

NATIONAL PEOPLE'S ACTION

American Profiteers How the Mainstream Banks Finance the Payday Lending Industry

In America today there are nearly as many payday lending outlets as there are McDonald's and Starbucks *combined*. The big bank-driven financial collapse has injected new levels of economic uncertainty to many families. Unemployment and underemployment has often meant little or no cushion in families' budgets to pay for financial emergencies. When faced with unexpected bills – like an unforeseen car repair or medical bill – more and more Americans are turning to the only option in their neighborhood; payday lenders.

Payday lenders charge an average of over 400% interest and routinely trap their customers into spiraling debt cycles, with most people taking out three and four loans in a row – often just to pay off the original payday loan. A \$300 payday loan actually costs someone an average of over \$750.

These lenders wouldn't be thriving without the financial backing of the mainstream banking industry. Analysis conducted by National People's Action (NPA) shows that major banks provide, at minimum, over \$1.5 billion in credit to payday lenders who fund an estimated \$15 billion in payday loans every year.¹ Wells Fargo, for example, may not want to sully its good name by opening up a payday storefront, but has no trouble financing one third (32%, or over 8,000) of all the payday storefronts in America. This report lays out how the payday lending industry operates and is financed.

American taxpayers bailed out all of the major banks funding payday lending. Now they are paying us back by profiting off us when we're down. We won't be able to rid our communities of the destruction wrought by payday lenders until we cut off the spigot of credit coming from the Big Banks. Wells Fargo, Bank of America and other funders of payday lenders need to immediately disinvest and instead offer affordable, small dollar loans to their communities.

¹ Securities and Exchange Commission. \$1.5 Billion in credit agreements are publicly disclosed in recent SEC filings. Much of the payday lending industry is privately owned and is not required to report their sources of funding publicly.

I. Payday Industry Overview

- An estimated 120 million payday loans are issued annually in the US worth a total value of \$42 Billion.²
- The payday lending industry together is about the size of Discover credit cards and about half the size of American Express credit cards.³ In 2008 the industry made \$7.3 billion in revenue from these loans.

The cash advance services industry grew rapidly from the early 1990s through this past decade. Growth was, in part, “in response to a shortage of available short-term consumer credit alternatives from traditional banking institutions.”⁴ In 1996, there were an estimated 2,000 payday lending stores operating in the U.S. There are an estimated 23,000 payday lender outlets nationwide⁵ -now equaling the number of McDonald’s and Starbucks stores in the country.⁶ A segment of this industry operates out of pawn shops and while another is located in check-cashing and payday loan stores. Online payday lending is also a growing segment and is offered by the major payday lending companies.

The Payday Lending industry in 2009 is as profitable as it has ever been. Many major payday lenders have increased their profits from loan fees amid the economic downturn (3.5% increase in net revenue 2009 over 2007).⁷

² Ernest & Young, September 2009 and Stephens, Inc 2008. Various studies report a total cash advance industry size of \$42 Billion in 2008 and \$47 Billion in 2006.

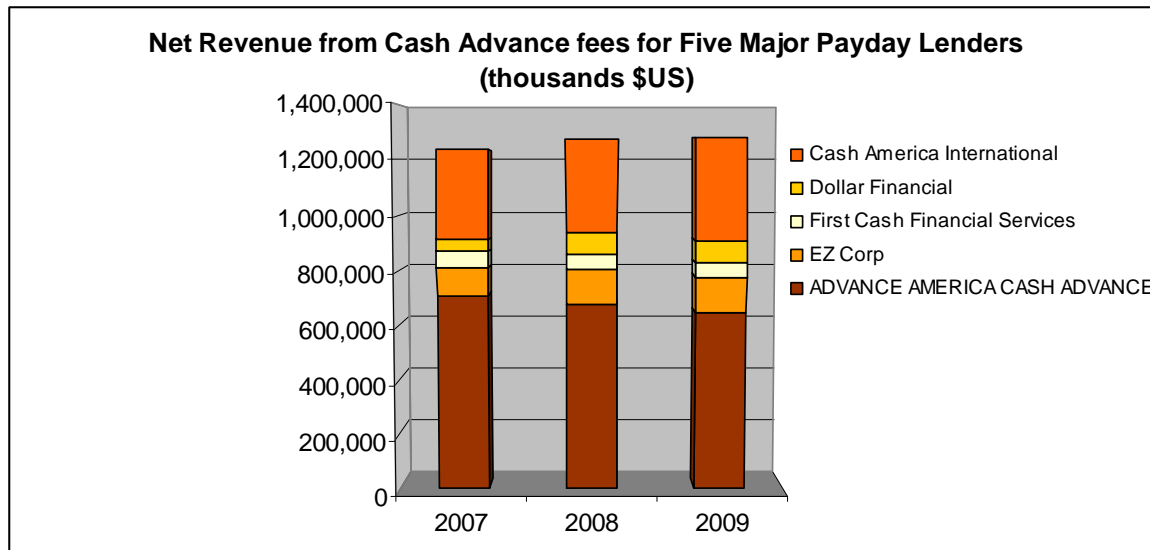
³ Comparison by payday annual lending volume and credit card outstanding balance. For industry totals see: www.creditcards.com

