NCLC National Consumer Law Center

After Payday Loans: Consumers Find Better Ways to Cope with Financial Challenges

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Payday lenders and high-cost installment lenders offer fast cash loans that do far more harm than good, adding to rather than alleviating financial distress. As a growing number of states have curtailed high-cost lending, experience shows that people are better off and find better options.

High-cost lenders, charging rates of 99% APR or higher, rely on their ability to collect payments rather than borrowers' ability to repay while meeting other expenses. Eighteen states and the District of Columbia effectively cap the costs of payday and other short-term loans,[1] and 32 states plus DC impose a rate cap of 36% or less on a $2,000, two-year installment loan.[2]

The American public, on a bipartisan basis, strongly supports capping interest rates at 36% or lower. Voters in several states have overwhelmingly supported rate caps whenever given a chance to vote on an initiative.[3] Polling has also consistently shown strong, bipartisan support for a 36% rate cap.[4]

But the question often arises: Once a state limits interest rates, what is the impact on consumers? In state after state, the impact is clear: consumers are better off and find better ways to cope with financial challenges:

- Former borrowers generally agree that they are better off without payday loans and express relief that the loans are no longer available.
- People use a variety of strategies to manage their finances, including borrowing from family and friends, negotiating payment plans with utility companies, and using pawn shops or traditional credit products like credit cards.
- Eliminating high-cost loans spurs an increase in affordable loans like credit union loans and more attention on other safer alternatives.
- Consumers do not turn to illegal internet loans in large numbers.

The solution to a financial challenge is not to create a financial disaster by charging a consumer triple digit interest, adding more debt they cannot afford to repay, or trapping them in a cycle of debt. There is no easy answer to a lack of money, but in states that restrict high-cost loans, consumers have successfully deployed strategies that are less destructive than triple-digit interest loans. Of course, if consumer protection laws have gaps or allow other predatory products to remain, lenders may attempt to exploit those loopholes. But other problems in the financial marketplace should not stop policymakers from tackling loans that do more harm than good.

This issue brief focuses what happened in states that previously allowed high-cost lending and then adopted or enforced an interest rate cap of 36% or less.[5] Other research has also shown that consumers are better off in states that have never allowed payday lending.[6]

Arkansas

Payday Free: 2008[7]; Restriction: 17% annual interest rate[8] *Estimated Annual Payday Fee Savings*: $77,504,338[9]

- **Arkansas Supreme Court Upholds Constitutional Usury Limits:** The Arkansas Constitution caps interest rates at 17%, but the legislature passed a law attempting to carve out an exception for short-term payday loans with rates exceeding 300%. In 2008, the Arkansas Supreme Court found the law was unconstitutional and all payday stores were closed by 2009.[10]
- **Arkansans Better Off Without Payday:** Most respondents to a Southern Bancorp survey of 100 former payday borrowers (59%) who had lodged complaints with AARP and/or the Attorney General's office indicated that they were better off after payday was banned. Borrowers reported that the ease and availability of the loans was ultimately what made payday loans attractive, but that the accompanying debt trap caused stress and anguish along with a ripple effect of ancillary hardships and financial distress with other vendors, companies, service providers, etc. One respondent noted: *"I found that I really could do without them. I work terms with my creditors. They are willing to accept something from you. I have actually paid off debts by a little at a time. I keep more money in the home and not having to pay back loans that triple the amount borrowed."*[11]
- **Borrowers in Arkansas Adapt to Less Risky Credit Sources:** Respondents to the survey indicated a wide range of alternatives to payday loans they had used after payday loans were banned. The three most popular alternatives were: Friend/Family Loan (36), Credit cards (21), Pawn Shops (19).[12]
- **Consumers Did Not Generally Turn to Illegal Internet or Border State Loans:** Southern Bancorp also conducted a survey of credit counselors (fourteen counselors responded, seven of whom had been counselors since at least 2008). The survey found that clients had more payday loans in 2008 than in 2014, suggesting that use declined after the ban despite the availability of internet and border state payday loans.
- **Overall Debt Load Remains Stable:** The credit counselors surveyed also reported that the overall debt load for consumers in 2014 compared to 2008 "remained the same or increased somewhat." The studies' authors suggested that a number of factors prevented debt loads from declining, including failure of income to track the cost of living, as well as the mortgage crisis and recession in the years following the 2009 ban of payday. [13]

