



# High-Cost Alternative Financial Services: Policy Options

## EXECUTIVE SUMMARY

Many Canadians turn to high-cost alternative financial services<sup>1</sup> when they need a short-term fix for a budgetary issue. Though these banking and credit alternatives are a convenient choice for individuals in search of fast cash, particularly those who face barriers to obtaining credit at a bank or credit union, access comes at a steep price and with a high degree of risk. On its own, one high-cost loan has the potential to trap a borrower in a cycle of debt, not only amplifying their short-term problem, but also limiting their ability to secure the income and assets needed to thrive in the long term.

It is difficult to ignore the impact that these high-cost products have on low-income Canadians and their communities. The existence of high-cost alternative financial services reinforces a two-tiered banking system in which the poor pay more for expensive services, results in the depletion of capital from low-income communities and contributes to economic inequality. Without more stringent regulation, vulnerable Canadians will continue to experience financial exclusion and take on heavy debt loads—two major contributors to poverty in Canada.

Across Canada, the desire for improved regulation of high-cost alternative financial services is increasing. In the past few years, many provinces and municipalities—including Alberta and Calgary—have strengthened payday lending rules. In addition, several provinces have either introduced or proposed regulatory changes that apply to high-cost alternative financial services in general. Manitoba adopted new rules for high-cost credit products in 2016, and provincial governments in Ontario, British Columbia, Quebec and Alberta are currently reviewing existing consumer protection legislation to better address various forms of high-cost lending.<sup>2</sup>

The policy recommendations presented in this brief, and summarized in the chart on page two, are inspired by the regulatory initiatives across the country, and reflect ways in which all three levels of government can contribute to better consumer protection for all Canadians. Specifically, these recommendations respond to the areas of concern highlighted in our previous research<sup>3</sup> on high-cost alternative financial services: high cost, inadequate disclosure, unfair and unreasonable practices, and a willingness to lend to vulnerable borrowers.

Policy change is only one of the many interventions necessary to address the issues of high-cost alternative financial services. Financial literacy, consumer education and the creation of safe and affordable financial products are also essential components of financial inclusion. These elements merit the consideration of community organizations, banks and credit unions, as well as consumers. Importantly, neither the list of services discussed in this brief, nor the suite of options presented, is exhaustive; instead, these recommendations represent an important next step in our shared work to strengthen consumer protection, increase financial inclusion and reduce poverty in Canada.

1. Our research focuses on six high-cost alternative financial services: instalment loans, pawn loans, title loans, rent-to-own financing, cheque cashing and sub-prime or non-prime auto loans.  
 2. See Appendix A for a summary of changes, both adopted and proposed, to consumer protection legislation across Canada.  
 3. For a summary of this research, including links to specific reports, see Momentum, Summary Brief: High-Cost Alternative Financial Services, (Calgary: Momentum Community Economic Development, 2017), <http://momentum.org/files/Publications/Fringe%20Financial%20Summary%20Brief.pdf>.

## Summary of Federal, Provincial and Municipal Policy Recommendations

|                                 | Government of Canada  | Government of Alberta   | City of Calgary   |
|---------------------------------|---|---|---|
| High Cost                       | <ul style="list-style-type: none"> <li>Review and strengthen federal usury laws, and consult Canadians to inform this review</li> <li>Clarify how the Criminal Code maximum rate of borrowing is calculated and enforced</li> </ul>                   | <ul style="list-style-type: none"> <li>Advocate for a review of the criminal code maximum rate of borrowing</li> <li>Advocate for clarification on how the Criminal Code maximum rate of borrowing is calculated and enforced</li> <li>Limit loan fees and add-ons to one monthly charge</li> <li>Introduce price caps for rent-to-own contracts</li> <li>Reduce the cost of cheque cashing, and support employers to offer direct deposit</li> </ul> | <ul style="list-style-type: none"> <li>Support employers to offer direct deposit</li> </ul>   |
| Inadequate Disclosure           | <ul style="list-style-type: none"> <li>Mandate a standardized Financial Facts Label on all credit agreements and advertising for federally regulated financial products</li> </ul>  | <ul style="list-style-type: none"> <li>Mandate a standardized Financial Facts Label on all credit agreements and advertising for provincially regulated products</li> <li>Prohibit solicitation of additional loans and refinancing options</li> <li>Require reinstatement rights in rent-to-own and title loan contracts</li> </ul>  | <ul style="list-style-type: none"> <li>Improve disclosure requirements</li> <li>Mandate distribution of financial literacy information</li> </ul> |
| Unfair Practices                | <ul style="list-style-type: none"> <li>Host an inter-jurisdictional consultation to create a pan-Canadian consumer protection strategy</li> <li>Equip law enforcement with the knowledge, tools and resources to enforce rules effectively</li> </ul> | <ul style="list-style-type: none"> <li>Advocate for and participate in the creation of a pan-Canadian consumer protection strategy</li> <li>License all businesses that provide high-cost alternative financial services</li> <li>Equip law enforcement with the knowledge, tools and resources to enforce rules effectively</li> </ul>   | <ul style="list-style-type: none"> <li>License all business that provide high-cost alternative financial services</li> </ul>                      |
| Lending to Vulnerable Borrowers | <ul style="list-style-type: none"> <li>Improve access to basic financial services and credit products through the Bank Act</li> </ul>   | <ul style="list-style-type: none"> <li>Require lenders to assess a borrower's ability to repay</li> <li>Create a provincial Financial Empowerment Fund</li> </ul>   | <ul style="list-style-type: none"> <li>Introduce minimum distancing through a land use bylaw</li> </ul>   |

## POLICY RECOMMENDATIONS

High-cost alternative financial services are expensive and unsafe; yet, they are often the only option for low-income individuals, particularly those who struggle to obtain credit at mainstream financial institutions like banks and credit unions. Previously, Momentum examined the issues and impact of six of the most prevalent high-cost services: instalment loans, pawn loans, cheque cashing, rent-to-own financing, title loans and sub-prime/non-prime auto loans. The next step in our work on high-cost credit, this brief contains series of policy solutions to the key issues identified in earlier research: high cost, inadequate disclosure, unfair and unreasonable practices, and willingness to lend to vulnerable borrowers.<sup>4</sup>

The recommendations contained in this brief span all three levels of government, and are intended to strengthen consumer protection with regard to high-cost alternative financial services—both those that exist in the market place today, as well as those that may emerge in the future. Momentum urges all levels of government to consider improvements to the rules that govern high-cost credit, and to collaborate where appropriate, to ensure that policy can respond to an evolving and changing industry with flexibility and effectiveness.