⁴ Advance America, Cash Advance Centers, Inc. 10-K filing with SEC
<http://www.sec.gov/Archives/edgar/data/1299704/000104746909002196/a2190876z10-k.htm>

⁵ From report by financial services firm Stephens, Inc. 2008

⁶ Wikipedia lists 11,000 Starbucks stores nationally, and reports some 13,000 McDonalds restaurants in the U.S.

⁷ Source: SEC. Based on a survey of 5 major payday lending companies comprising about 20% of the industry by revenue.



Source: SEC 10-K (Advance America, Ez Corp, First Cash Financial, Dollar Financial, Cash America)

II. Costs of Payday Lending: What the Borrower Pays

- The average effective interest rate on a payday loan is 455% (APR). For a loan of \$300, a typical borrower pays on average \$775, with \$475 or 185% of loan principal going to pay interest and fees over an average borrowing cycle.⁸

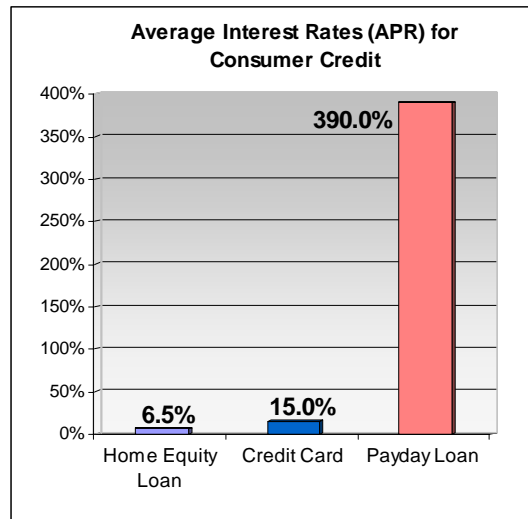
III. Who Uses Payday Day Loans?

- An estimated 12 million borrowers per year
- Most earn between \$25,000 and \$50,000 per year
- People with a job but who have no access to affordable credit options
- Borrowers receive on average 8 to 13 short-term loans per year⁹

Payday lending is significantly more expensive than other consumer credit options.

⁸ This example assumes an average loan term of 14 days and 9 loans per year charging a fee of \$17.50 per \$100 dollars borrower. Loan terms and fees are consistent with surveyed industry practices. See ["Quantifying the Economic Cost of Predatory Payday Lending", Center for Responsible Lending, 2003](#) which rep. Also, see Payday Loan calculator at: <http://ago.mo.gov/cgi-bin/ConsumerCorner/calculators/payday.cgi>

⁹ This fact runs counter the payday lending industry's usual presentation of their average customer as a one-time borrower with a limited, short-term financing need.



