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Commentary

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The High Cost of Being Poor

MOST OF US HAVE SEEN THE signs which advertise "Fast Cash: All It Takes Is Your Good Word. No Credit Check!" Such ads are the work of payday lenders, the latest scheme in predatory financial services that take advantage of working families.

The typical payday lending scheme works like this: The customer, usually a low-income individual with a steady job and a bank account, goes into a payday lender's office to borrow money to meet short-term need. Maybe they don't have enough money to pay an overdue bill without bouncing a check, perhaps they need money for Christmas presents or an unexpected financial emergency has popped up. Whatever the reason, payday lenders are attractive because they promise quick and easy cash without a credit check.

Once inside the payday lender's office, the individual borrows some amount, usually between $100 and $500, and agrees to repay the loan when his next payday arrives, typically 14 days later. For this "privilege," the borrower has to repay the original amount, plus a "fee," which is really interest that amounts to more than 400 percent on an annual basis.

Unfortunately, when payday arrives, the customer may not have the funds to "cover" the payday loan. It's here that the "debt trap" begins. Without the money to repay the original loan, a visit to another payday lender to cover the first payday loan is often what follows, pushing them further into debt. Even if they have the money to repay the original loan, they will have paid an interest rate that is 20 to 30 times higher than that paid by borrowers using traditional lenders.

But doesn't Arkansas have a law preventing the charging of such exorbitant interest rates? Yes, it does. Article 19, Section 13 of the Arkansas Constitution sets a limit for interest rates charged on consumer loans to no more than 17 percent, a far cry from the 400 percent or higher rate charged by payday lenders.

So how do payday lenders get by with this? In 1999, the Arkansas Legislature passed Act 1216, a law which classifies the charge for borrowing as a "fee" rather than as interest. By simply changing what interest is called, the Legislature has allowed payday lenders to charge fees that would otherwise be illegal under any other name.

What can be done to protect our struggling working families, our military personnel and retirees who are the favorite targets of this predatory industry? The legislature should repeal the 1999 legislation that exempts payday lenders from the lending requirements that banks, mortgage companies and other financial institutions have to meet. Then, it should go further by establishing safeguards that prevent the payday loan industry from reinventing itself in ways that thwart the intention of the Arkansas Constitution.

Just as importantly, Arkansas must promote reasonable alternatives to payday lenders. Employers could offer credit lines to employees equal to 2.5 percent of their salaries that could be repaid through payroll deductions spread over a year without interest. Credit counseling can be tied to low-cost loans by banks and credit unions. Branches of banks could be opened in low-income neighborhoods and offer check-cashing services, money orders and savings accounts to directly compete with payday lenders.

It's time Arkansas took the steps to prevent payday lenders from preying upon the poor. Given the challenges low-income families already face, it's time to lower the high cost of being poor.

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