



# High-Cost Alternative Financial Services: Issues and Impact

## DEFINING HIGH-COST ALTERNATIVE FINANCIAL SERVICES

Several banking and credit alternatives exist beyond the traditional financial system. Referred to as high-cost alternative financial services in this report, these alternatives supply credit-constrained individuals with fast, convenient access to cash or assets at a high price. Their interest rates sometimes meet or exceed the 60 per cent maximum set out in the Criminal Code of Canada. These services also often have added fees, hidden fees and high default rates.

Like payday lenders,<sup>1</sup> providers of the high-cost alternative financial services explored in this report are predominantly located in lower-income neighbourhoods (see appendix A).<sup>2</sup> Though some studies reveal nuanced demographic differences in who seeks what type of product,<sup>3</sup> community research suggests that individuals who access these high-cost alternative financial services do so for the same reasons they access payday loans, and also fit within similar demographic groups.<sup>4</sup> Many borrowers encounter barriers to banking and securing credit with mainstream financial institutions, and for some, these high-cost alternatives are the only option.<sup>5</sup>



1. Momentum, *Opportunities for Municipal Action on Payday Lending* (Calgary: Momentum Community Economic Development Society, 2014), 1, <http://momentum.org/files/Publications/Municipal%20Micro-Lending.pdf>.
2. Please see Appendix A for a map of Calgary, which illustrates the relationship between neighbourhood poverty rates and the prevalence of businesses that offer high-cost alternative financial services.
3. For an analysis of who uses high-cost alternative financial services and why, please see the following report: Joe Fantauzzi, *Predatory Lending: A Survey of High Interest Alternative Financial Service Users* (Toronto: Canadian Centre for Policy Alternatives Ontario Office and ACORN Canada, 2016), 9, <https://www.policyalternatives.ca/sites/default/files/uploads/publications/Ontario%20Office/2016/12/CCPA-ON%20predatory%20lending%20Dec%201.pdf>.
4. Momentum, *High-Cost Alternative Financial Services: The Customer Experience* (Calgary: Momentum Community Economic Development Society, 2017) <http://www.momentum.org/files/Publications/Part%202%20Experiences%20with%20High%20Cost%20Financial%20Services.pdf>.
5. Though this report is focused on the negative impact of high-cost alternative financial services on lower-income individuals and communities, several demographic groups including middle- and high-income consumers do access these products. High-cost alternative financial services can harm anyone's financial well-being, and the lending practices of these businesses often violate the rules that govern fair and responsible lending in other jurisdictions.

## CONTEXT

In 2016, the Government of Alberta undertook a significant reform of the rules that govern payday lenders. The legislative and regulatory changes introduced in *An Act to End Predatory Lending* have considerably reduced the cost of a payday loan, enabling Albertans to get out of debt sooner, and have spurred the creation of payday loan alternatives at mainstream financial institutions. These are important changes, particularly for individuals living in poverty, and these successes can be built upon.

A variety of high-cost lenders exist across the province in addition to payday loan companies. Considered together, these products and services warrant the attention of government, financial institutions, communities and consumers for a variety of reasons. This report explores a number of the high-cost alternative financial services currently available in Alberta, identifies common themes and issues with these products, and considers their impact on people living on a low income and the communities in which they live. The services analyzed in this report are: rent-to-own (RTO) financing, high-cost instalment loans; pawn loans, cheque cashing, title loans, and sub-prime auto loans.

When compared to payday lending, little is known about these high-cost alternative financial services. Unlike payday lenders some of these services are unlicensed, and data describing use, prevalence, financial value of businesses and overall impact is limited. Thus, the list provided in this report is not comprehensive and should be viewed as a starting point.<sup>6</sup> Products were selected for analysis based on popularity (i.e., used most frequently), pervasiveness (both in terms of number of stores and advertisements), extent of documented challenges experienced by consumers and additional feedback received through consultation with Albertans living on a low-income.

High-cost alternative financial services explored in this report	
Service	Description
<b>Rent-to-own financing</b>	A financing option that allows consumers to lease a major household appliance or piece of furniture for a weekly, bi-weekly or monthly fee over a set period of time (e.g., 130 weeks). If the consumer makes all payments over the duration of the contract, they are granted ownership of the item.
<b>Instalment loans</b>	High-interest loans between \$500 and \$15,000 that are paid back in instalments over a set period of time (up to 60 months).
<b>Pawn loans</b>	Short-term loans (often 30 days) secured against personal property such as electronics and jewelry. The amount loaned is determined based on the value of the pawned product. To buy back an item, the borrower must pay back the loan plus interest.
<b>Cheque cashing</b>	A service that allows individuals to, for a fee, cash cheques and receive funds immediately without the account holds and waiting periods often imposed by mainstream financial institutions.
<b>Title loans</b>	High-interest loans between \$1000 and \$50,000 that are secured against a borrower's vehicle. Contract lengths range from 30 days to five years.
<b>Auto loans</b>	Sub-prime auto loans offered at a high interest rate to individuals with low credit scores. Extended term loans often result in lower monthly payment amounts but a higher overall cost of borrowing.