## Government of Canada

### 1. Host an inter-jurisdictional consultation on a pan-Canadian Consumer Protection Strategy

In Canada, all three levels of government oversee consumer protection laws and regulate aspects of the high-cost credit industry. In 2016, the Government of Manitoba updated its consumer protection legislation to include rules for high-cost credit providers. In addition, several provinces, including Quebec, British Columbia, Ontario and Alberta, are currently exploring changes to their own consumer protection laws. At the federal level, the Department of Finance is undertaking a review of the Federal Financial Sector Framework, given a statutory sunset of March 29, 2019.<sup>5</sup> This framework, which includes the *Bank Act*, should ensure that the financial sector “meets the needs of an array of consumers,”<sup>6</sup> including by providing access to affordable small-dollar credit.

A pan-Canadian Consumer Protection Strategy would improve the effectiveness of these legislative and regulatory frameworks, as well as any policy initiatives that governments undertake related to consumer protection. The federal government should take on a leadership role in the development of such a strategy by hosting an inter-jurisdictional consultation with the provinces and territories. Moreover, governments should take into consideration best practices from countries such as Australia<sup>7</sup> and the United States<sup>8</sup> in developing and implementing the strategy. Finally, the federal government, provinces and territories should ensure that the pan-Canadian Consumer Protection Strategy addresses the following three recommendations:

4. Momentum, High-Cost Alternative Financial Services: Issues and Impact (Calgary: 2017) <http://www.momentum.org/files/Publications/Part%201%20High-Cost%20Alternative%20Financial%20Services.pdf>

5. Government of Canada, Department of Finance, “Department of Finance Canada Launches Consultations to Review the Federal Financial Sector Framework,” press release, August 26, 2016, <https://www.fin.gc.ca/n16/16-105-eng.asp>.

6. Ibid.

7. Australian Government, Department of the Treasury, “Government response to the final report of the review of the small amount credit contract laws,” press release, November 28, 2016, <http://kmo.ministers.treasury.gov.au/media-release/105-2016/>.

8. Consumer Financial Protection Bureau, “Consumer Financial Protection Bureau Proposes Rule to End Payday Debt Traps,” press release, June 2, 2016, <https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-proposes-rule-end-payday-debt-traps/>.

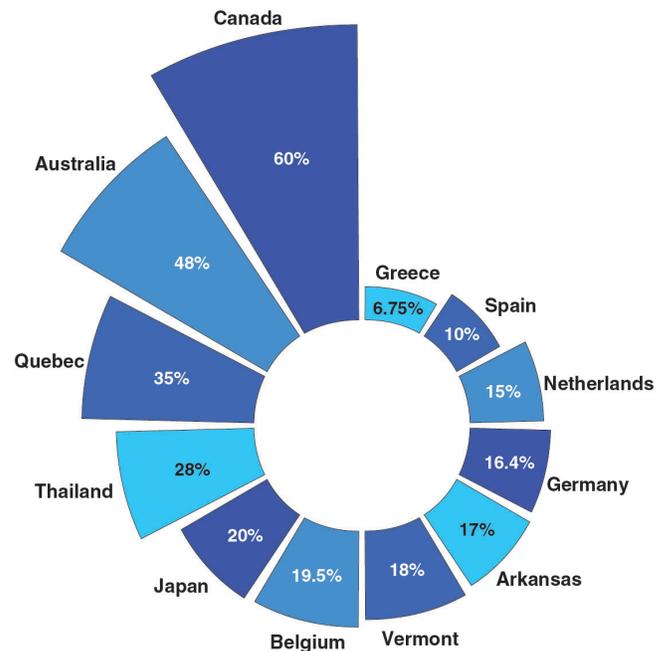
**A.** Review and strengthen federal usury laws, and consult Canadians to inform this review

Seventy-six countries have adopted an interest rate cap for loans, with one of the most commonly-stated objectives being to protect consumers from excessive interest rates.<sup>9</sup> Several countries also note a specific aim of shielding consumers from predatory lending.<sup>10</sup> Since 1980, the Government of Canada has capped allowable interest rates at 60 per cent through section 347 of the *Criminal Code*.

Canadian organizations have called for a lowering of the criminal interest rate to 30 per cent.<sup>11</sup> In addition, a private member's bill, introduced unsuccessfully in the Canadian Senate in 2004, aimed to set the usury ceiling at 35 per cent above the Bank of Canada's overnight lending rate.<sup>12</sup> In the United States, the Center for Responsible Lending has advocated for a 36 per cent interest ceiling at the national level, based on the cap introduced by Congress in 2006 to protect military personnel from payday lenders.<sup>13</sup> Though not enacted, a bill was introduced in the US Senate in 2009 by Senator Dick Durbin that would have established a national usury rate of 36 per cent for consumer credit transactions.<sup>14</sup> At the time, public opinion in the United States indicated a high level of support for such a measure.<sup>15</sup>

There is precedent in other jurisdictions for a lower usury ceiling (see Figure 1). To ensure that Canada's usury law offers sufficient protection to consumers, the Government of Canada should review section 347 of the *Criminal Code*. This review would be strengthened through consultation with Canadians, and particularly through collaboration with the provinces and territories due to their primary responsibility for consumer protection.