The Federal Trade Commission has issued numerous consumer alerts and warnings on payday lending. Congress has also taken the step to protect all military service members and dependents from payday loans create by capping rates to this group of borrowers at 36%.¹⁰

IV. How the Major Banks Finance Payday Lending Companies

Key Facts:

- a) There are some 17 major payday lending companies (both public and privately-held) that operate approximately half of the nation's total of 22,00 payday lending outlets¹¹.
- b) Major payday loan companies receive their funding from the largest national banks (see list presented below).
- c) Major banks provide over \$1.5 Billion in credit available to fund major payday lending companies.¹²
- d) The major banks funding payday lending include Wells Fargo, Bank of America ,US Bank, JP Morgan Bank, and National City (PNC Financial Services Group).
- e) All together, the major banks directly finance the loans and operations of, at minimum,

¹⁰ Federal Trade Commission Consumer Alert March 2008 <http://www.ftc.gov/bcp/edu/pubs/consumer/alerts/alt060.shtm>

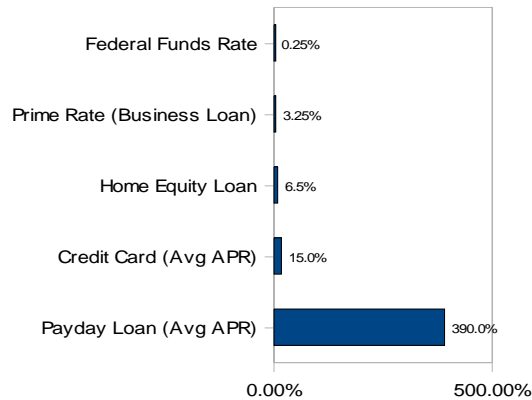
¹¹ Ernst & Young estimates industry size at 22,000 in 2009. 12,000 stores are quoted to be operated by the largest 17 companies with a total industry size of 23,600, as reported from Stephens, Inc. 2008. Also see: SEC 10-K filing for First Cash Financial Services. <http://www.sec.gov/Archives/edgar/data/840489/000092623609000014/fcf08q4.htm>

¹² Note: It is often difficult to determine the exact amount of financing provided by a given bank to a payday company because funding is often pooled from a variety of lenders and the specifics are not disclosed by SEC.

38% of the entire payday lending industry, based on store locations.¹³

- f) Our analysis finds that the major banks indirectly fund approximately 450,000 payday loans per year totaling \$16.4 Billion in short-term payday loans.
- g) Wells Fargo is a major financier of payday lending and is involved with financing companies that operate one third (32%) of the entire payday lending industry, based on store locations.¹⁴
- h) All of these above mentioned banks received TARP bailout funds in 2008-09 and have benefited from accessing capital at exceptionally low interest rates from the Federal Reserve.
- i) In summary: Major banks access credit from the Federal Reserve discount window at 0.5% or less, these banks extend an estimated \$1.5 Billion annually to eight major payday lending companies, who in turn use this credit to issue millions of payday loans to consumers every year at average rates of 400% APR.

Average Borrowing Rates for Banks, Business, and Consumers



V. Types of Financing Provided to Payday Lenders:

Access to credit is the life-blood of any lending business, including the payday industry. Credit is necessary to fund loans, maintain the liquidity needed to make more loans, and to cover operating costs. Funding is provided in the forms of lines of credit and direct loans made by

¹³ This figure is based store locations. The major payday lending companies which operate some 8,800 store locations out of an estimated 23,000 total store locations nationwide, according to a 2008 industry study by Stephens, Inc.

¹⁴ This figure is based store locations. The major payday lending companies funded by Wells Fargo are listed below in this document and together operate some 7,500 store locations out of an estimated 23,000 total store locations nationwide.

banks to the payday lender companies. As Advance America, the nation's largest payday lender, states in its 2008 annual filing: "If we are unable to maintain access to external sources of liquidity, our ability to finance our current operations or future dividends would be impaired."¹⁵

Payday Lenders rely on and use their available credit, at times drawing down over 75% or more of their available credit.¹⁶

- **Line of Credit:** also called a "revolving" credit facility. The most common type of financing used by payday lenders. A company is approved for a maximum amount, and funds are charged to account on an as needed basis to fund loans. Interest rates are typically variable¹⁷ and only paid on the funds actually withdrawn. These lines of credit are periodically extended, renewed, or modified by the lender(s).
- **Term Loan:** less common but also used by payday lending companies. All the loan funds are issued to the borrowing company up front and repaid according to a specified payment schedule.