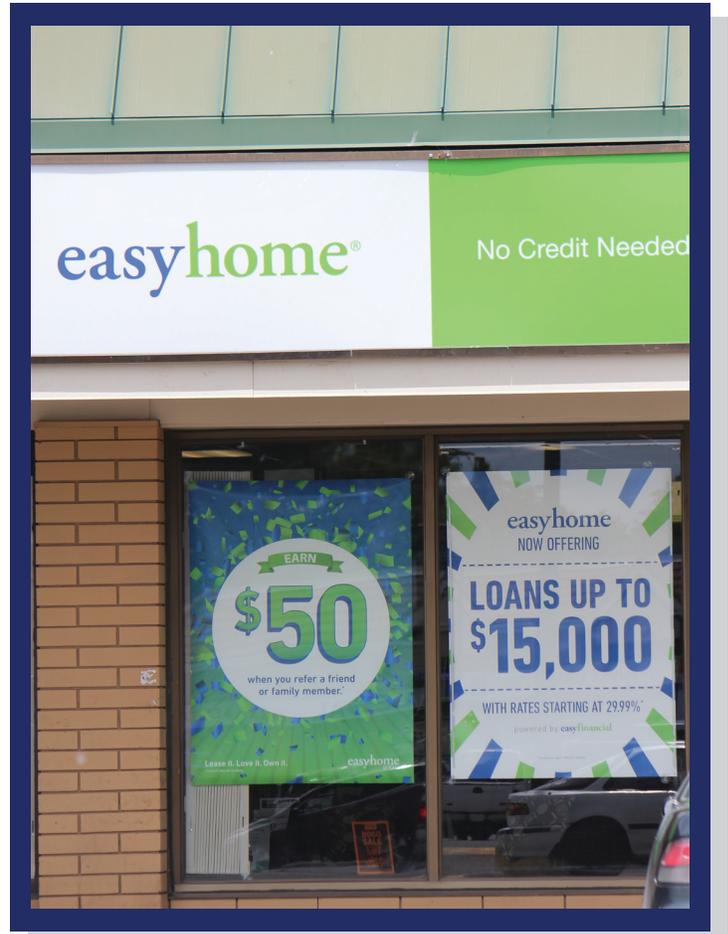
6. Additional products and services came to our attention during our research. They include settlement loans, mortgage refinancing services, tax refund advancers, credit repair companies, high-cost private colleges and training institutes and medical product rentals. All merit further consideration but were outside the scope of this report.

## HIGH-COST ALTERNATIVE FINANCIAL SERVICES IN FOCUS

### 1. Rent-to-own financing

RTO businesses such as Easyhome and Aaron's, allow customers to lease common household items like furniture, electronics and appliances for a weekly, bi-weekly or monthly fee without providing a credit report or down payment. If a customer successfully completes all payments over the rental term, which is often as long as three years, they will own the item.

Businesses like Easyhome market RTO financing as an accessible pathway to ownership with few conditions and flexible terms. This emphasis on ownership is reflected in the respective slogans of Easyhome and Aaron's: "Lease it. Love it. Own it.,"<sup>7</sup> and "Own it."<sup>8</sup> Marketing materials also highlight the convenience of these products. For example, the Easyhome website states that the company "approve[s] 97% of customers for leases, all you need is a source of income and a place of residence."<sup>9</sup> Considered alongside the nature of RTO agreements, these marketing tactics appeal to consumers who are able to make small, periodic payments, but lack the savings or credit to purchase an item outright. According to the Consumers Council of Canada, Easyhome describes its target market as "cash- and credit-constrained consumers,"<sup>10</sup> while Aaron's characterizes its customers as those "with limited access to traditional credit sources such as bank financing, instalment credit or credit cards."<sup>11</sup>



Though RTO rates appear affordable at first glance, particularly when compared to the upfront cost of an item, calculations reveal that the total cost of RTO financing can overwhelmingly exceed the cost of purchasing an item outright, typically by two to 3.4 times the retail price.<sup>12</sup> For example, the Easyhome website lists the rental price of a Macbook Air at \$39/week for a term of 130 weeks, or \$5,070 upon conclusion of the rental term. The same laptop retails for \$1,999 at the Apple Store, a price that indicates Easyhome charges customers 323 per cent more than Apple for the same item. This cost discrepancy means that when a customer enters into a RTO contract they accept negative equity, owing much more than the item is worth. Moreover, if a customer fails to make payments and is forced to return the item, contributed funds are not recouped. The Annual Percentage Rates (APR) associated with RTO financing are equally steep. Though Easyhome lists an APR of 29.9 per cent on its website, in reality the APR on some contracts exceeds the 60 per cent limit set out in the Criminal Code. In its study of the RTO industry the Consumers Council of Canada found a median APR of 79.8 per cent across 28 Easyhome audits,<sup>13</sup> and the maximum APR calculated for a product was 193.3 per cent.<sup>14</sup>

7. Easyhome Ltd., "The Winter Event," accessed May 29, 2017, [https://www.easyhome.ca/cmsstatic/FebMar\\_Flyer\\_EN\\_r3.pdf](https://www.easyhome.ca/cmsstatic/FebMar_Flyer_EN_r3.pdf).

8. Aaron's, "Own It," accessed May 29, 2017, <https://www.aarons.com/t-ownit.aspx>.

9. Easyhome Ltd., "Find out why Easyhome is the better choice," accessed May 29, 2017, <https://www.easyhome.ca/>.

10. Easyhome Ltd., "Easyhome Ltd. Introduces New Masterbrand – goeasy," press release, September 23, 2014, <http://investors.goeasy.com/phoenix.zhtml?c=83047&p=irol-newsArticle&ID=1970454>

11. Denise Barrett Consulting, *Consumer Experiences with Rent-to-Own* (Toronto: Consumers Council of Canada, 2016), 35, [http://www.consumerscouncil.com/site/consumers\\_council\\_of\\_canada/assets/pdf/ccr\\_rent\\_to\\_own\\_web.pdf](http://www.consumerscouncil.com/site/consumers_council_of_canada/assets/pdf/ccr_rent_to_own_web.pdf).