**Figure 1**  
Examples of interest rate caps around the world



**Sources:**

Constitution of the State of Arkansas of 1874, <http://www.arkleg.state.ar.us/assembly/Summary/ArkansasConstitution1874.pdf>  
 The Vermont Statutes, 9 V.S.A § 41a, <http://legislature.vermont.gov/statutes/section/09/004/00041a>  
 Institut für Finanzdienstleistungen e.V., Study on interest rate restrictions in the EU: Final Report, [http://ec.europa.eu/internal\\_market/finances-retail/docs/credit/irr\\_report\\_en.pdf](http://ec.europa.eu/internal_market/finances-retail/docs/credit/irr_report_en.pdf)  
 Australian Government, National Consumer Credit Protection Act 2009, Section 32A, <https://www.legislation.gov.au/Details/C2017C00196>  
 World Bank, Interest Rate Caps around the World, <http://documents.worldbank.org/curated/en/876751468149083943/pdf/WPS7070.pdf>

**B.** Clarify how the Criminal Code maximum rate of borrowing is calculated and enforced

In Alberta, the Cost of Credit Disclosure Regulation utilizes the annual percentage rate (APR) as the measure when communicating cost of borrowing. The APR calculation is set in a national template adopted by all provinces and the federal government under national trade agreements. Section 347 of the *Criminal Code*, however, uses the effective annual rate (EAR) to express interest rates. Though similar, EAR and APR are calculated differently, and thus produce different numbers. For example, a 60 per cent EAR can equate to a 47.9 per cent APR.<sup>16</sup>

9. Samuel Munzele Maimbo and Claudia Alejandra Henriquez Gallegos, Interest Rate Caps around the World: Still Popular, but a Blunt Instrument (World Bank Finance and Markets Global Practice Group, 2014), 6, <https://openknowledge.worldbank.org/bitstream/handle/10986/20494/WPS7070.pdf?sequence=1&isAllowed=y>.  
 10. Ibid.  
 11. Joe Fantauzzi, Predatory Lending: A Survey of High Interest Alternative Financial Service Users (Toronto: Canadian Centre for Policy Alternatives Ontario Office and ACORN Canada, 2016), 17, <https://www.policyalternatives.ca/sites/default/files/uploads/publications/Ontario%20Office/2016/12/CCPA-ON%20predatory%20lending%20Dec%201.pdf>.  
 12. Bill S-19, An Act to amend the Criminal Code (criminal interest rate), 1st sess., 38th Parliament, 2004, [http://www.parl.ca/Content/Bills/381/Private/S-19/S-19\\_1/S-19\\_1.PDF](http://www.parl.ca/Content/Bills/381/Private/S-19/S-19_1/S-19_1.PDF).  
 13. Center for Responsible Lending, Issue Brief: Interest rate cap protects families, communities and economies (2009), <http://www.responsiblelending.org/payday-lending/policy-legislation/congress/payday-and-the-economy.pdf>.  
 14. Protecting Consumers from Unreasonable Credit Rates Act of 2009, S. 500, 111th Cong., <https://www.govtrack.us/congress/bills/111/s500>.  
 15. Center for Responsible Lending, Research Brief: 36% cap Survey (2009), <http://www.responsiblelending.org/research-publication/interest-rate-survey>.  
 16. Denise Barrett Consulting, Consumer Experiences with Rent-to-Own (Toronto: Consumers Council of Canada, 2016), 49 [http://www.consumerscouncil.com/site/consumers\\_council\\_of\\_canada/assets/pdf/ccc\\_rent\\_to\\_own\\_web.pdf](http://www.consumerscouncil.com/site/consumers_council_of_canada/assets/pdf/ccc_rent_to_own_web.pdf).

This inconsistency results in confusion and legal ambiguity, particularly when potential infringements are noted by or reported to the province, and then forwarded to relevant police services. A review of the national standard for APR and EAR, undertaken in collaboration with the provinces and territories, would provide the opportunity to achieve consistency in cost of borrowing calculations across all jurisdictions that regulate, monitor and enforce consumer protection.

A review of the federal usury law would also provide the opportunity to clarify to which credit arrangements and agreements the law applies. For example, it is unclear whether the federal usury law applies to financing mechanisms like rent-to-own. To account for existing, emerging and future forms of credit, it would be most effective to define credit in the broadest sense possible. The current list of exceptions to what constitutes interest should also be revised. For example, the *Criminal Code* lists cost of insurance as an exception; however, the cost of insurance merits inclusion in criminal interest calculations given its impact on cost of borrowing in many high-cost credit agreements.

**C.** Equip law enforcement with the knowledge, tools and resources to enforce rules effectively

Section 347 of the *Criminal Code* identifies that charging more than 60 per cent annual interest is punishable by a fine and jail time.<sup>17</sup> However, there appear to be cases of lenders offering credit at annual interest rates above the 60 per cent maximum. Of particular concern are pawn loans and rent-to-own.<sup>18</sup> The Government of Canada should provide clarity with regard to the application and enforcement of section 347 by issuing communications that identify how interest is calculated, to which products and services the maximum rate applies, how lenders must adhere to the *Criminal Code* and the consequences for not doing so.

Governments must also ensure that law enforcement (e.g., RCMP; local police forces; provincial and federal regulators such as the Financial Consumer Agency of Canada; and the civil and criminal courts) has the tools, resources and mandate to enforce the *Criminal Code*.

## 2. Mandate a standardized Financial Facts Label

Similar to the nutritional labels found on all food packages, a Financial Facts Label<sup>19</sup> is a standardized box that displays financial information about a credit product, such as loan amount, annual interest rate, fees, payment amounts and total cost of borrowing. By ensuring that all relevant information is presented in a clear and standardized way, the label strengthens the cost disclosure practices of businesses, and enables consumers to easily compare credit products and companies across the marketplace.