Georgia

Payday Free: 2004; Restriction: Payday loans are banned[14] *Estimated Annual Payday Fee Savings*: $284,112,449[15]

- **Georgia Lawmakers Impose Criminal Penalties on Payday Lenders:** While payday lending was effectively restricted by the Georgia Industrial Loan Act of 1955, which required licensing and imposed rate caps,[16] the Georgia Assembly determined that rent-a-bank arrangements were being used to circumvent restrictions on payday lending[17].
- In 2004, the Georgia legislature passed the Payday Lending Act of 2004 which, among other things explicitly banned rent-a-bank arrangements,[18] prohibited loans of less than $3,000 that did not comport with existing law (including those relating to interest and usury)[19] and established penalties of 1 year in prison, a fine not to exceed $5,000, or both.[20]

- **Involuntary Bank Account Closures in Georgia Declined After Payday Ban:** Relative to counties in bordering states, a 2012 study found that, after the payday loan ban, Georgia counties within 60 miles of a state border experienced an over 9% decline in the mean rate of bank account closures, and counties more than 60 miles from a border (during the study period all bordering states allowed payday lending)[21] experienced an over 30% decline in the mean bank account closure rate.[22] Study authors found that this decline was "consistent with the "debt trap" critique of payday lending where the practice leads to increased rates of involuntary bank account closure."[23]
- **Work Remains to Eliminate other Predatory Loans:** A recent study found that car title lenders, who can still charge interest rates as high as 300%, had 755 locations in Georgia in 2018 with over 74% of them in areas with a poverty rate above the national average.[24]

Illinois

Payday Free: 2021; *Restriction*: 36% annual interest[25] *Estimated Annual Payday Fee Savings*: Estimate not yet complete

- **From 20% Interest to 297% Interest:** Prior to 1985, it was a felony in Illinois to make a loan at an interest rate over 20%, but in 2019, the average APR on a payday loan in Illinois was 297%.[26]
- **Broad Support for Ending High-Cost Lending in Illinois:** The Predatory Loan Prevention Act was introduced as part of the anti-racism agenda of the Illinois Legislative Black Caucus Agenda. The law caps the interest rate of consumer loans at 36%, calculated including all fees and credit insurance consistent with the rules under the Military Lending Act. Over 100 individuals and organizations encompassing state and local government, clergy, industry lenders and advocates pushed to end that predatory practice.[27] The bill, passed by large margins—110-0 (two voting present) in the House, and 39-5 in the Senate with bipartisan support.[28]
- **Affordable Alternatives Guide:** Passage of the bill spurred development of a guide pointing consumers to safe and affordable alternatives to high-cost loans. The guide includes resources to help consumers negotiate with creditors, and where to access low APR credit options.[29]
- **Increased Demand for Affordable Alternatives:** Within days of the law going into effect, a Community Development Financial Institution (CDFI) whose average interest rate is 13% saw a 70% increase in applications, with a similar increase in loan closings.[30] The CDFI also found that the cost of publicizing their low-cost loans decreased after the law passed, as there were fewer high-cost lenders bidding on keywords used in search engines.[31]

Montana

Payday Free: 2010; *Restriction*: 36% annual interest[32] *Estimated Annual Payday Fee Savings*: $20,750,969[33]

- **Montanans Overwhelmingly Vote to End Payday:** A 2010 ballot measure, approved by 73% of those voting, created a 36% interest rate cap for loans that had previously been as high as 500%.[34]
- **Usage of Low-Cost Credit Union Loans Increases:** During the campaign for the interest rate cap in Montana, Montana Credit Unions for Community Development launched a campaign to make people aware that credit unions offer better alternatives to payday loans.

