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Testimony of David Rothstein

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"Trapped in Debt: The Growth of Payday in Ohio"

Hearing on Foreclosure, Predatory Lending, and Payday Lending in America's Cities

Before the Subcommittee on Domestic Policy of the
House Committee on Oversight and Domestic Reform

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Chairman Kucinich, Ranking Member Issa, distinguished members of the Subcommittee, thank you very much for the opportunity to appear before you today. I am David Rothstein, a researcher for Policy Matters Ohio, a nonprofit, nonpartisan organization that provides research on economic issues that matter to low- and moderate-income working families in Ohio. Policy Matters provides this research and education with the objective of fostering an economy that works for all Ohioans. We appreciate your invitation to discuss our research on payday lending in Ohio.

The Economy in Ohio

The economic situation for many Ohio workers is difficult. Policy Matters' research has shown that Ohio wages have been stagnant, employment has not recovered from the last recession, and those who do work are often without health care or retirement benefits.[1] This troubling economic climate is worsened by predatory lending from companies who sell loans to working families at egregious rates, often 391% for a two-week payday loan.

Payday Lending Explosion in Ohio

In a recent report co-authored with the Housing Research and Advocacy Center, Policy Matters Ohio found that payday lending locations in Ohio had increased dramatically from 107 in 1996 to 1,562 in 2006. In those 11 years, there was a 1400% increase in lending locations across Ohio. What's more, our analysis found that while payday lenders were concentrated in mostly urban areas at the beginning of our analysis, by 2006 they were in urban, suburban, and rural neighborhoods. The report, "Trapped in Dept," maps the dispersal of lending locations from a small number of scattered locations in 1996 to 86 of Ohio's 88 counties by 2006. [2] Large urban counties had the most payday lenders in absolute terms, but less populated counties had a greater number of lenders per capita. Payday lenders are so common

[1] Please refer to the report by Amy Hanauer of Policy Matters Ohio entitled "The State of Working Ohio," included with this testimony.
[2] Please refer to the report by David Rothstein and Jeffrey D. Dillman entitled "Trapped in Debt: The Growth of Payday Lending," in Ohio included with this testimony.

throughout Ohio, that by 2006, there were more payday lending locations than McDonalds, Burger King, and Wendy's restaurants *combined*.

The sheer volume of payday lenders in Ohio is problematic because of the weak regulation of the industry. Ohio has a maximum limit of $800 per loan, with a maximum allotted charge of $15 for every $100 borrowed. The Center for Responsible Lending (CRL) estimates that most borrowers (99 percent) are repeat borrowers, taking out loans between seven and 14 times a year. In Ohio, borrowers cannot "roll over" their loans but can do back-to-back transactions where after a 24-hour cooling off period, they can take out a loan to repay previous loans.

Payday lending affects various demographic groups. Our analysis found little relationship between lending locations and areas of low- and moderate-income housing or African-American tracts. A recent study found that "lenders who cultivate more repeat business from existing customers will fare better financially than those who do not."[3] In the business of payday lending, all workers are potential clients regardless of race, income, or living area.

Lenders in Ohio are mostly chains or franchises. The two most common locations are Advance America and Cashland Financial Service, with more than 100 locations each. The top 10 lending companies in Ohio account for more than 55 percent of all payday lenders in Ohio. One lender in Ohio, Buckeye Check Cashing, received substantial financing in grants and loans from the State of Ohio to expand operations in Ohio. The lending industry in Ohio is extremely volatile with lending locations opening and closing frequently within a given year. For instance, in 2005, a total of 113 payday lending locations closed but 357 new locations opened. That same year, 12 locations opened and then closed in that same year.

[3] Michael A. Stegman and Robert Fairs "Payday Lending: A Business Model that Encourages Chronic Borrowing" Economic Development Quarterly (February 2003).

A $500 loan could carry an origination fee of $50 and interest charges of $25 for an effective APR of 391% for the two-week loan. Borrowers face an even more difficult situation when the loan comes due because their economic situation is often the same or worse than before, meaning they either need another loan to repay the first loan or they default on the post-dated check. Thus, the cycle of borrowing keeps borrowers trapped in a constant state of debt.

Recommendations

In our report, we recommend that the protections extended to service members and veterans in the Talent-Nelson Amendment be extended to all working families. Capping lending rates at 36 percent, while still a high APR compared to other loans and forms of borrowing, is a vast improvement over loans made in the 300 percent range. Additionally, credit unions and banks should be offering competitive, fair, and responsible loan products to working families in their communities. Fair and responsible lending is an economic and social benefit to the entire community. Members of Congress can play a pivotal role in implementing these policy recommendations, which again, benefit the entire economic community.

Conclusions

Mr. Chairman, Ranking Member Issa, distinguished members of the Subcommittee, we thank you again for the opportunity to present our findings on the dangerous expansion of payday lending in Ohio. We strongly believe that our policy recommendations will lead to a better economic situation for everyone involved. We look forward to working with the Subcommittee and to Congress on payday lending and other economic issues.