To improve existing disclosure requirements, the Government of Canada should mandate the inclusion of a standardized Financial Facts Label on the front page of contracts and on all advertising materials, for federally-regulated financial services. We encourage the provinces and territories to do the same for all products and services that fall within their purview, ensuring that the mandated labels are uniform across jurisdictions.<sup>20</sup> For further information pertaining to the Financial Facts Label, please see the section of recommendations for the Government of Alberta.

17. R.S.C., 1985, c. C-46, s.347(1), <http://laws-lois.justice.gc.ca/PDF/C-46.pdf>.

18. An analysis of high-cost credit contracts, conducted for Momentum by a fellow of the Canadian Institute of Actuaries, revealed interest rates ranging from 24% to 2334%. To access the full report, contact Momentum. Denise Barrett Consulting, Consumer Experiences with Rent-to-Own (Toronto: Consumers Council of Canada, 2016), 49 [http://www.consumerscouncil.com/site/consumers\\_council\\_of\\_canada/assets/pdf/ccc\\_rent\\_to\\_own\\_web.pdf](http://www.consumerscouncil.com/site/consumers_council_of_canada/assets/pdf/ccc_rent_to_own_web.pdf).

19. José Quiñonez, Vivian Pacheco, and Eva Orbuch, Just the financial facts, please! A Secret Survey of Financial Services in San Francisco's Mission District (San Francisco: Mission Asset Fund, 2010), [http://policylinkcontent.s3.amazonaws.com/JustTheFinancialFactsPlease\\_MissionAssetFund\\_0.pdf](http://policylinkcontent.s3.amazonaws.com/JustTheFinancialFactsPlease_MissionAssetFund_0.pdf)

20. Canadian Literacy and Learning Network, St. Christopher House, Momentum, SEED Winnipeg, and SEDI, Toward a Comprehensive and Inclusive Consumer Protection Framework for Canada – Submission to Finance Canada (2014), <https://www.fin.gc.ca/consultresp/fcpf-cpcpsf/076-fcpf-cpcpsf.pdf>.

### 3. Improve access to basic financial services and credit products through the Bank Act

Banks play a vital role in supporting the financial health of Canadians. However, unlike some credit unions, banks do not presently provide access to affordable small dollar loans as an alternative to high-cost credit.<sup>21</sup>

The Bank Act and the Access to Basic Banking Services Regulations outline that banks have a responsibility to make basic banking services available to all Canadians. Many interpret the term ‘banking’ to mean only basic deposit accounts, rather than a fuller suite of financial services; yet, in Canadian society today, access to a broad range of financial services including credit, is basic. Accordingly, banks must assume greater responsibility for meeting the financial needs of all Canadians—particularly individuals living on a low income—which includes offering safe and affordable alternatives to high-cost credit. Research indicates that if provided with clear, consistent regulations, banks and credit unions can profitably make such loans at prices that are six to eight times lower than those offered by payday lenders.<sup>22</sup>

## Government of Alberta

### 1. License all businesses that provide high-cost alternative financial services

Too little is known about an industry that has such significant repercussions for the financial health of individuals and communities, and this is due, at least partially, to a lack of licensing. In Alberta, payday lenders are licensed provincially, and cities such as Calgary license pawnbrokers; however, many of the high-cost alternative services outlined in our research are not licensed at all.

Despite the documented challenges many consumers experience with high-cost lenders,<sup>23</sup> they do not often file complaints. Licensing all high-cost lenders would extend the province’s ability to enforce rules beyond the existing consumer complaint process by enabling the investigation of businesses through audits. This would allow regulatory bodies and law enforcement to handle infractions proactively and with greater effectiveness. Licensing all high-cost lenders would also provide the Government of Alberta with better data, and thus a deeper understanding of the high-cost credit industry.

The Government of Alberta should specifically license rent-to-own stores, instalment lenders, title lenders, pawnbrokers and cheque cashers; however, licensing requirements should be broad enough to apply to forms of high-cost credit that may emerge in the future. In Canada, several jurisdictions require lenders (in addition to payday lenders) to be licensed, including: Quebec,<sup>24</sup> Manitoba,<sup>25</sup> Saskatchewan<sup>26</sup> and Nova Scotia.<sup>27</sup>

21. Janet McFarland and Tavia Grant, “Payday loans: What are the alternatives?” The Globe and Mail, May 15, 2015, <http://webcache.googleusercontent.com/search?q=cache:8sgubTZTitcJ:https://www.theglobeandmail.com/report-on-business/payday-loans-what-are-the-alternatives/article24463099/&num=1&hl=en&gl=ca&strip=0&vwsrc=0>

22. The Pew Charitable Trusts, “Pew Identifies 4 Risks in Shift to Payday Installment Lending,” press release, August 11, 2016, <http://www.pewtrusts.org/en/about/news-room/press-releases/2016/08/11/pew-identifies-4-risks-in-shift-to-payday-installment-lending>.

23. Momentum, High-Cost Alternative Financial Services: The Customer Experience (Calgary: 2017), <http://www.momentum.org/files/Publications/Part%20-%20Experiences%20with%20High%20Cost%20Financial%20Services.pdf>.

24. Consumer Protection Act, s. 321, <http://legisquebec.gouv.qc.ca/en/pdf/cs/P-40.1.pdf>.

25. The Consumer Protection Amendment Act (High-Cost Credit Products), Bill 34, As Passed April 14, 2016 (Manitoba, 40th Leg., 3rd sess.), <https://web2.gov.mb.ca/bills/40-3/pdf/b034.pdf>.

26. Trust and Loan Corporations Act, 1997, c.T-22.2, s.17(1), <http://www.qp.gov.sk.ca/documents/English/Statutes/Statutes/T22-2.pdf>; note that Saskatchewan does not specifically license high-cost lenders, but instead requires that any corporation that carries on business of lending money and is lending to Saskatchewan residents needs to be licensed as a financing corporation under the Trust and Loan Corporations Act.