Twelve credit unions tracked Payday Alternative Loan use during and after the campaign and found an over 24% increase in usage for July through September 2010, and an over 26% increase for October through December 2010.[35]

- **After a Temporary Adjustment, Consumers Avoid Online Lenders:** Complaints to the Attorney General about online payday lenders temporarily spiked after the interest rate cap went into effect, with 103 complaints in 2013. But this was likely a temporary adjustment period for consumers who were looking for ways to roll over unaffordable payday loans. Complaints later plummeted, and in 2016 there were only seven complaints against payday lenders.[36] This adjustment period seems to confirm previous research that determined that rates of online payday borrowing were not significantly higher in states with no storefront payday lenders (1.58%) than in states that allow payday lending at triple digit rates (1.37%).[37]

Nebraska

Payday Free: 2020[38]; *Restriction*: 36% annual interest[39] *Estimated Annual Payday Fee Savings*: Estimate not yet complete

- **Broad Support for Ending Payday in Nebraska:** An overwhelming 82.8% of those voting in November 2020 voted in favor of Nebraska Initiative 428, the ballot initiative that created the 36% interest rate cap.[40]
- *** Early results promising.** No data is yet available on the impact of Nebraska's new rate cap, but early indicators show a smooth transition.

New Hampshire

Payday Free: 2009; *Restriction*: 36% annual interest[41] *Estimated Annual Payday Fee Savings*: $27,390,363[42]

- **NH Legislature Finds Payday Interest Unreasonable and Predatory:** New Hampshire (NH) had a small loan interest rate ceiling until it was removed in January 2000.[43] However, in 2008 (law effective 2009) the New Hampshire legislature found that “the rates of interest charged by many title loan lenders and payday lenders are unreasonable and predatory” and capped the annual percentage rates at 36%.[44]
- **New Hampshire Former Payday Borrowers Are “Glad They’re Gone:”** In a focus group of 10 former NH storefront payday borrowers conducted by Pew, participants mostly expressed relief that the lenders were gone although some acknowledged they would likely use the loans again if the stores returned. Former borrower comments include:
    - *“I’m glad they’re gone. I hope they never come back.”*
    - *“I think they need to find other ways to help people out than just make it so easy to do that, because that’s why people do it.”*
    - *“They’re out, leave them out, and you know what I mean? Then you don’t have to worry about it.”*
    - *“[Now that payday lenders are gone] you can’t get stuck in it.”*[45]
- **Former Borrowers Develop New Strategies:** In a 2011 Pew survey former payday loan borrowers discussed a variety of strategies they employ now that NH is payday-free,

including “rebudgeting, prioritizing bills, pawning or selling belongings, borrowing from family members, or, as one borrower stated, working out ‘payment plans with utility companies.’”[46]

North Carolina

Payday Free: From 2001 to 2006 payday lending wound down; *Restriction*: 36% annual interest[47] *Estimated Annual Payday Fee Savings*: $255,144,890[48]

- **North Carolinian Legislators Realize Their Mistake in Authorizing Payday Loans:** From 1997 to 2001, North Carolina authorized payday loans by exempting them from usury limits. The state allowed the law authorizing payday loans to sunset in 2001, and in March 2006 the remaining payday lender chains that were operating in partnership with out of state banks entered into a consent agreement with the Attorney General and ceased to operate.[49]
- **North Carolinians Positively Impacted by Payday Ban:** In a 2007 report designed, among other things, to determine the effect the end of payday lending had on low- and middle-income households. Twice as many surveyed former payday borrowers reported that the absence of payday had a positive rather than a negative impact on their household.[50]
- **Consumers Develop New Strategies:** The 2007 report also found that the vast majority of households surveyed use a variety of options to manage shortfalls and the loss of any one option (like payday) impacted few.[51] But some borrowers were impacted by the continuing availability of other forms of predatory lending (not generally within the scope of small dollar high cost lending regulation), such as overdraft loans and EZ leases for appliances secured by postdated checks.[52]
- **Credit Unions Step In With Lower Cost Options:** In 2001, when the payday authorizing law was allowed to sunset, the State Employees’ Credit Union launched its Salary Advance Loan and Savings program (SALOS), an open-ended line of credit up to $500 with rates between 5.75% and 12.25% and no fees and a savings component.[53] The program has grown in volume from nearly 24,000 members in 2003[54] to 200,000 members who are either actively using the program or have moved their funds to a traditional savings account and exited the program in 2016.[55]
- **Other Products Supply Credit after Restriction of Payday:** After the law authorizing payday lending was allowed to sunset in 2001, the number of loans under $600 made by finance companies increased 37% in the four years from 2002 to 2006.[56] In recent years, the number of finance company loans under $600 has dropped[57] although ultimately this may be a positive shift as these loans are not without their own problems[58] and better alternatives exist.

