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# THE FISCAL NOTE

An Examination of Tax and Fiscal Matters  
By the Arizona Free Enterprise Club

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## Payday loans serve constituency

Should government outlaw how much someone pays for a sofa on eBay or Craigslist? Or something more rare, like a Ty Cobb rookie card? Of course not. The terms of a private (and legal) transaction between two parties are not government's business. It makes no difference whether someone pays \$20,000 for the sofa or the card.

The same logic applies to payday loans (short term loans or cash advances). The industry provides a product for a price. No one is forced to use this option—or any option for that matter—to secure a loan. But payday lending will not continue to be an option unless the Arizona legislature and governor agree to extend the framework under which the industry currently exists.

## Background

Arizona's deferred presentment licensing program (payday lending industry) is regulated by the Arizona Department of Financial Institutions under Arizona Revised Statutes Title 6, Chapter 12.1. It was created in 2000 and expires on July 1, 2010. This sunset date effectively kills the industry. Next year the Legislature will consider legislation which restructures the economics of the payday product and adds regulation designed to address the concerns raised about borrowers borrowing too often. While we disagree with the need for additional regulations—the market seems to have done a good job so far—this is a deal worth making.

## Payday loans: An alternative

Payday loans aren't necessarily the first choice for those in need of cash, but like banks, credit unions, and credit cards, payday loans fill a niche. According to the Texas Public Policy Foundation, 40 percent of low-income Texans who used payday loans said they were turned away by banks or credit unions. Half of

payday loan users needed cash to pay bills, 46 percent needed money for gas or groceries, and more than 33 percent said they were faced with an emergency.

Opponents of payday lending argue that the current fee and interest structure are too steep for consumers. They claim that the annual percentage rates charged on payday loans should be capped at 36 percent. In other words, opponents believe that people need to be protected from the industry. This is nonsense. Loans from cash advance centers are not annual loans. Payday loans are limited to a maximum of \$500 with a repayment period of between five days and thirty days, and the loan cannot be rolled over more than three times. The fees associated with this type of loan are clearly competitive if only measured by the fact that it's a \$40 billion a year industry. If the fees associated with payday lending were too high, the industry would not survive. Thus, the fees and rates are exactly where they should be in the current marketplace.

### Competition

The average payday loan customer is lower-income and higher-risk than most borrowers. Most banks and credit unions willingly choose not to enter into this market. Markets change, however. Credit unions are devising products to meet the needs of some of their members who utilize payday loans. According to *Arizona Republic* columnist Russ Wiles, nearly 200 of Alhambra Credit Union's 3,600 members use payday loans. That was enough to motivate Alhambra to come up with a product designed to meet the short term borrowing needs of their customers. This is the market at work.

### Conclusion

Payday lending might not be everyone's cup of tea. That doesn't mean the industry should be put out of business. In a free market, and especially in the current economic climate, policymakers should do what they can to ensure that for those who have credit needs all viable options remain open.



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