27. Consumer Protection Act, 1989, R.S., c. 92, s. 11(1), <http://nslegislature.ca/legc/statutes/consumer%20protection.pdf>.

## 2. Create a provincial Financial Empowerment Fund

In cities across the province, Financial Empowerment<sup>28</sup> programs are already helping families to reduce debt, increase income and savings, and build assets. In doing so, they are addressing the root causes that lead individuals to access high-cost credit in the first place. In addition, Financial Empowerment Collaboratives in Edmonton and Calgary are exploring systemic issues like barriers to banking and access to safe and affordable financial products.

We recommend that high-cost lenders contribute annually to a Financial Empowerment Fund, potentially through licensing fees, to boost the potential and reach of Financial Empowerment<sup>29</sup> initiatives in Alberta. For example, the Fund could support access to impartial financial counselling for social assistance recipients in Alberta. In Manitoba, high-cost lenders must make an annual contribution of \$500 to the Manitoba Borrowers' Financial Literacy Fund, which supports programs and activities intended to improve the financial literacy of borrowers and potential borrowers.<sup>30</sup>

| <b>FINANCIAL FACTS</b>                      |               |
|---|---------------|
| Loan amount                                 | \$5000        |
| Loan term                                   | 12 months     |
| <hr/>                                       |               |
| Annual interest rate*                       | 59.9%         |
| Monthly Payment                             | \$249.58      |
| Total fees                                  | \$0           |
| Insurance fee                               | \$0           |
| Late payment fee                            | \$15.50       |
| <hr/>                                       |               |
| Percentage of budget going to loan payment* | 12.5%         |
| <hr/>                                       |               |
| <b>Total cost of borrowing per year:</b>    | <b>\$2995</b> |
| <hr/>                                       |               |
| *Based on a monthly net income of \$2000    |               |

## 3. Mandate a standardized Financial Facts Label

Evidence suggests that disclosure can have a positive impact on the financial choices of consumers. One American study found that disclosing how payday loan fees add up over time, and what repayment looks like on average, resulted in less borrowing, and that communicating the cost of borrowing in terms of dollars, rather than through a percentage, resulted in a reduction in borrowing of 23 per cent.<sup>31</sup> Another study specific to the rent-to-

own industry found that total cost disclosure laws had an impact on a borrower's decision making process, as borrowers in states with such laws were less likely to use rent-to-own to purchase an item.<sup>32</sup>

Behavioural research indicates that financial product disclosures are most effective in aiding decision making when they are short and simple, standardized, clear about risks and benefits, meaningful, well-presented and tested.<sup>33</sup> A Financial Facts Label is one approach to effective disclosure. Like the nutritional labels found on all food packages, a Financial Facts Label<sup>34</sup> is a standardized box that displays

financial information about a product, such as loan amount, annual interest rate, fees, payment amounts, total cost of borrowing and late penalties. For rent-to-own contracts, an effective Financial Facts Label would also incorporate aspects of rent-to-own disclosure rules such as displaying the "buy it now price,"<sup>35</sup> as is done in states such as California<sup>36</sup> and New Hampshire.<sup>37</sup>

28. United Way of Calgary and Area, "Financial Empowerment," accessed September 10, 2017, <http://www.calgaryunitedway.org/financial-empowerment-yyc>.

29. Ibid.

30. Government of Manitoba, "High-Cost Credit Products," accessed September 10, 2017, [https://www.gov.mb.ca/cca/cpo/pdf/high\\_cost\\_credit\\_grantor\\_licence.pdf](https://www.gov.mb.ca/cca/cpo/pdf/high_cost_credit_grantor_licence.pdf)

31. Marianne Bertrand and Adair Morse, "Information Disclosure, Cognitive Biases, and Payday Borrowing," Working Paper, (Chicago: Booth School of Business, University of Chicago, 2010), cited in Signe-Mary McKernan, Caroline Ratcliffe, and Daniel Kuehn, Prohibitions, Price Caps, and Disclosures: A Look at State Policies and Alternative Financial Product Use, (Washington D.C.: Urban Institute, 2010), 7, [http://web.law.columbia.edu/sites/default/files/microsites/transactional-studies/files/9PDL\\_McKernan\\_Ratcliffe\\_and\\_Kuehn\\_2010\\_Prohibitions-Price-Caps-and-Disclosures.pdf](http://web.law.columbia.edu/sites/default/files/microsites/transactional-studies/files/9PDL_McKernan_Ratcliffe_and_Kuehn_2010_Prohibitions-Price-Caps-and-Disclosures.pdf)

32. Ibid.

33. New Zealand, Ministry of Business, Innovation & Employment, Financial Product Disclosure: Insights from Behavioural Economics, report prepared by Kirsty Johnston, Christine Tether, and Ashley Tomlinson, Occasional Paper 15/01 (2015), iii-iv, [http://www.mbie.govt.nz/publication\\_s-research/publications/economic-development/2015-occasional-papers/Financial%20product%20disclosure%20insights%20from%20behavioural%20economics.pdf](http://www.mbie.govt.nz/publication_s-research/publications/economic-development/2015-occasional-papers/Financial%20product%20disclosure%20insights%20from%20behavioural%20economics.pdf).

34. Quiñonez, Pacheco, and Orbuch, Just the financial facts, please!

35. The buy it now price refers to the cost of buying the item upfront from the rent-to-own store.

36. California Department of Consumer Affairs, "Rent-to-Own Transactions in California: Legal Guide S-10," accessed on September 10, 2017, [http://www.dca.ca.gov/publications/legal\\_guides/s-10.shtml](http://www.dca.ca.gov/publications/legal_guides/s-10.shtml).

37. New Hampshire Department of Justice, "Consumer Sourcebook – Rent-to-Own," accessed on September 10, 2017, <https://www.doj.nh.gov/consumer/sourcebook/rent-to-own.htm>.