South Dakota

Payday Free: 2016; *Restriction*: 36% annual interest[59] *Estimated Annual Payday Fee Savings*: $81,720,716[60]

- **A Long Road Back to a Rate Cap:** South Dakota was the first state to repeal its interest rate cap in 1980 (to attract credit card companies to the state) and payday lending was first codified by the legislature in the early 2000s. While predatory lenders successfully fended off efforts to regulate payday lending through legislation in the 2000s, a successful ballot initiative campaign in November 2016 instituted a 36% rate cap.[61]

- **Broad Support for Ending Payday Lending in South Dakota:** An overwhelming 75.58% of those voting supported the South Dakota Payday Lending Initiative, Initiated Measure 21.[62]
- **The Sky Doesn't Fall:** Credit remains available after the rate cap went into effect. Credit union payday alternative loans and unsecured loans increased by volume in South Dakota after the rate cap passed, and a credit union moved into a location formerly occupied by a payday lender.[63]
- **Public support for the rate cap remains high two years later.** A poll conducted in August 2018 revealed strong levels of support for keeping the rate cap in place and strong opposition to any legislative attempt to allow higher rates than those the voters' approved – including among voters who voted against the rate cap.[64]

Conclusion

In states that expel predatory lenders, consumers are relieved that those lenders are gone and adapt by seeking out alternatives and employing a variety of strategies that leave them better off. There are no easy solutions to low wages and expenses that outstrip income, but predatory lending is a disease, not the cure. When confronted with the question, "But what will people do without high-cost loans?," policymakers should feel confident that stopping predatory lending will benefit their constituents and lead them to better options.

Endnotes

[1] Arizona, Arkansas, Connecticut, Georgia, Illinois, Maryland, Massachusetts, Montana, Nebraska, New Hampshire, New Jersey, New York, North Carolina, Pennsylvania, South Dakota, Vermont, Washington D.C., West Virginia. *See* Center for Responsible Lending, Map of U.S. Payday Interest Rates. Many more states impose interest rate caps on longer term loans. *See* National Consumer Law Center, Predatory Installment Lending in the States (May 2021).

[2] National Consumer Law Center, State Rate Caps for $500 and $2,000 Loans, July 2021.

[3] *See* Nebraska Initiative 428, Payday Lender Interest Rate Cap Initiative (2020), (82.8% in favor of a 36% rate cap); Pat Ferrier, Fort Collins Coloradoan, "Colorado election: Proposition 111, capping interest on payday loans, passes" (Nov. 6, 2018) (77% of voters voted to approve a 36% rate cap); South Dakota Official Election Returns and Registration Figures, Primary Election (June 7, 2016), (76% in favor of a 36% rate cap); Matt Volz, Missoulian, Montana Voters Approve Payday Loan, Real Estate Tax Initiatives (Nov. 3 2010). (73% of Montana voters approved a 36% rate cap); Ohio Payday Lender Interest Rate Cap, Referendum 5 (2008), (63% in favor of a 28% rate cap); Arizona Payday Loan Reform, Proposition 200 (2008), (60% of voters opposed continuing an exemption from the state's rate cap). In Arizona, the payday lenders later found a loophole for auto title loans. In Ohio, the payday lenders found a loophole in the mortgage laws. The Ohio legislature later closed that loophole but allowed higher-cost loans than the voters had approved.