12. Denise Barrett Consulting, *Consumer Experiences with Rent-to-Own*, 6.

13. Ibid, 43.

14. Ibid, 42.

Information presented to customers by RTO businesses, both in-store and online, is often insufficient to support informed decision making.<sup>15</sup> For example, webpages and signage emphasize the weekly payment and contract duration (e.g., \$39/week for 130 weeks), but do not provide the total cost of ownership (i.e. the full cost of leasing the product to term). Moreover, the listed weekly payment includes the cost of insurance, (or Total Protection Coverage (TPC)), yet advertisements do not disclose that purchasing TPC is optional, and the APR of 29.9 per cent provided in-store and online is calculated based on the cost of product alone. Consumers have also identified that RTO businesses frequently engage in unfair and unreasonable practices, such as leasing used items as though they are new and offering delivery of an item for free when there is actually a fee.<sup>16</sup> Other borrower complaints include the use of aggressive collection tactics and termination of contracts (and subsequent repossession) after only one missed payment.<sup>17</sup>

As documented in a CBC *Marketplace* investigation of the RTO industry,<sup>18</sup> Canadians spend \$260 million each year on RTO products,<sup>19</sup> many of which are essential items like mattresses, fridges, and laundry appliances. The findings of a 2016 Canadian Centre for Policy Alternatives and ACORN Canada study of high-interest alternative financial service users in Canada confirms the growing prevalence of RTO financing: one in five survey respondents noted that they had made a RTO purchase.<sup>20</sup>

#### KEY ISSUES:

- High interest rates and added fees
- Unfair and unreasonable practices: selling above the standard retail price, and representing used products as new
- Willingness to lend to vulnerable consumers, and high default rates as a result
- Inadequate cost disclosure in both advertising materials and agreement terms
- Potential for negative equity

## MARGARET

Margaret explained to Momentum that she needed a washer and dryer for her family, as taking laundry for four people on transit was difficult. She went to a rent-to-own store for a washer and dryer, which she found at a cost of \$1,199. Her contract included a \$25 administration fee, as well as a \$12.34/month optional insurance policy fee that she did not know was optional. Her total cost was calculated at \$99.34/month, or \$1,688 over 17 months. Margaret was not able to keep up with payments, and eventually had to return the washer and dryer. She didn't receive any of the money back, which left her in worse financial health and with the same problem she had in the first place: carrying laundry for four people on public transit.

15. Option Consommateurs, "Rent-to-own": portrait of an industry and its clientele (Montréal: 2008), 7, [http://option-consommateurs.org/documents/principal/en/File/oc\\_easyhome\\_execsum\\_200808.pdf](http://option-consommateurs.org/documents/principal/en/File/oc_easyhome_execsum_200808.pdf).  
16. Denise Barrett Consulting, *Consumer Experiences with Rent-to-Own*, 48.  
17. Ibid, 19.  
18. See CBC Marketplace, "Busted: Easyhome," CBC News video, <http://www.cbc.ca/marketplace/m/episodes/2010-episodes/busted-easyhome>.  
19. Holly Moore, "Rent-to-own practices in Canada would be illegal in parts of the U.S.," CBC News, November 26, 2014, <http://www.cbc.ca/news/canada/manitoba/rent-to-own-practices-in-canada-would-be-illegal-in-parts-of-u-s-1.2850023>.  
20. Fantauzzi, *Predatory Lending*, 9.

## 2. High-cost instalment loans

As municipal and provincial payday lending laws have tightened, lenders like Money Mart have shifted their marketing tactics and now mainly promote instalment loans. Instalment loans are long-term personal loans that can be paid back over a period lasting up to 60 months, and typically range from \$500 to \$15,000.

Like other high-cost alternative financial services, instalment loans are marketed as a simple and fast way to obtain money, particularly for those with poor credit scores and limited access to bank loans. For example, marketing slogans state “We say yes when banks aren’t an option,” or note that they “specialize in long term loans for bad credit.” One factor distinguishing some instalment loan providers from other high-cost lenders is that they report to the credit bureau. In fact, Easyfinancial and Cashco present their instalment and flex loans as a way to rebuild a poor credit score or establish credit in Canada. However, what appears to be a benefit at first glance may actually be a risky undertaking for many vulnerable consumers. This is because the potential for further harm to a credit score is high, particularly given low loan qualification standards. Though default rates for the industry as a whole are unknown, roughly 15 per cent of Easyfinancial’s consumer loans go bad – a high rate when considering soured loans at large Canadian banks account for less than 0.4 per cent of overall retail loans.<sup>21</sup>



Interest rates on instalment loans are not as steep as those associated with payday loans; however, instalment loan contracts still subject borrowers to high rates near or in excess of the Criminal Code maximum.<sup>22</sup> For example, Easyfinancial offers a \$1000 loan for a bi-weekly payment of \$57.39 over 12 months, which translates to \$1492.14 for a \$1000 loan. Instalment loan contracts can also include poorly-disclosed additional fees and insurance products, such as loan protection and benefits. Often accepted by borrowers who are unaware that they are optional, these add-ons further increase the cost of borrowing.<sup>23</sup> Moreover, borrowers are often encouraged to get another loan after paying one off, to extend the term of an existing loan, or to take out a larger loan than originally desired. As was the case with payday loans, borrowers have spoken out about their negative experiences with instalment loans, often citing hidden fees and near-inescapable debt cycles.<sup>24</sup>

21. Doug Alexander, “This lender’s stock is beating the banks by luring borrowers they turn away,” *The Globe and Mail*, November 15, 2016, <http://www.theglobeandmail.com/globe-investor/investment-ideas/goeasy-beats-banks-by-tapping-borrowers-they-turn-away/article32851257/>.

22. For example, as of April 2017 Money Mart listed an APR of 59.9 per cent, Cash Money noted a fixed APR of 46.93 per cent, Easyfinancial provided a range of 29.99 per cent - 46.96 per cent, and Cashco listed an APR of 48.99 per cent.

23. Cash Money displays a list of common instalment loans on its website. For a \$5,000 loan with a term of 40 months and an APR of 46.93 per cent, the borrower is required to make a monthly payment of \$337.29. This payment is based on the inclusion of a loan protection fee. Without the inclusion of the fee, monthly payments based on the same APR are roughly \$232, suggesting that the borrower pays an exorbitant \$100+ for insurance each month in addition to the cost of the loan. See: <https://www.cashmoney.ca/rates-and-terms/alberta/>. Accessed May 29, 2017.