Example: Advance America paid over \$11.2 million in interest on their \$250 million in credit from major bank lenders in 2008. For their money borrowed, Advance America paid average interest rates of 4.1% and 7.76%, in 2007 and 2008 respectively.¹⁸

VI. Example of a Major Bank funding Payday Lending: Wells Fargo

Wells Fargo finances the most major payday lending companies of any major national bank. Wells Fargo provides funding to least 9 major "cash advance" companies that operate approximately one third (32.6% or some 8,500 stores) of the total industry's 22,000 payday lending stores nationwide. They have provided hundreds of millions of dollars in credit to at least 9 major "cash advance" (aka "payday") loan companies since 2006. Wells Fargo, as the

¹⁵ Advance America, Cash Advance Centers, Inc. 10-K filing with SEC

¹⁶ For example, First Cash Financial a major payday lender with over 500 pawn and payday loan shops on December 31, 2008 had \$68,500,000 outstanding under their \$90 Million Credit Facility with \$21,500,000 available for borrowings.

¹⁷ The interest paid on a line of credit is typically a variable rate and determined by a base rate (LIBOR-based or prime rate) plus an applicable margin which may range from 1% to 3.5%.

¹⁸ The weighted average interest rate on our \$142.3 million of variable interest debt as of December 31, 2007 was approximately 7.76%. The weighted average interest rate on our \$189.8 million of variable interest debt as of December 31, 2008 was approximately 4.17%.

sole lender or as a lending partner, has extended credit which funds an estimated \$12 Million in payday loans (an estimated 30 Million short-term loans) annually.

A list of recent funding arrangement with the companies follows below:

VII. The Major Payday Companies Funded by Big Banks¹⁹

Advance America, Cash Advance Centers, Inc:

Advance America is the nation's largest payday lending company with over 2,500 store locations operating in 32 states. As the industry leader, Advance America issued over \$1.2 Billion in payday loans in 2009. Wells Fargo, together with other bank partners (including Bank of America, US Bank, and Wachovia), provides a \$275-\$300 Million line of credit to the corporation (agreement amended March 24, 2008 and credit matures on March 24, 2013). In 2009 the Advance America was able to lend out in the form of payday loans, over 4.4 times their credit limit.

ACE Cash Express, also operating under the name Global Cash Express, with over 1,800 stores is the second largest player in the industry. Wells Fargo, along with a group of other banks (including JP Morgan Chase, US Bank, Keybank National), provided \$300 Million in financing dated February 2006).²⁰

Cash America International:

Cash America International operates approximately 670 payday lending stores nationally (431 in its "Cash America" pawnshops, in 74 standalone Cash America Payday Advance locations, in 174 locations operated by its wholly-owned subsidiary CashLand Financial Services, Inc).²¹ Cash America is also a major payday lender via the internet, with 1.7 million loans made last year via the web.²² Wells Fargo along with eight bank lending partners (including JP Morgan Chase, US Bank, and Key Bank) provide a \$300 Million line of credit, amended and restated as of February, 2009 extending through March 2012. This \$300 Million allowed the company to issue a total of 3.2 million payday loans in 2009.

¹⁹ "Major" in this case means large and publically traded companies. This analysis relies on finance agreements for publically-held companies are filed with the SEC.

²⁰ ACE Cash Express was previously publically held. The company was purchased in 2007 and is now owned by a private investment concern. Latest updates to funding agreement is not publically available but finance partners are likely the same as in earlier years.

