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Pew's Policy Recommendations to Fix Payday Loan Problems

Payday loans are packaged as short-term loans due on a borrower's next payday, but in reality, borrowers are indebted far longer and pay far more than advertised. The average loan requires one-third of a borrower's biweekly paycheck, exceeding what most can afford without having to borrow again.

Policymakers should act now to fix the problems with payday lending in the 35 states where it currently exists.

5 regulations that will minimize harm to consumers and make small-dollar loans more affordable:

1 Limit payments to an affordable percentage of a borrower's income

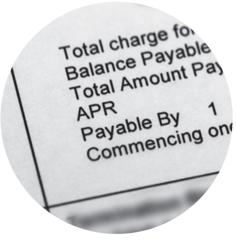
Monthly payments above 5 percent of monthly pretax income are unaffordable for most borrowers. Loans requiring more should be prohibited unless rigorous underwriting shows that the borrower can pay the loan while meeting other financial obligations.

2 Spread costs evenly over the life of the loan

Front-loading of fees and interest should be prohibited. Any fees should be paid evenly over the life of the loan, and loans should have substantially equal payments that amortize smoothly to a zero balance.

3 Guard against harmful repayment or collections practices

Policymakers should prevent or limit the use of postdated checks and automatic withdrawals from borrowers' bank accounts. They should also make it easier to cancel automatic electronic withdrawals and protect against excessively long loan terms.



4 Require concise disclosures of periodic and total costs

Loan offers should clearly disclose, with equal weighting: the periodic payment schedule, the total repayment amount, the total finance charge, and the effective annual percentage rate (APR) inclusive of all fees.

5 Continue to set maximum allowable charges

Almost every state sets maximum allowable rates on some small-dollar loans because these markets serving those with poor credit histories are not price competitive. Policymakers may limit rates to 36 percent or less if they do not want payday lenders to operate, or somewhat higher if they do.

For more information, please visit:
pewtrusts.org/small-loans

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