24. Sunny Freeman, “Borrow \$10,000, Owe \$25,000: The Face Of Predatory Lending In Canada,” *The Huffington Post*, July 31, 2015, [http://www.huffingtonpost.ca/2015/07/31/predatory-lending-canada\\_n\\_7898598.html](http://www.huffingtonpost.ca/2015/07/31/predatory-lending-canada_n_7898598.html).

According to the credit monitoring company Equifax, high-cost instalment loans now represent the second-fastest-growing type of debt in Canada after experiencing a 7.7 per cent increase in 2016,<sup>25</sup> and account for \$132 billion dollars owed.<sup>26</sup> The growth of Easyfinancial, a subsidiary of Goeasy Ltd. (also the parent company of Easyhome), illustrates well the increasing prevalence of instalment lending. Goeasy Ltd., which now operates over 200 Easyfinancial locations and 180 Easyhome stores across Canada, and whose shares gained 21 per cent in 2016 outperforming almost all mainstream lenders in Canada, has plans to further increase loan business to \$500 million by 2018.<sup>27</sup>

#### **KEY ISSUES:**

- High interest rates and added fees.
- Willingness to lend to vulnerable consumers, and high default rates as a result
- Inadequate cost disclosure in both advertising materials and agreement terms
- High instance of roll-over and/or extended-term loans
- Growing prevalence
- Unfair and unreasonable practices: aggressive marketing and direct soliciting to reborrow, borrow more and sign up friends and family

## MARIA

Maria borrowed \$3000 from an instalment lender to cover moving expenses for a family member who had been hurt in an accident and had just sold their house. The annual interest rate on the loan was 59.9 per cent, which translated to a cost of borrowing of \$1024.52 over 12 months. Maria was able to pay off the loan gradually by prioritizing payments, and wishes to never borrow again. However, the lender often sends advertisements in the mail and calls frequently to promote additional loans.

### **3. Pawn loans**

Pawn loans are short-term loans offered to a borrower in exchange for personal property such as jewelry, electronics or equipment, which acts as collateral. When an item is pawned, the broker and the borrower enters into a contractual relationship for a fixed period of time – often 30 days – after which the borrower may redeem the item by repaying the loan plus interest. If the borrower is unable to buy back the item within the established time period, they are often given the option of extending the term of the loan by another 30 days. In such situations the cost of borrowing increases. If an individual chooses not to repay the loan, the pawned item will be offered for sale to other customers. Pawnbrokers also display for sale items that have been sold to them outright.

25. Pete Evans, "Canadians' average debt load now up to \$22,081, 3.6% rise since last year," *CBC News*, December 7, 2016, <http://www.cbc.ca/news/business/equifax-debt-loads-1.3884993>.

26. Aaron Saltzman, "CBC Investigation: Instalment loans the new high-interest danger for consumers," *CBC News*, February 27, 2015, <http://www.cbc.ca/news/business/instalment-loans-the-new-high-interest-danger-for-consumers-1.2971067>.

27. Alexander, "This lender's stock is beating the banks by luring borrowers they turn away."

One pawnbroker that operates across Canada discloses a cost of borrowing of \$30 per \$100: five per cent interest plus a 25 per cent storage fee,<sup>28</sup> and a pawn ticket from Quik Cash Pawn Shop lists an interest rate of 60 per cent. Common complaints raised by recipients of pawn loans include unreasonable conditions, such as having to buy back at the same time all items pawned on the same ticket, undervaluing of goods like jewelry and a high likelihood of not being able to buy back a pawned item. Pawn loan repayment rates are not well-documented; however, Pawn Princess in Edmonton reports that 82 per cent of customers redeem their ring or other pawned item within a month.<sup>29</sup>

#### **KEY ISSUES:**

- High interest rates
- Willingness to lend to vulnerable consumers, and high default rates as a result
- Unfair and unreasonable conditions: strict buy-back conditions and undervaluing of items
- Potential for negative equity

## FRANCIS

Francis pawned a 50 inch television to cover the cost of a payday loan. The value of the loan was \$150, and was provided at a cost of 30 per cent (\$45) for the 30 day period. These same costs, if charged every month for a year, work out to an annual interest rate of 360 per cent. Francis had to keep borrowing for several months, and eventually lost the television (and all the payments he had made). He has also pawned and lost a laptop and jewelry of sentimental value.

#### **4. Cheque cashing**

Many high-cost alternative lenders that provide payday and instalment loans also offer cheque cashing and other basic banking services. Cheque cashing services allow individuals to cash cheques immediately without the account holds and waiting periods – usually three to five days – often imposed by mainstream financial institutions. In addition, cheque cashing businesses boast convenient hours, and do not always require an individual to provide the same personal identification and banking information as at a traditional bank. Costs at cheque cashing outlets combine a flat item or transaction charge with a fee based on a percentage of the cheque cashed: for example, \$2.99 per item plus a rate of 2.99 per cent of the cheque.<sup>30</sup>

At some cheque cashers and other high-cost lenders funds can be loaded directly onto a prepaid, reloadable MasterCard, a product that is growing in popularity. As indicated in a 2016 Money Mart press release, the Titanium+ Prepaid MasterCard has a 90 per cent reload rate.<sup>31</sup> Though this service provides many individuals access to a credit card, numerous fees are charged to use it, including a \$6.50 monthly fee, a \$0.50 fee per transaction, a \$1.99 withdrawal fee and a \$2.99 loading fee, among others.<sup>32</sup>

#### **KEY ISSUE:**

- High fees

28. Cash Canada, "Pawn Loans in Canada," Cash Canada, accessed May 26, 2017, <http://www.cashcanada.com/pawn-buy-sell/pawn-loans>.

29. Elise Stolte, "Pawn Princess tries to bring empathy to Edmonton pawn shop debate," *Edmonton Sun*, April 19, 2017, <http://www.edmontonsun.com/2017/04/19/edmonton-debates-new-limits-on-local-pawn-shops>.

