The Dow Jones industrial average closed at 10,667.39. -213.32

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Banks urged to provide payday-loan substitutes

BY DAVID SMITH
ARKANSAS DEMOCRAT-GAZETTE

Banks have the best opportunity to offer alternatives to "payday lending," Arkansas Advocates for Children and Families says.

The nonprofit organization released this week a four-page report, "Alternatives to Payday Loans," that says banks and credit unions have the tools and infrastructure to allow them to offer such products at a low cost.

In an example of payday lending, a typical borrower writes a check for $400 and receives $350. The payday lender agrees not to cash the check for two weeks. The $50 charge, which payday lenders call a fee, equals a 373 percent annual rate in that instance. Some borrowers eventually pay two or three times the amount of their original check in charges.

Some possible alternatives to payday loans include revolving lines of credit, a no-minimum loan policy, bounce-proof checking and a provision that allows a customer to write a check without a penalty for insufficient funds.

Some Arkansas banks already have some of these products, but they are generally available only

See LOANS, Page 2D

Loans

• Continued from Page 1D

to established customers and are not widely marketed, with the exception of bounce-proof checking, the report said. Many payday loan customers have low incomes or are facing financial crises and may not qualify for such products, the report said. Some banks outside Arkansas, including Citibank, have products targeted specifically at payday loan customers.

One thing that would make the alternatives to payday loans attractive to bankers is if regulators allow the products to qualify for Community Reinvestment Act credit. The act requires banks to meet the credit needs of the communities where they are located, especially low- and moderate-income neighborhoods.

If Arkansas banks could get a Community Reinvestment Act credit, they would be more likely to offer a product as an alternative to payday loans, said Alan Bufford, a senior vice president with Citizens Bank of Batesville.

"Banks are always looking for ways to help the community and I think this would be one way they could do that," Bufford said.

Arkansas Advocates wants a lending model that banks in Arkansas can offer their customers who use payday lenders, said Kathryn Hazelette, research and fiscal policy analyst for the group.

"We're hoping when we have that model mapped out that regulators will let the banks receive CRA credit," Hazelette said.

Federal regulators probably will give banks community reinvestment credit for the products in the "not-too-distant future," said Sheila Bair, professor at the Isenberg School of Management at the University of Massachusetts at Amherst.

Bair said in her 83-page report, "Low-Cost Payday Loans: Opportunities and Obstacles," that the biggest obstacle to banks offering payday loan alternatives is making a profit without charging high rates. If banks received some of their required Community Reinvestment Act credit for offering the products, making a profit might not be as much of a necessity. She wrote the report for the Annie E. Casey Foundation.

Since the Legislature passed the Check Cashers Act of 1999, which characterizes the charge payday lenders make for their loans as a fee and not interest, the businesses have proliferated in Arkansas. The state now has 281 payday lenders, more than twice the number of McDonald's restaurants, the report said.

With the approval of the 1999 law, the high interest common to payday loans is overlooked. A case pending before the Arkansas Supreme Court will determine if the Check Cashers Act is unconstitutional.

There has been no research to see if such alternative products by banks reduce the business of payday lenders, Bair said.

"One of the concerns about payday loan alternatives is are they being used by customers as an alternative or are they just being used in addition to payday loans that they are getting?" Bair said. "Hopefully they are not. A lot of banks, when they offer the payday loan alternatives, will require that you don't have outstanding payday loans."