[4] For example, a January 2020 poll showed that 70% of voters support a 36% annual interest cap, with nearly equal levels of support among Democrats (72%), Independents (67%) and Republicans (70%). Support was consistent across the country with 64% to 73% total support

across all 50 states and DC. Morning Consult, Interest Rate Cap Polling Results (January 2020). A May 2020 poll showed even higher support for capping rates during the coronavirus crisis. *See* Lake Research Partners, New Data Shows Strong Support for Regulating High-Interest Lending (May 5, 2020).

[5] The focus of this brief is examining the impact on consumers after states cap interest rates, and it does not attempt to compile every academic paper addressing the potential impacts of payday loan bans or comparing payday free jurisdictions with states that allow payday lending.

[6] See Center for Responsible Lending, Shark-Free Waters: States are Better Off without Payday Lending (Aug. 17, 2016) (updated Sept. 2017).

[7] The Arkansas Supreme Court ruled that the law authorizing payday lending was unconstitutional in 2008, though the legality of the practice was unclear as early as 2001. Neil Bhutta, Jacob Goldin, Tatiana Homonoff, Consumer Borrowing After Payday Loan Bans, February 5, 2016, pg. 8, Fn. 9.

[8] Covington, Johnson, Southern Bancorp Community Partners, Into the Light: A Survey of Arkansas Borrowers Seven Years after State Supreme Court Bans Usurious Payday Lending Rates, at 4 (April 2016) ("Into the Light"). *See* McGhee v. Arkansas State Bd. of Collection Agencies, 289 S.W. 3d 18, 2008.

[9] Center for Responsible Lending, Shark-Free Waters: States are Better Off without Payday Lending, Pg. 9, Figure 1, (Aug. 17, 2016) (updated Sept. 2017).

[10] Into the Light at 4.

[11] *Id*. at 5, 6.

[12] *Id*. at 7.

[13] *Id*. at 9.

[14] OCGA § 16-17-1(e) reiterating that payday lending is illegal in Georgia. OCGA § 7-4-18(a) also establishes a criminal usury cap of 60%. *See* Georgia Watch and Georgia Financial Protection Coalition, Making Small-Dollar Lending Safer for Georgians, 2018.

[15] Center for Responsible Lending, Shark-Free Waters: States are Better Off without Payday Lending, Pg. 9, Figure 1, (Aug. 17, 2016) (updated Sept. 2017).

[16] Georgia Department of Law, Consumer protection Unit, A-Z Consumer Topics, Payday Loans.

[17] OCGA § 16-17-1(c) "The General Assembly has determined that various payday lenders have created certain schemes and methods in order to attempt to disguise these transactions or to cause these transactions to appear to be "loans" made by a national or state bank chartered in another state in which this type of lending is unregulated, even though the majority of the revenues in this lending method are paid to the payday lender."

[18] OCGA § 16-17-2(b)(4)

[19] OCGA § 16-17-2(a)(1)(E)

[20] OCGA § 16-17-2(d)

[21] D. Campbell et al., Bouncing Out of the Banking System: An Empirical Analysis of Involuntary Bank Account Closures, Journal of Banking & Finance, 36 (2012) 1224–1235, 1231.

[22] *Id*. at 1232.

[23] *Id*.

[24] Georgia Watch and Georgia Financial Protection Coalition, Making Small-Dollar Lending Safer for Georgians, pg. 3, 2018.

[25] 815 ILCS 123/15-5-5, eff. 3-23-21.

[26] Woodstock Institute, SB 1792 would cap the interest rate on loans at 36% APR.

[27] *Id*.

[28] Coalition letter to Gov. Pritzker (January 25, 2021).

[29] Resource Guide: Affordable Alternatives to Predatory Loans.

[30] *See* Woodstock Institute, Will Illinois borrowers find predatory loan alternatives? They already are, says Capital Good Fund's Andy Posner (July 23, 2021).

[31] *Id*.

[32] Neil Bhutta, Jacob Goldin, Tatiana Homonoff. Consumer Borrowing After Payday Loan Bans, February 5, 2016, pg. 8.