30. Rates offered in Alberta include: a 2 per cent flat fee (Equity Cash); 2.99 per cent plus \$2.99 (Speedy Cash); 3.00 per cent plus a \$2.99 item fee (Money Mart); 2.9 per cent plus a \$3.95 loading fee (Cashco); and 3.5 per cent (Cash Canada).

31. Money Mart, "Money Mart Recognized for Best Consumer Funded Prepaid Program at 2016 PX Payments Awards," press release, April 28, 2016, [https://www.moneymart.ca/Content\\_1.0.0.0/themes/press-release.pdf](https://www.moneymart.ca/Content_1.0.0.0/themes/press-release.pdf).

32. Nextwave Titanium+ Prepaid MasterCard®, "Titanium+® Prepaid Mastercard® Cardholder Agreement," accessed May 26, 2017, <https://www.mytitanium.ca/signup/signup>.

## 5. Title loans

Title loans are high-interest loans that are secured against a borrower's vehicle, and in some cases their boat, recreational vehicle or heavy-duty equipment. A way to receive fast access to a loan with few eligibility requirements, a title loan is granted without a borrower having to provide credit history or proof of income; individuals qualify for loan amounts based on the value of the asset rather than their ability to repay. Contract lengths range from 30 days to five years, and loan amounts are typically between \$1,000 and \$50,000 depending on the value of the asset. In the United States, title loans have taken the place of other high-cost loans, particularly in states that have enacted strict or prohibitory payday lending regulations.<sup>33</sup>

Like similar high-cost financial services, title loans are advertised as a way to gain fast and simple access to money. Product marketing reflects the ease with which such loans are granted, and includes statements like "Borrow from \$1,000 to \$50,000 instantly,"<sup>34</sup> "Instantly Borrow The Money You Need Today – No Limits, No Credit Checks and No Delay!"<sup>35</sup> and "At Alberta Car Title Loans, your loan request will never be turned down."<sup>36</sup> Title lenders target individuals with poor credit ("Good, poor, or bad credit? No problem! [...] We don't do credit checks"),<sup>37</sup> the unemployed ("Are you a victim of declining oil & gas products? Recently laid off? In between jobs?"),<sup>38</sup> and newcomers ("not a Canadian citizen or permanent resident? The Loan King does not deal with credit bureaus or credit companies.")<sup>39</sup>

Interest rates listed by title lenders operating in Alberta range from 27 per cent<sup>40</sup> to 60 per cent.<sup>41</sup> However, these rates do not include mandatory setup fees and checks, which can amount to as much as \$500<sup>42</sup> for anything from vehicle monitoring, storage, and documentation, to lien searches and auto checks. In the case of late and partial payments, daily interest charges are applied. These additional fees add up to APRs that can exceed the maximum rate set out in the Criminal Code.

Since the nature of title lending is such that the borrower offers their vehicle as collateral, individuals are faced with the possibility of losing a primary asset if they cannot repay the loan. In Canada, individuals have reported their vehicle being seized despite having made loan payments totalling more than four times the principal.<sup>43</sup> Not only does a borrower lose their vehicle once it is seized, they may also lose all equity in it regardless of the amount owed. Given the possibility of repossession, borrowers are inclined to renew loans; in fact, the American Consumer Financial Protection Bureau (CFPB) noted over half of borrowers took out at least four consecutive loans.<sup>44</sup> The result is a long-term loan for which borrowers end up paying more in interest than what is received in credit. Additionally, in some instances companies install starter interrupters which disable a car when a borrower fails to make loan payments.<sup>45</sup>

### KEY ISSUES:

- High interest rates and added fees
- Willingness to lend to vulnerable consumers, and high default and repossession rates as a result
- Inadequate cost disclosure in both advertising materials and agreement terms
- High instance of roll-over and/or extended-term loans
- Potential for negative equity
- Unfair and unreasonable conditions: charging for installation of starter disrupters

33. Mehrsa Baradaran, *How the Other Half Banks: Exclusion, Exploitation, and the Threat to Democracy* (Cambridge, MA: Harvard University Press, 2015), 113.

34. Snap Car Cash, "Personal Title Loans," accessed May 29, 2017, <http://www.snapcarchash.com/area-served/car-title-loans-alberta/>.

35. Mr. Good Loans, accessed May 29, 2017, <http://www.mrgoodloans.com/>.

36. Pit Stop Loans, "Alberta Car Title Loans," accessed May 30, 2017, <http://www.pitstoploans.com/alberta-car-title-loans>.

37. Snap Car Cash, "Why Choose Snap Car Cash," accessed May 30, 2017, <http://www.snapcarchash.com/>.

38. Mr. Good Loans, accessed May 30, 2017, <http://www.mrgoodloans.com/>.

39. The Loan King

40. Direct Car Loans, "Our Advantages," accessed May 26, 2017, [www.directcarloans.ca](http://www.directcarloans.ca).

41. Fast Cash Auto Solutions, "Canada's Fastest Title Loans," accessed May 26, 2017, <http://raifinance.com/>.

42. Ibid.

43. Canada. Industry Canada. Consumer Measures Committee, *Stakeholder Consultation Document on a Proposed Consumer Protection Framework for the Alternative Consumer Credit Market* (Ottawa, ON: 2004), 7, [https://www.ic.gc.ca/eic/site/cmc-cmc.nsf/vwapj/accm.pdf/\\$FILE/accm.pdf](https://www.ic.gc.ca/eic/site/cmc-cmc.nsf/vwapj/accm.pdf/$FILE/accm.pdf).

44. United States. Consumer Financial Protection Bureau, *Single-Payment Vehicle Title Lending* (Washington, D.C.: 2016), 4, [http://files.consumerfinance.gov/f/documents/201605\\_cfpb\\_single-payment-vehicle-title-lending.pdf](http://files.consumerfinance.gov/f/documents/201605_cfpb_single-payment-vehicle-title-lending.pdf).