#### **4. Advocate for and participate in the creation of a pan-Canadian consumer protection strategy**

In Canada, all three levels of government oversee consumer protection laws and regulate aspects of the high-cost credit industry. To improve the effectiveness of these frameworks, the Government of Alberta should advocate for the creation of a pan-Canadian consumer protection strategy. This inter-jurisdictional strategy would be most effective if developed collaboratively, and should also involve consultations with Canadians. A pan-Canadian consumer protection strategy should address the following three recommendations:

- A.** Review and strengthen federal usury laws, in consultation with Canadians
- B.** Clarify how the Criminal Code maximum rate of borrowing is calculated and enforced
- C.** Equip law enforcement with the knowledge, tools and resources to enforce rules effectively

For further discussion of this recommendation, please see the section pertaining to the Government of Canada.

#### **5. Reduce the cost of cheque cashing, and support employers to offer direct deposit**

Though cheque cashing services offer customers quick and convenient access to funds without holds, the fees imposed can be significant for vulnerable customers, particularly in the case of large cheques. For example, the cost to cash a cheque in Alberta can be as high as \$3.50 plus 3.5 per cent of the cheque's face value. That is nearly \$60 for an Assured Income for the Severely Handicapped (AISH) client to cash their monthly benefit cheque.

The Government of Alberta's decision to make direct deposit mandatory for Income Support payments, and the Government of Canada's work to encourage direct deposit for all payments, has significantly reduced the number of people who use cheque cashers to access government benefits. To build on this progress, and to better protect those who continue to take government cheques (and others) to cheque cashers, the Government of Alberta should place a limit on allowable fees for cheque cashing. To do so, the Government of Alberta should consider existing and proposed caps in other provinces:

- Manitoba: \$3.00, plus two per cent of cheque's face value (for government cheques)
- Quebec: prohibits charges for the cashing of government cheques
- Ontario: draft regulations suggest a limit of the lesser between \$2.00 plus one per cent of the cheque's face value, and \$10.00 (for government cheques)

#### **6. Prohibit solicitation of additional loans and refinancing options**

Borrowers often report that once they have paid off a loan, lenders engage in aggressive sales tactics in order to get them to revisit a store and reborrow. In addition, lenders frequently promote refinancing options to borrowers with outstanding loans. It is well documented that payday and instalment lending businesses profit from repeat customers, and thus such businesses dedicate significant resources to the solicitation of additional loans and refinancing options. Pressure to refinance—specifically in the case of instalment and auto loans—is particularly concerning, as it extends the period over which a borrower must repay a loan, and often results in a higher cost of borrowing.

The Government of Alberta should prohibit high-cost lenders from soliciting additional loans and refinancing options. Presently, Ontario is looking at prohibiting contact to solicit refinancing on instalment loans. Albertans would benefit from the same. This is based on the rationale that refinancing an instalment loan may unnecessarily extend the indebtedness of the consumer, particularly if refinancing involves additional fees. By prohibiting solicitation of refinancing and additional loans, the Government of Alberta can protect consumers from this risk.

## 7. Introduce price caps for rent-to-own contracts

Rent-to-own stores routinely lend above standard retail prices, sometimes by as much as four times.<sup>38</sup> In fact, a rent-to-own store in Calgary lists an Amana refrigerator for \$1993, yet a similar refrigerator is available from Home Depot for \$698 – a third of the cost.<sup>39</sup>

Section 6(2)(d) of Alberta's *Fair Trading Act* prevents businesses from charging a price that "grossly exceeds the price at which similar goods or services are readily available without informing the consumer of the difference in price and the reason for the difference." However, several barriers exist to enforcing this provision, as "grossly excessive" is not defined in the legislation, and the province often only learns of infringements if a consumer complaint is made.

To address these issues, the Government of Alberta should introduce a price cap specific to rent-to-own contracts, expressed in relation to the standard retail value of the item (either the Manufacturers Suggested Price or Suggested Retail Price). Introducing a price cap for rent-to-own contracts would provide legal clarity beyond "grossly excessive," and would reduce, in some cases significantly, the cost of rent-to-own financing.

Six American states have established price caps for rent-to-own products, the most stringent of which is two times the buy-it-now price.<sup>40</sup> A price cap is also being considered for rent-to-own financing in the United Kingdom, where a limit was recently introduced for payday loans.<sup>41</sup>

## 8. Require reinstatement rights in rent-to-own and title loan contracts

In the case of title loans and rent-to-own financing, borrowers face the possibility of losing an asset in which they have invested a significant amount if they miss a payment or if their contract becomes delinquent. Reinstatement rights allow borrowers to reinstate a contract by remitting payments that are past due, and by paying late fees.

Ontario is considering mandating the provision of reinstatement rights, as well as a grace period before late fees can be charged.<sup>42</sup> The Consumers Council of Canada reports that the two largest rent-to-own businesses in Canada include reinstatement rights in contracts, but that store managers are provided discretion in carrying out this provision.<sup>43</sup> All American states require rent-to-own contracts to include reinstatement rights, though the nature of these rights varies by state (anywhere between 21 to 180 days after an item has been returned).<sup>44</sup> In addition, many states allow businesses to charge a reinstatement fee, often of five dollars.<sup>45</sup>

38. Denise Barrett Consulting, Consumer Experiences with Rent-to-Own, 6.

39. Home Depot, "Amana 16 cu. ft. Top Freezer Refrigerator in White," <https://www.homedepot.ca/en/home/p.16-cu-ft-top-freezer-refrigerator-in-white.1000812971.html>.

40. Association of Progressive Rental Organizations, Rent-to-own Rules and Regulations, (2017), 2, [https://www.rtohq.org/wp-content/uploads/2016/04/RTORulesRegs\\_APRO2017.pdf](https://www.rtohq.org/wp-content/uploads/2016/04/RTORulesRegs_APRO2017.pdf).

41. UK Financial Conduct Authority, Call for Input: High-cost credit, Including review of the high-cost short-term credit price cap, (2016), <https://fca.org.uk/publication/call-for-input/call-input-high-cost-short-term-credit.pdf>.

