turn to payday and auto title lenders in an effort to meet the economic needs of their families. Yet Wells Fargo, JPMorganChase, US Bank and Bank of America (the largest banks in the United States) are creditors to the major payday lending companies in those same communities. So, while the banks are physically neglecting low-income neighborhoods where parents of color live. So, those bank corporations are positioned to make money from customers with stronger credit scores through traditional bank and credit card loans while having no incentive to offer the same safe consumer-safeguarded products to fathers and mothers of color who have low incomes and low credit scores. Banks have positioned themselves to maximize profits by failing to locate banks in those neighborhoods and by instead offering lines of credit to payday and auto title lenders. While maximizing their own profits, banks are also helping to undermine the economic security of families of color with low incomes.

> Wells Fargo, JPMorganChase, US Bank and Bank of America (the largest banks in the US) are creditors to the major payday lending companies.

So, fathers and mothers of color with low incomes that are trying to take care of their children are not protected through the consumer safeguards afforded to others. It is essential to remember that less than five percent of people use payday or auto title loans, yet these multibillion dollar industries have developed on the backs of a tiny percentage of the population and are established in low income neighborhoods where unbanked and underbanked people live. The behind-the-scenes role of banks suggests both the need for federal regulation and for accountability to people whose economic security is being undermined, particularly fathers and mothers of color with lower incomes. As the US Congress and individual states work to regulate or ban payday and auto title lending and as the Consumer Financial Protection Bureau (see box on right) finalizes related rules, they would benefit from considering who the borrowers actually are, the flow of money within those families and communities and the development of the industries and the impacts they are having on the economic security of low-income parents as they work to provide for, protect, and support their children and themselves.

Conclusion

As wages have declined over the last 40 years, people utilize payday and auto title loans to meet everyday expenses. While we do not have the complex analysis that looks across these demographic categories to fully understand who the borrowers are, the data suggests that many of the people who turn to these loan options are single mothers and fathers of color with low-incomes who are struggling to provide for their children and do not have a college degree. We also know that payday and auto title lenders are setting up storefronts in neighborhoods where there are no banks. These are the neighborhoods with high unemployment rates, where people of color, Spanish-only speakers and/or those who are born outside the United States and who are not citizens live. When 49% of people taking out payday loans and 42% of people taking out auto-title loans make less than $25,000/year, and when the loans follow the payday and auto-title

Consumer Financial Protection Bureau's (CFPB's) Proposed Rules

The CFPB has proposed rules to regulate payday and auto title loans as well as other alternative financial services providers. The public is encouraged to comment before October 7, 2016. Comments can be share online at: https://www.regulations.gov/. Included below are links to the analyses of a few organizations.

- The Pew Charitable Trusts
- Center for Responsible Lending
- National Community Reinvestment Coalition

Given what we understand about how the payday and auto title lending industries function and therefore, who borrows, please review and comment in ways that support the economic security of fathers, mothers, children, families and communities of color with low incomes.

lending business models, which are predicated on repeat borrowing, people's economic security is undermined. We know that the individual borrowers—and in all likelihood, their families, children and communities—will be pushed into or fall further into poverty. By calculating a $600 loss of annual savings and the estimated loss of investment per payday loan customer, a small community with 200 payday customers is found to lose about $15,000,000 in wealth over 30 years (Kurban, Diagne and Otabor, 2014). Payday and auto title loans are structured to create repeat borrowers in neighborhoods where the economic security of individuals, families and communities is easily undermined.

As part of the Center for Family Policy and Practice's work around understanding the economic lives of families of color with low incomes, we are in regular conversations with those fathers and mothers, especially in Georgia, Louisiana, Mississippi and Wisconsin. We seek to understand how these mothers and fathers navigate policies and related practices (e.g., child support, payday and auto title lending, SNAP, birth cost recovery) many of which serve to undermine the economic security of their families. Their stories and the lessons learned will inform our future reporting on these issues.

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Mission Statement: The mission of the **CENTER FOR FAMILY POLICY AND PRACTICE (CFFPP)** is to strengthen society through the expansion of opportunities for low-income parents – mothers and fathers – to protect and support their children. CFFPP operates as a policy think tank to remove the unique barriers and negative public perceptions that affect low-income men of color. Through technical assistance, policy research and analysis, and public education and outreach, CFFPP works to support low-income families and develop public awareness of their needs.

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