

August 1, 2013

By Electronic Delivery

The Honorable Charles Timothy Hagel
Secretary of Defense
U.S. Department of Defense
1000 Defense Pentagon
Washington, DC 20301-3010

Re: Department of Defense Rules Implementing the Military Lending Act (Docket ID: DoD-2013-OS-0133)

The following comment provides a short summary of research findings about payday lending from The Pew Charitable Trusts. Pew is a non-profit, research-based organization, and our interests include providing data and analysis to help ensure a safe and transparent marketplace for consumer financial services. Pew's safe small-dollar loans research project focuses on conducting research that identifies the needs, perceptions, and motivations of those who use payday, deposit advance, auto title, and similar loans, as well as the impacts of market practices and potential regulations. We have been studying this issue closely for more than two years. Our research includes a unique, nationally representative telephone survey of payday loan borrowers and more than a dozen focus groups with small-dollar loan borrowers across the country.

We have published two reports so far in our *Payday Lending in America* series, available at www.pewtrusts.org/small-loans. Our website also includes helpful summaries and animated videos explaining what payday loans are, who uses them, and why.

Pew's research demonstrates that those who borrow short-term, small-dollar loans routinely struggle to keep up with living expenses, and most often they use the loans to pay rent, utility bills, and other routine obligations (as opposed to spreading the cost of purchases over time, which is a more traditional use of credit). Lenders offer these loans to almost anyone with a checking account and a source of income—without assessing the borrower's ability to repay the loan—in exchange for the right to take full repayment from the borrower's checking account on his or her next payday. With other loans, borrowers choose which bills to pay first, and may elect to make a rent or mortgage payment for example, before servicing consumer debt; thus lenders tend only to offer credit to those who have the capacity to repay it. But payday lenders have the unusual ability to collect payment before the customer pays other bills, allowing them to thrive even as they make loans to borrowers who cannot afford them.

Similarly, auto title loans are available to those with clear title to a car, and lenders generally do not assess the borrower's ability to repay these loans.

Key Findings from Pew's *Payday Lending in America* Series of Reports

Pew has published two reports in this series so far (July of 2012 and February of 2013). Additional publications will follow.

- Twelve million people use payday loans annually. The average loan size is \$375.
- Although payday loans are characterized as a short-term solution for unexpected expenses, the opposite is true. The average borrower is in debt for five months during the year, spending \$520 in interest to repeatedly re-borrow the loans. Sixty-nine percent of first-time borrowers used the loan for recurring bills, while just 16 percent dealt with an unexpected expense.
- Most payday loan borrowers have trouble meeting monthly expenses at least half the time.
- Payday loans are unaffordable. The average borrower can afford to pay \$50 per two weeks to a payday lender, but only 14 percent can afford the more than \$400 needed to pay off the full amount of these non-amortizing loans.
- Forty-one percent of borrowers have needed a cash infusion, such as a tax refund or help from family or friends, to pay off a payday loan.
- If payday loans were unavailable, 81 percent of borrowers say they would cut back on expenses such as food and clothing. Majorities also would delay paying bills, borrow from family or friends, or sell or pawn possessions.
- In states that enact strong legal protections, the result is a large net decrease in payday loan usage. Rates of online borrowing are similar in states with payday loan storefronts and those with none.
- Payday loans do not eliminate overdraft risk. A majority of borrowers overdraft as well.
- A majority of borrowers say payday loans take advantage of them, and a majority also say they provide relief.
- By almost a 3-to-1 margin, borrowers favor more regulation of payday loans.

In sum, Pew's research shows that payday loans require lump-sum repayments that far exceed most borrowers' financial capacity. The predictable result is that customers are unable to repay the loans and meet their other financial obligations, resulting in prolonged periods of renewing or re-borrowing. The product poses significant risk of harm to consumers, and it is based on a business model that is highly inconsistent with sound lending practices.

Other loans, such as auto title loans, whether they last shorter or longer than six months, or installment loans lasting longer than 90 days, can also have payments that exceed borrowers' financial capability. Such payments can put borrowers at risk of not being able to cover essential expenses, such as rent or a mortgage. As the Department of Defense has found previously, these risks can be particularly acute for servicemembers. In order for small-dollar loans to be safe and transparent, their payments must fit into a borrower's budget, so that it is feasible to retire that debt and cover other expenses without needing to re-borrow.

Thank you for addressing this important issue.

Sincerely,

A handwritten signature in blue ink, appearing to be 'NB' with a stylized flourish.

Nick Bourke
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www.pewtrusts.org/small-loans