42. Ontario, Ministry of Government and Consumer Services, Strengthening Protection for Consumers of Alternative Financial Services – Phase One, Consultation Paper (2017), 24, <http://www.ontariocanada.com/registry/showAttachment.do?postingId=24431&attachmentId=34584>.

43. Denise Barrett Consulting, Consumer Experiences with Rent-to-Own, 70.

44. Association of Progressive Rental Organizations, Rent-to-own Rules and Regulations, 10.

45. Ontario Ministry of Government and Consumer Services, Strengthening Protection for Consumers of Alternative Financial Services, 25.

## 9. Require lenders to assess a borrower's ability to repay

When deciding upon loan amounts and terms, as well as whether to lend at all, responsible lenders consider if and how the borrowers will be able to pay a loan off. High-cost lenders should take a borrower's circumstances—including income level, debt load and monthly expenses—into account when determining the size of a loan. Governments in Ontario,<sup>46</sup> Quebec,<sup>47</sup> British Columbia<sup>48</sup> and the United States<sup>49</sup> have either adopted or are considering rules that require high-cost lenders to assess a borrower's ability to repay a loan, and which also restrict loan amounts based on a borrower's income level.

The Government of Alberta should also introduce rules that require lenders to assess a borrower's ability to repay. Specifically, laws should require high-cost lenders to calculate a borrower's expected net income over the proposed term of the loan, and then calculate a maximum loan amount based on a set percentage of income. Ontario, for example, is exploring a maximum loan amount of 40 per cent of net income,<sup>50</sup> and The PEW Charitable Trusts (United States) proposes a maximum of 5 per cent of a borrower's income.<sup>51</sup> Australia has recommended changing the cap on the total amount of all repayments, from 20 per cent of the consumer's gross income to 10 per cent of the consumer's net income.

Though such policy may limit who qualifies for a loan and how much they qualify for, this can be positive in the long term. A recent study out of The Ohio State University suggests that limiting the supply of payday loans can have a positive effect on those who typically access them. In the study, habitual borrowers displayed a reduction in financial distress when payday lending was restricted.<sup>52</sup>

## Municipal Government

The City of Calgary has shown great leadership on the issue of high-cost credit, most recently in introducing new licensing and land use rules for payday lenders. These successes should be built upon, and similar policies applied to the variety of high-cost services identified in Momentum's research. For example, the City of Calgary should license all providers of high-cost alternative financial services, establish a minimum distancing requirement to prevent the clustering of these businesses in low-income neighbourhoods, improve disclosure requirements and mandate that financial literacy information be provided to customers.

The City of Calgary should also consider ways it might support all employers to adopt direct deposit in an effort to curb cheque cashing fees. The Current CSF campaign for electronic pay is a successful example of government collaborating with employers to encourage direct deposit.<sup>53</sup> Launched by the City of San Francisco's Office of Financial Empowerment, the campaign is focused on partnering with employers to increase the number of workers paid through direct deposit. Encouraging employers to use direct deposit to nudge people to open bank accounts and reduce their reliance on cheque cashers is also a successful Financial Empowerment intervention under the Safe Financial Products pillar.<sup>54</sup>

46. Ibid, 5-6.

47. An Act mainly to modernize rules relating to consumer credit and to regulate debt settlement service contracts, high-cost credit contracts and loyalty programs, Bill 134, (Quebec, 41st Leg., 1st sess.), sec. 103.2 [http://www.assnat.qc.ca/Media/Process.aspx?MediaId=ANQ\\_Vigile.Bil.DocumentGenerique\\_129323en&process=Default&token=ZyMoxNwUn8ikQ+TRKYwPCjWrKwg+viv9rjij7p3xLGTZDmLVSmJLoqe/vG7/YWzz](http://www.assnat.qc.ca/Media/Process.aspx?MediaId=ANQ_Vigile.Bil.DocumentGenerique_129323en&process=Default&token=ZyMoxNwUn8ikQ+TRKYwPCjWrKwg+viv9rjij7p3xLGTZDmLVSmJLoqe/vG7/YWzz)

48. British Columbia Ministry of Public Safety and Solicitor General, "High-Cost Alternative Financial Services Stakeholder Consultation – September 2016," accessed September 11, 2017, <https://forms.gov.bc.ca/content/uploads/sites/5/2016/09/high-cost-alt-fin-serv-consult.pdf>.

49. The Pew Charitable Trusts, "Pew Identifies 4 Risks in Shift to Payday Installment Lending," accessed on September 11, 2017, <http://www.pewtrusts.org/en/about/news-room/press-releases/2016/08/11/pew-identifies-4-risks-in-shift-to-payday-installment-lending>

50. Ontario Ministry of Government and Consumer Services, Strengthening Protection for Consumers of Alternative Financial Services, 6.

51. The Pew Charitable Trusts, "Pew Identifies 4 Risks in Shift to Payday Installment Lending."

52. Brian Baugh, "Payday borrowing and household outcomes: Evidence from a natural experiment," Fisher College of Business, The Ohio State University, 1, <https://www.smu.edu/~media/Site/Cox/Departments/Finance/FINASeminarSeries/Payday-borrowing-and-household-outcomes.ashx?a=en>

53. San Francisco Office of Financial Empowerment, "Current CSF," accessed on September 11, 2017, <http://currentcsf.org/>.

54. Prosper Canada, "Safe Financial Products," accessed on September 11, 2017, <http://prospercanada.org/Financial-Empowerment/Safe-Financial-Products.aspx>.

## FURTHER CONSIDERATIONS

Momentum recognizes that government regulation, although important, is not the only solution to the issues presented by high-cost credit. Concerns regarding the potential consequences of regulation merit consideration, and other approaches—such as enhancing financial literacy and increasing access to safe and affordable alternatives—must also be adopted to address these issues.