²¹ 10-K Filing for Year End 2007. <http://www.sec.gov/Archives/edgar/data/807884/000095013409004054/d66566e10vk.htm>

²² SEC filing, 10-K

Dollar Financial Group Inc

Dollar Finance Group operates some 1,200 stores in the US and internationally. The company claims to have “the largest financial services store network of its kind” in each Canada (461 stores) and the United Kingdom (337 stores) and the second-largest network of its kind in the United States (358 stores). In fiscal year 2009, Dollar Financial originated 4.1 million single-payment consumer loans with an average principal amount of \$406. On October 30, 2006, Dollar Financial entered into a Credit Agreement with Wells Fargo and Credit Suisse totaling \$475 Million in financing (\$375.0 million in a six-year term loans held by UK and Canadian subsidiaries, a \$75.0 million revolving credit facility in the U.S. and a \$25.0 million revolving credit facility in Canada.)²³

EZ Corp, Inc

Operates 479 EZ Money stores nationwide (as of year end 2009) and is funded through a credit agreement dated 12/31/2008. Wells Fargo provides \$50 Million (42%) of the total \$120 Million in credit available to funds company’s operations and payday loans. Financing includes a \$80 Million line of credit, of which Wells Fargo is the major lender providing \$33.3 Million, and a \$40 Million term loan, of which Wells Fargo is also the lead lender providing \$16.6 Million in financing.²⁴

First Cash Financial Services

First Cash has 546 locations (383 pawn shops and 163 Short-Term Loan/Check Cashing stores) in twelve U.S. states and sixteen states in Mexico.²⁵ Wells Fargo is one of two lenders (the other being JP Morgan Chase) providing the Company with \$90 Million available under its Credit Facility, dated Sept 7 2007 and which matures in April 2010.²⁶

Other Companies funded by Wells Fargo:

- Check Into Cash: 1,100 stores nationwide.²⁷ Privately held companied in Tennessee

²³ 10-K filing dated 03/09/2009 <http://www.sec.gov/Archives/edgar/data/1271625/000095012309040898/w74935e10vk.htm> and 8-K filing dated 10/30/2006 <http://www.sec.gov/Archives/edgar/data/1028643/000089322006002317/w26544exv10w1.htm>

²⁴ 8-K filing dated 12/31/2008 <http://www.sec.gov/Archives/edgar/data/876523/000095013409000019/d65775exv10w1.htm>

²⁵ In addition, the company is a 50% partner in Cash & Go, Ltd., a Texas limited partnership. Effective December 2009, the Company sold all 22 of its stores located in California, Washington and Oregon to privately-held California Check Cashing Stores, LLC. This decision is the result of the Company’s strategy to increase focus on its pawn operations and further reduce regulatory exposure from payday lending products.

²⁶ 8-K filing exh 10.1 <http://www.sec.gov/Archives/edgar/data/840489/000092623607000094/exh10-1.htm>

²⁷ UCC filing

Credit extended by Wells Fargo on 11/06/2008.²⁸

- Mister Money, 43 Stores nationally
- American Payday Loans, 21 Stores nationally.

VII. ADDITIONAL INFORMATION

State Regulation of the Payday Industry

Many states have passed laws limiting payday lending activities. The most direct and comprehensive regulation undertaken by many state governments is to cap interest rates at 36%, which can effectively prohibit payday lenders from operating in the state²⁹. Currently fifteen states and the District of Columbia have placed interest rate caps on payday lending.

There have been frequent reports of some payday lenders violating state laws limiting payday lender fees and practices.³¹ There have also been reported findings that the payday loans encourage chronic and repeated borrowing.³²

Maps of Payday Lending Outlets Nationwide

The below maps reveal the geographic concentrations of payday lending in the US. Maps reveal that the payday lending stores are heavily concentrated in urban areas throughout the Midwest and South and Southeast. Maps also show that payday lending industry has been effectively eliminated in many states on the East coast due to state-enacted 36% rate caps.