45. Craig Desson, "Auto Lenders Quietly Install a Digital Repo Man," *The Toronto Star*, January 14, 2015, [https://www.thestar.com/business/2015/01/14/auto\\_lenders\\_quietly\\_install\\_a\\_digital\\_repomani.html](https://www.thestar.com/business/2015/01/14/auto_lenders_quietly_install_a_digital_repomani.html).

## 6. Auto loans

Auto loans are available through a dealership or separate company to finance the purchase of a vehicle. Offered at a higher interest rate to people who do not qualify for a bank auto loan due to a low credit score, sub-prime auto loans pose a significant risk to an individual's financial wellbeing. These loans are growing in popularity, despite high default rates relative to traditional car loans.

Extended term loans are also on the rise, and present additional risks. These loans have grown from shorter terms of 48 months to terms of as many as 96 months, and are typically associated with new vehicles. The extended term draws out payments, thereby lowering the weekly or monthly costs, but significantly increases the overall cost of borrowing given the duration of payments. The principal is paid down so gradually that the borrower may be left owing more on the vehicle than what it is actually worth. Canadian data from J.D. Power and Associates shows that in 2008 34 per cent of all new car finance deals were 72 months or longer, versus 64 per cent in 2013. Occasionally, an incomplete auto loan (there is still money owing) is incorporated in a new credit agreement when the first vehicle is traded in. When an old loan is rolled into a larger loan the buyer is placed in a position of negative equity, ultimately owing more than the vehicle is worth.

Consumers report that lenders often inflate vehicle prices, and frequently employ aggressive sales techniques for add-on products such as rust protection, undercoating, fabric protection and various forms of insurance. Some buyers also complain of mandatory fees (around \$600) for start-disabler devices, so that if they miss too many payments the dealer can repossess the vehicle. Car repossession rates of finance companies, as opposed to those of banks and credit unions, recently rose by 69.1 per cent.<sup>46</sup>

High-cost, non-traditional auto financing has made car ownership more accessible for some; however, others would argue that this type of lending results in huge costs for those who cannot afford the car in the first place.<sup>47</sup>

### **KEY ISSUES:**

- High interest rates and added fees
- High instance of extended-term loans
- Willingness to lend to vulnerable consumers, and high default rates as a result
- Inadequate cost disclosure in both advertising materials and agreement terms
- Unfair and unreasonable practices and conditions: charging for the installation of starter disrupters and inflated vehicle prices
- Potential for negative equity

## LEILA

Leila sought out an auto loan for a 2015 Ford Focus so that she could travel to her new job. The cost of the vehicle was \$17,000. In addition to paying back this amount, Leila paid 28.8 per cent in interest, as well as \$299 for an administration fee, \$599 for an auto-tracker, \$985 in lender and referral fees, and \$25/month in optional insurance fees. This amounted to a cost of borrowing of more than \$17,000, which Leila had to pay on top of the \$17,000 it cost her to buy the vehicle. Leila was not able to keep up with payments. She says she paid more than \$10,000 over the course of the first year, until she was laid off. After two months of non-payment the lender disabled the car in her driveway, eventually repossessed it and sent her a final invoice. She says she wishes she had never gotten the loan in the first place.

46. Melinda Zabritski, "State of the Automotive Finance Market, First Quarter 2014," (presentation, Experian Information Solutions, Inc., 2014), 16, <http://www.rsig.com/2014seminar/Experian.pdf>.  
47. Ibid.

## THE IMPACT OF HIGH-COST ALTERNATIVE FINANCIAL SERVICES

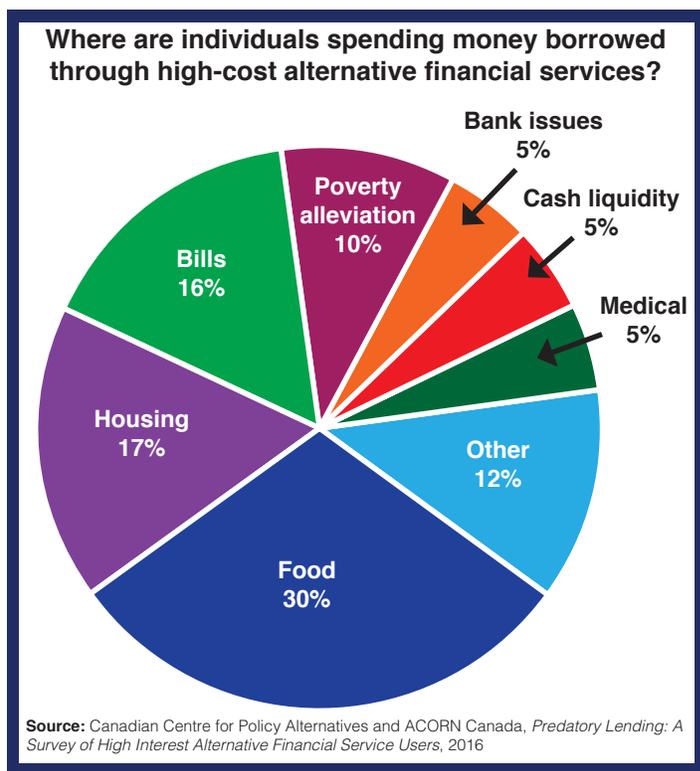
Recent changes to Alberta's payday lending rules are promising and can be built upon. It remains to be seen how the high-cost alternative financial services market will evolve in Alberta, particularly given the introduction of more restrictive payday lending legislation; however, what is clear is that existing products will continue to negatively impact both individuals and the communities they live in. These effects are explored below.

### Individual and household impact

The high-cost alternative lenders analyzed in this report target low-income individuals, recent immigrants who have not yet established credit history in Canada, unemployed individuals or those who have recently been laid off and people who are generally strapped for cash. Individuals within this target population often struggle to afford items outright or to cover unexpected expenses, encounter barriers to securing credit with mainstream financial institutions and generally experience financial exclusion.<sup>48</sup> This means that in many cases, high-cost alternative lenders are their only option. Ultimately, those who can least afford it must pay the most to access short-term credit, and are often forced to accept exorbitant rates that verge on, and in some cases, are illegal.