[33] Center for Responsible Lending, Shark-Free Waters: States are Better Off without Payday Lending, Pg. 9, Figure 1, (Aug. 17, 2016) (updated Sept. 2017).

[34] Matt Volz, Missoulian, Montana Voters Approve Payday Loan, Real Estate Tax Initiatives, Nov. 3, 2010.

[35] Passman, Wack, CUs Skeptical About Expanding Colorado's Payday Loan Law Nationwide, Credit union Journal, Dec. 3, 2014.

[36] Liz Farmer, The Myth vs. the Truth About Regulating Payday Lenders, Governing the States and Localities, March 2017.

[37] Bourke, Horowitz, Roche, Payday Lending in America: Who Borrows, Where They Borrow, and Why, Pew Charitable Trusts, July 2012, pg. 23.

[38] Payday Loans: a Legislative Research Library Backgrounder, Dec. 2020.

[39] Nebraska Initiative 428, Payday Lender Interest Rate Cap Initiative (2020).

[40] *Id*.

[41] Neil Bhutta, Jacob Goldin, Tatiana Homonoff. Consumer Borrowing After Payday Loan Bans, February 5, 2016, pg. 8.

[42] Center for Responsible Lending, Shark-Free Waters: States are Better Off without Payday Lending, Pg. 9, Figure 1, (Aug. 17, 2016) (updated Sept. 2017).

[43] Melzer, Morgan, Competition in a Consumer Loan Market: Payday Loans and Overdraft Credit, April 2, 2014, pg. 38. *See* SB 99 ch. 248 (1999).

[44] HB 267 ch. 301 (2008).

[45] Urahn, Plunkett, How Borrowers Choose and Repay Payday Loans, Feb. 2013, pg. 51.

[46] Bourke, Horowitz, Roche, Payday Lending in America: Who Borrows, Where They Borrow, and Why, Pew Charitable Trusts, July 2012, pg. 17.

[47] North Carolina Consumers After Payday Lending: Attitudes and Experiences with Credit Options, November 2007, pg. 21. (North Carolina Consumers)

[48] Center for Responsible Lending, Shark-Free Waters: States are Better Off without Payday Lending, Pg. 9, Figure 1, (Aug. 17, 2016) (updated Sept. 2017).

[49] North Carolina Consumers at 22.

[50] *Id*. at 1.

[51] *Id*.

[52] *Id*. at 17.

[53] State Employees' Credit Union, Response to Payday, Vehicle Title and Certain High-Cost Installment Loans Proposed Rule, Docket # CFPB-2016-0025, Oct. 5, 2016, pgs. 1-2.

[54] Credit Union Times, SECU of North Carolina Expands Salary Advance Loan Program to Encourage Saving, Feb. 18, 2003.

[55] State Employees' Credit Union, Response to Payday, Vehicle Title and Certain High-Cost Installment Loans Proposed Rule, Docket # CFPB-2016-0025, Oct. 5, 2016, pg. 3.

[56] North Carolina Consumers at 20.

[57] North Carolina Commissioner of Banks, Consumer Finance Annual Report, 2016, pg. 14.

[58] Kelly Tornow, Center for Responsible Lending, Alfred Ripley, NC Justice Center, Comment on Proposed rulemaking for consumer finance licensees and objections to 04 NCAC 03E .0601(8)(a) through (e), June 1, 2018, pg. 3.

[59] South Dakota Payday Lending Initiative, Initiated Measure 21, 2016.

[60] Center for Responsible Lending, Shark-Free Waters: States are Better Off without Payday Lending, Pg. 9, Figure 1, (Aug. 17, 2016) (updated Sept. 2017).

[61] Rios, Standaert, Farahi, Center for Responsible Lending, The Sky Doesn't Fall: Life After Payday Lending in South Dakota (Jan. 2020), ("Center for Responsible Lending, The Sky Doesn't Fall").

[62] South Dakota Payday Lending Initiative, Initiated Measure 21, 2016, Ballotpedia.

[63] Center for Responsible Lending, The Sky Doesn't Fall, at 12.

[64] *Id.* at 17-19.