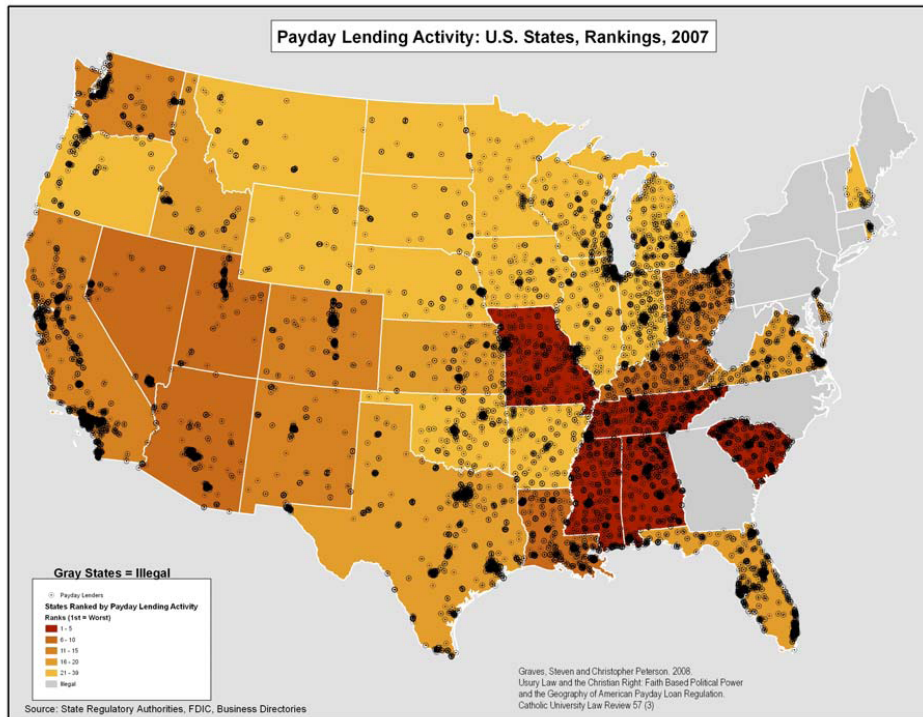
²⁸ Tennessee Dept of State website UCC # 308066055

²⁹ From Wikipedia: "As a result of the interest-rate cap enacted by D.C., all licensed payday lenders have withdrawn from the market, and no lawful payday loans are presently available in D.C."

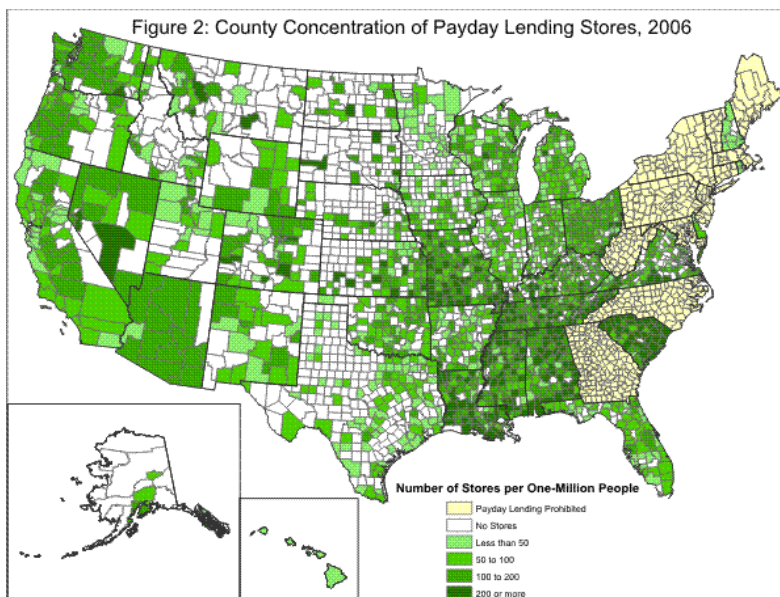
³¹ From Wikipedia entry on Payday Lenders: "On May 30, 2008, the [Illinois Department of Financial and Professional Regulation](#) fined [Global Payday Loan](#) \$234,000—the largest [fine](#) in [Illinois](#) history against a payday lender—for exceeding the \$15.50 per \$100 limit on charges for payday loans." Also see Iowa Independent article: "[Payday lenders use loopholes to continue high-interest loans](#)"

<http://iowaindependent.com/26824/payday-lenders-use-loopholes-to-continue-high-interest-loans>

³² http://www.kenan-flagler.unc.edu/assets/documents/CC_Payday_lending.pdf



Map used with permission, from Testimony of Uriah King, Center for Responsible Lending before the Ohio Senate Finance and Financial Institutions Committee, May 2008³³ Note: AK, OH, and NH have recently passed rate caps.