The default, roll-over and repossession rates of these alternative loans are high, and one high-cost loan, on its own, is capable of trapping a vulnerable borrower in a cycle of debt. Of even greater concern, however, is the potential for individuals to borrow multiple products at once. In community consultations and during one-on-one interviews, Momentum heard numerous stories of individuals and families resorting to a second or third loan so that they could meet payments for an initial loan. One participant reported having to pawn an item purchased at a RTO store to feed her family. Already unable to cover basic expenses for the month, she is now scrambling to keep up with payments on the RTO item and to save enough money to buy it back from the pawn shop.

A lack of safe and affordable financial products available to families like the one described above results in the entrenchment of what some call the two-tiered banking system, in which the poor pay much more for far inferior services. Financial exclusion is only exacerbated by this two-tiered system. It also plays a role in perpetuating cycles of poverty, in which individuals are unable to secure neither the income nor the assets necessary to thrive in the long-term. There are also significant health impacts of financial exclusion. Drowning in debt and worrying about repaying a loan is extremely stressful, both for borrowers and their families, and chronic stress – particularly financial stress – has profoundly negative effects on physical and mental health.<sup>49</sup>



48. See Jerry Buckland, *Hard Choices: Financial Exclusion, Fringe Banks, and Poverty in Urban Canada* (Toronto: University of Toronto Press, 2012).

49. Mamie Purciel-Hill et al., *Drowning in Debt: A Health Impact Assessment of How Payday Loan Reforms Improve the Health of Minnesota's Most Vulnerable* (Oakland, CA: Human Impact Partners, 2016), 4, [http://www.humanimpact.org/wp-content/uploads/PaydayLendingHIA\\_FinalReport.pdf](http://www.humanimpact.org/wp-content/uploads/PaydayLendingHIA_FinalReport.pdf).

## Impact on low-income communities and local economies

Financial exclusion is a major contributor to economic leakages from not only low-income households,<sup>50</sup> but communities as well. For example, findings conclude that the presence of payday lenders in a community increase the area's risk of poverty and disinvestment.<sup>51</sup> This is because wealth is stripped from lower-income households, diminishing their capacity to support local businesses.<sup>52</sup> Money that could have been spent by individuals and households on goods and services in the community instead goes to service astronomical debt costs.<sup>53</sup>

In the words of a resident of Calgary's Greater Forest Lawn area, the clustering of high-cost alternative financial services in lower-income neighbourhoods has a significant impact on how the community is perceived. The presence of these businesses reinforces narratives about the area (as undesirable to live or start a business, dangerous, crime-ridden, poor, etc.), and greatly limits the community's ability to present an alternative, positive narrative. The resulting economic impacts cannot be ignored. When high-cost lenders cluster in neighbourhoods with higher poverty rates, they drive away more desirable businesses, prevent those that do exist from thriving, and erode investment in the area.

## ISSUES AND IMPACT IN SUMMARY

### 1. High cost

- High interest rates, added fees and lengthy loan terms result in borrowers paying prices that most consumers would find shocking. In some cases, interest rates exceed the Criminal Code maximum of 60 per cent.
- For many, these loans are difficult to pay off. They can easily trap a borrower in a cycle of debt, and often force borrowers to extend a loan's term or obtain an additional loan from a different lender.
- RTO businesses routinely charge two to three times, and in some cases more than four times, the retail price of products. Consumers make similar complaints regarding sub-prime, extended-term auto loans.

### 2. Inadequate disclosure

- In most cases, providers of high-cost alternative financial services do not communicate the total cost of borrowing clearly. For example, rather than disclosing fees and add-ons upfront, lenders often bury such information in lengthy loan contracts.
- Optional fees are not always presented as such, which results in borrowers signing up for expensive add-ons without realizing they are able to opt out. Insurance is often included automatically, though it is optional. RTO businesses often present home delivery as a free service when there is actually a charge.

### 3. Unfair and unreasonable practices

- Borrowers report a significant amount of direct soliciting to re-borrow, borrow more and sign up friends and family, particularly over the telephone.
- Conditions on pawn loans make it difficult for a borrower to buy back a pawned item.
- Charges are applied for the installation of starter disablers.
- Inaccurate product valuation: pawn shops undervalue items they received, while RTO stores and auto lenders routinely inflate the price.
- Used products are represented as new at RTO businesses.

50. Buckland, *Hard Choices*.

51. Charis E. Kubrin et al., "Does fringe banking exacerbate neighborhood crime rates?," *Criminology & Public Policy*, 10, no. 2 (2011): 437–466.

52. Haydar Kurban, Adji Fatou Diagne, and Charlotte Otabor, *The Economic Impact of Payday Lending in Economically Vulnerable Communities* (Washington, D.C.: Howard University Center on Race and Wealth, 2014), <http://coas.howard.edu/centeronraceandwealth/reports&publications/1214-the-economic-impact-of-payday-lending-in-economically-vulnerable-communities.pdf>.

53. Jerry Buckland, Blair Hamilton, and Brendan Reimer, "Fringe Financial Services, Inner-city Banking & Community-based Solutions," *Canadian Journal of Urban Research*, 15, no. 1 (2006): 109–128.

#### 4. Willingness to lend to vulnerable borrowers

- To account for the risk involved in lending to individuals with poor credit, lenders increase interest rates and other borrowing costs to exorbitant levels. The result is that those who have no other option –often the most financially vulnerable – pay the most to borrow even small amounts of money.
- Many lenders accept social assistance and Employment Insurance cheques, as well as Canada Pension Plan and disability insurance, as proof of income. These examples suggest a fixed income, meaning that if an individual currently needs a loan they are unlikely to have the money to repay it next month.
- For some individuals a loan is not a good idea; however, high-cost lenders make a profit by lending to people who may be better served through basic needs assistance, credit counselling, debt consolidation or other community supports.
- Delinquencies and late payments are costly for borrowers, who end up having to pay additional fees and often see their assets - and equity in those assets - repossessed.