One expressed-concern is that increased regulation will result in less profitability for the industry, which may cause some lenders to close their doors, thus reducing the supply of credit. If fewer credit options exist, some critics fear that vulnerable borrowers will turn to unregulated markets, including the online marketplace. However, this frequently-cited concern is not demonstrated in research. In fact, there is evidence that fewer high-cost credit options simply leads to less borrowing—an important change for those for whom a loan is not a good idea.<sup>55</sup>

The complex issue of high-cost credit requires a comprehensive response spanning sectors and stakeholder groups. Banks and credit unions can and must do much more to reduce barriers to banking, improve access to low-interest credit for emergencies and create a viable alternative to high-cost lenders.<sup>56</sup> The charitable sector should support the scaling up and availability of financial empowerment programs, and should continue to provide social programs and resources, which can often act as an alternative to a loan. Consumers also have a role to play, and can do so by increasing their financial literacy, reducing their debt levels and increasing their credit scores. Together, and in partnership with government, these groups can facilitate the creation of more affordable financial products, which is an integral step in preventing Canadians from falling into dangerous debt traps and increasing financial inclusion. Finally, it bears repeating that the recommendations outlined in this brief are not exhaustive; rather, they represent an important step in our shared work to improve consumer protection and reduce poverty in our communities.

55. The Pew Charitable Trusts, *Fraud and Abuse Online: Harmful Practices in Internet Payday Lending*, (2014), 20 [http://www.pewtrusts.org/~media/assets/2014/10/payday-lending-report/fraud\\_and\\_abuse\\_online\\_harmful\\_practices\\_in\\_internet\\_payday\\_lending.pdf](http://www.pewtrusts.org/~media/assets/2014/10/payday-lending-report/fraud_and_abuse_online_harmful_practices_in_internet_payday_lending.pdf); Baugh, "Payday borrowing and household outcomes," 1.

56. ACORN Canada, *It's Expensive to be Poor: How Canadian Banks are Failing Low-Income Communities*, (2016), <https://www.acorncanada.org/resource/its-expensive-be-poor-how-canadian-banks-are-failing-low-income-communities>.

## Appendix A

|                         | <b>Recent Changes to High-Cost Credit Rules in Canada<br/>(implemented and proposed)</b>   |
|-------------------------|--|
| <b>Manitoba</b>         | <p><b>The Consumer Protection Act - High-Cost Credit Products Regulation<sup>1</sup></b></p> <ul style="list-style-type: none"> <li>• Came into force in September 2016</li> <li>• Provides a definition of high-cost credit products</li> <li>• Requires high-cost credit lenders to be licensed through the Consumer Protection Office, and to pay an annual licensing fee, as well as an annual financial literacy support levy</li> <li>• Sets out specific disclosure requirements for high-cost lenders</li> </ul>   |
| <b>Quebec</b>           | <p><b>Bill 134 – An Act mainly to modernize rules relating to consumer credit and to regulate debt settlement service contracts, high-cost credit contracts and loyalty programs<sup>2</sup></b></p> <ul style="list-style-type: none"> <li>• Introduced in May 2017 to modernize the Consumer Protection Act, and to outline new rights for consumers</li> <li>• Proposes a new regime for high-cost credit</li> <li>• Includes new licensing requirements for high-cost lenders, requires providers of consumer credit to assess a borrower’s capacity to repay a loan, and introduces new restrictions on advertising.</li> <li>• Bill 134 will be reviewed by a parliamentary committee, and could be adopted in late 2017.</li> </ul>   |
| <b>British Columbia</b> | <p><b>Business Practices and Consumer Protection Act - Payday Loans Regulation<sup>3</sup></b></p> <ul style="list-style-type: none"> <li>• Reduced, effective January 2017, the maximum cost of borrowing to \$17 per \$100 (previously \$23 per \$100)</li> </ul> <p><b>High-Cost Alternative Financial Services Stakeholder Consultation<sup>4</sup></b></p> <ul style="list-style-type: none"> <li>• Launched in September 2016 by the B.C. Ministry of Public Safety and Solicitor General</li> <li>• Objective is to obtain input from stakeholders regarding existing consumer protections for British Columbians who use high-cost alternative financial services (e.g., instalment and vehicle title loans, rent-to-own sales, and cheque cashing services)</li> <li>• Input will inform the ministry’s review of high-cost alternative services in the province</li> </ul> |
| <b>Ontario</b>          | <p><b>Ontario Ministry of Government and Consumer Services - Strengthening Protection for Consumers of Alternative Financial Services - Phase One<sup>5</sup></b></p> <ul style="list-style-type: none"> <li>• Consultation paper introduced in summer 2017</li> <li>• Outlines draft regulations for payday lending and cheque cashing</li> <li>• Presents areas for further consideration, specifically strengthened regulation of high-cost credit products</li> <li>• Discussion includes instalment loans and rent-to-own agreements</li> <li>• A Phase 2 consultation paper is expected in fall 2017</li> </ul>  |

1. High-Cost Credit Products Regulation, C200 — M.R. 7/2016, [http://web2.gov.mb.ca/laws/regs/current/\\_pdf-regs.php?reg=7/2016](http://web2.gov.mb.ca/laws/regs/current/_pdf-regs.php?reg=7/2016).

2. An Act mainly to modernize rules relating to consumer credit and to regulate debt settlement service contracts, high-cost credit contracts and loyalty programs.

3. Payday Loans Regulation, [http://www.bclaws.ca/Recon/document/ID/freeside/16\\_57\\_2009#section18](http://www.bclaws.ca/Recon/document/ID/freeside/16_57_2009#section18).

4. British Columbia, Ministry of Public Safety and Solicitor General, “High-Cost Alternative Financial Services Stakeholder Consultation – September 2016,” <https://forms.gov.bc.ca/content/uploads/sites/5/2016/09/high-cost-alt-fin-serv-consult.pdf>

5. Ministry of Government and Consumer Services, Strengthening Protection for Consumers of Alternative Financial Services – Phase One.