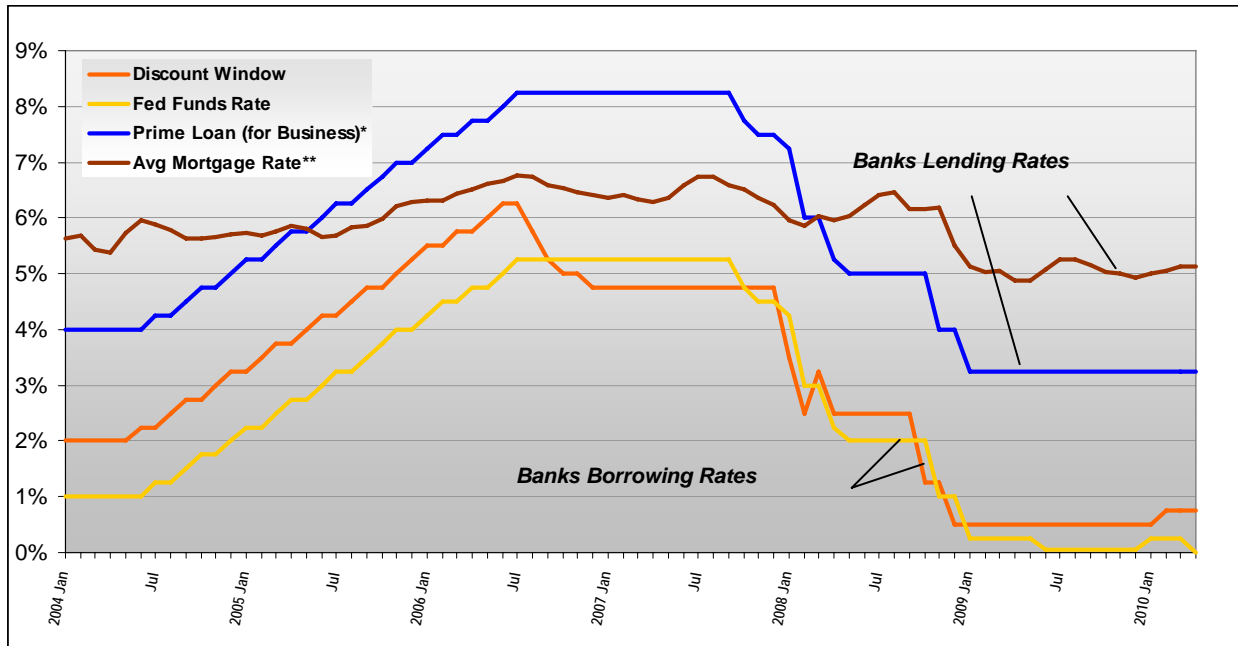
The Costs for Banks to Borrowing Funds: Public Intervention Subsidizes Bank Profits

Since the onset financial crisis, Banks –especially the major banks which have increased in size and marketshare in the past two years- have benefited from preferential terms in accessing capital from public sources. Beginning in Aug 2007, the Federal Reserve repeatedly cut the rates at which banks were allowed to borrow. Rates reached as low as 0% and remained there for most of 2009 (see Discount Window rate and Federal Funds rate in graph below). In addition, for 18 months from Aug 2007 to March 2010, the Federal Reserve extended the borrowing period to a 1 month term, up from the typical overnight term limit. This has allowed banks to access large amount of capital at almost no cost. Banks in turn can invest this capital in Treasury Securities (or other public agency-backed investments), or lend out at significantly higher rates as home mortgage or commercial/business loan. Public sector interventions such as this have preserved or improved the bank's investment returns by artificially reducing their cost of capital. For banks, their current "rate spread" (difference between the banks' borrowing cost and lending rates) is equal to or greater than the spread enjoyed during the years of housing bubble (2005-2007).

Common Interest Rates for Bank Borrowing and Lending, 2004-2010

³⁴

See: <http://www.federalreserve.gov/PUBS/FEDS/2009/200933/index.html>



Updated April, 2010
 Prepared by Nicholas Bianchi, NPA Research Analyst
 email: nick@npa-us.org