#### 5. Economic leakage

- The real impact of high-cost alternative financial services is in the reinforcement of the two-tiered banking system, and in the depletion capital from low-income households and communities, both of which contribute to economic inequality.<sup>54</sup> Not only are such businesses detrimental to the financial, mental and physical well-being of residents, they also detract from efforts to alleviate poverty in lower-income areas. When high-cost lenders cluster in neighbourhoods with higher poverty rates, they drive away more desirable businesses or prevent those that do exist from thriving.

### CONCLUDING THOUGHTS

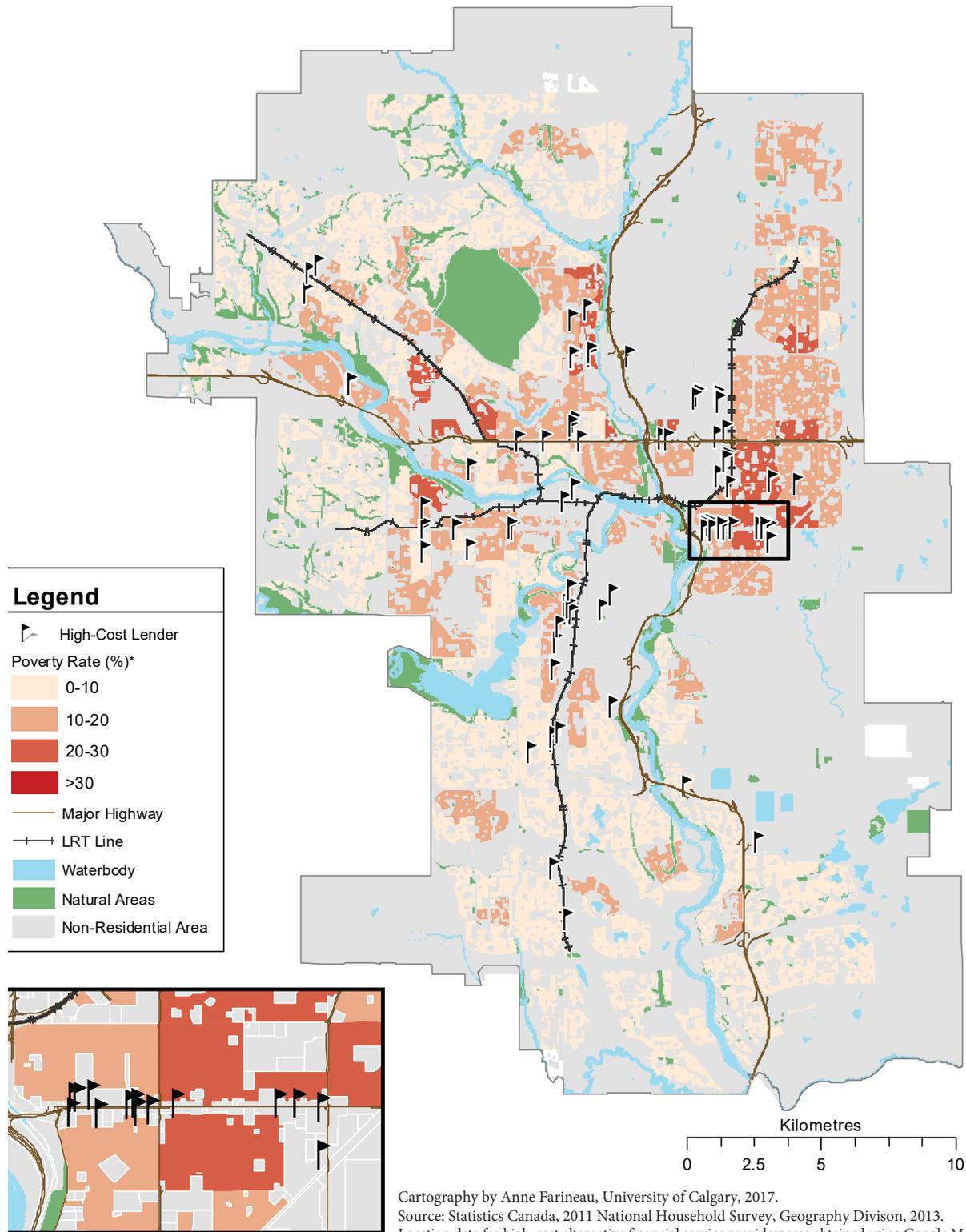
Many Albertans use high-cost alternative financial services as short-term fixes for serious financial issues. Though it is difficult to imagine a riskier solution to a financial shortfall, these products are often the only option for those who struggle to secure credit through a mainstream financial institution. The impact of these costly products on individuals, families, and communities – particularly in the absence of safe and affordable alternatives – cannot be ignored, and merits the consideration of government, mainstream financial institutions, communities, and consumers alike. The analysis presented in this report exposes several areas for reform, including cost of borrowing limits and cost disclosure standards. These and other recommendations will be explored in depth in a forthcoming paper, entitled High-cost Alternative Financial Services: Policy Recommendations.

This document is part of a series on high-cost alternative financial services. For more of Momentum's publications, visit [www.momentum.org/publications](http://www.momentum.org/publications).

54. Purciel-Hill et al., *Drowning in Debt*, page 5.

## Appendix A

# Calgary Poverty Levels and Location of High-Cost Lenders



1. The high-cost lenders identified on this map are high-cost alternative financial service providers operating in Calgary that exist outside of the mainstream banking system. They include rent-to-own businesses, pawn shops, instalment lenders and title lenders. Auto loan businesses are not represented, nor are stand-alone payday lenders. These lenders charge high interest rates relative to mainstream financial institutions: in some cases interest rates meet or exceed the 60 per cent maximum outlined in the Criminal Code of Canada.
2. Poverty rates were measured using the low-income measure after tax (LIM-AT). According to the LIM-AT, the poverty line for a single individual is \$19,460.