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Segregated Communities: Segregated Finance

Institute on Metropolitan Opportunity
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Research, Education and Advocacy

Segregated Communities: Segregated Finance

An Analysis of Race, Income and Small Consumer Loans in Minneapolis-St. Paul, MN, Portland, OR and Seattle, WA

A Report to the Northwest Area Foundation

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Segregated Communities: Segregated Finance[1]

The racial composition of neighborhoods is related to access to good, affordable credit. In low income communities of color, high cost loans— both in the home mortgage market and small consumer loan market—are much more common than they are in white and middle-class communities. Poor people of color pay more for loans—an extra cost that many families can ill-afford.

Previous work by the Institute on Race and Poverty documented a dual credit market in the Twin Cities mortgage markets—where even high-income people living in neighborhoods of color were overwhelmingly likely to apply for and receive subprime loans and even low income people living in white segregated communities were overwhelmingly likely to apply for and receive prime loans.

This research looks at the geographic and legal landscape of consumer credit: Access to small loans, commonly known as payday loans, in the three largest metropolitan regions in the North West Area Foundation's service area: Minneapolis-St. Paul, Seattle, and Portland.

Geography and Payday Lending: Race Affects the Concentration of High Cost Lenders

The Minneapolis-St. Paul, Seattle and Portland metropolitan areas have different geographies of income and race- leading to differential access to both credit and payday lending across the metropolitan regions:

- In all three metros it is clear that racially segregated communities of color fared the worst in terms of accessing banks and having more lenders that charge very high interest rates for small loan products, such as payday lenders, check cashers and pawnshops. This is especially evident in Minneapolis-St. Paul where non-white segregated census tracts are more numerous and concentrated in the lower-income core of the region.

- Communities of color have better access to banks in less segregated metropolitan regions. There are fewer segregated neighborhoods in Portland and Seattle, and there are an abundance of banks in racially integrated areas in these regions.

- Lower income neighborhoods also had disproportionate shares of non-conventional lenders and residential neighborhoods of the central cities had comparably fewer banks than elsewhere in the region, but these differences were not as stark as in non-white segregated neighborhoods.

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Law and Payday Lending: Effective Regulation

The legal restraints on payday lending affect the concentration of payday lenders in all metropolitan regions. The restriction that appears to most effectively limit the proliferation of payday lenders is interest rate and fee caps.

- Washington allows the highest cost payday loans- and, unsurprisingly has the greatest number of payday lenders. Although Washington has aggressive laws that attempt to limit loan rollovers—where borrowers end up taking out payday loans to repay payday loans—these industry-supported provisions seem to do little to limit the proliferation of payday lending.

- Minnesota has historically required lower-cost payday loans, and, correspondingly, has fewer payday lenders. The discovery of a loophole in payday lending regulation—the state's industrial thrift act—has increased the maximum cost of payday loans in Minnesota and encouraged the expansion of payday lenders in the region.

- Oregon has the most stringent requirements for payday lenders of the group—limiting both the cost and duration of loans—although payday lending in not banned in the state.

Recommendations

While the bans on roll-over and "cooling off" periods between payday loans tend to be easier to pass in state legislatures—these bills tend to be supported by the payday loan industry—rate caps are the most effective means of reducing the cost of payday lending. Likewise, increasing the amount of consumer disclosures, or increasing efforts to educate consumers about the cost of these loans, has not been shown to effectively reduce the harms of high-cost lending.

Ineffective Regulation:

- Cooling-off Periods: Borrowers and lenders easily circumvent cooling off periods between loans, rendering even fairly sophisticated attempts to stop loan roll-overs ineffective.

- Consumer Disclosures: There is little evidence that consumer disclosures or consumer education effectively changes consumer behavior.

Effective Regulation:

- Rate Caps: After a Department of Defense Study found that payday lending was harming military readiness, Congress passed, and George W. Bush signed a law that prohibits lenders from charging more than 36 percent APR to active-duty military families. Research by consumer advocacy groups, such as the Center for Responsible Lending have also found that a 36 percent rate cap on payday loans was the most effective way to prevent consumers from becoming trapped in an ever-growing debt cycle.

- Create Alternative to Payday Loans: Encouraging traditional lenders, banks, and credit unions to offer affordable short term credit to low income consumers will provide a safe alternative to high-cost payday loans.

Fix the Safety Net:

- High—or moderate—cost loans cannot resolve the problem of increasing economic security for lower and even middle income Americans.[2] Payday and other predatory lending and the attendant consequences for families and communities will remain until real fixes to the social safety-net are implemented.

I. Introduction

With economic times the way they are now it is becoming harder for everyone to makes ends meet; some are going to a payday loan to get them by till next payday. There is another way but one must be very careful to recognize if it is a possibility. ***You can ask for a raise****. When I say you must be careful, I mean you should tread lightly and realize if you really deserve a raise or if you just think you deserve a raise, and if your company can even afford to give you a raise right now. ... And remember if you do get a "No," or even if you get a "Yes," but are not able to make bills on time, a* ***payday loan*** *may be what you need to get through.*[3]

Payday loans are short-term, high cost loans that, depending on your perspective, are trapping America's working poor in an ever-deepening cycle of debt or providing needed short-term credit. The reality is probably both assertions are true; although, the very fact that America's working poor have to acquire high-cost credit to survive may indicate deeper problems with our economic safety-net. Research by reputable scholars, as well as consumer groups has found that most payday consumers take out not one, but many payday loans. This type of borrowing is very expensive for families, destabilizing their already fragile economic position and increasing their likelihood of becoming bankrupt- among other negative outcomes. Nonetheless, families do have economic shortfalls, sudden expenses, such a medical bills or car repairs are often greater than families' immediate resources and short-term loans allow families to get necessary medical treatment, keep utilities on and cars running.

A predominate reason borrowers use payday loans is to deal with unexpected expenses.[4] Payday loans are not the only method that families have to get over these income shortfalls. Families facing unexpected expenses use their own savings, credit cards, borrow from friends or relatives, renegotiate bills or payment with utilities and creditors, and take out short term loans from banks and credit unions. Most people do not take out payday loans. In fact in 2007 only 2.9 percent of the population used payday loans.[5] Most payday borrowers are unmarried women and have a

[2]Historically, states have developed usury laws during times when the income inequality is high. Glaeser (1994).
[3] Quote from: http://personalmoneystore.com/moneyblog/2009/01/26/pay-raise-or-payday-loan-you-decide/ last accessed 05/29/2009.
[4] Half of payday borrowers use the money to cover emergencies or basic consumptive needs- including food and shelter. Logan and Weller (2009) at 11.
[5] Logan and Weller (2009) at 4 Data from the Federal Reserve's triennial Survey of Consumer Finances.

high school, but no college degree.[6] The mean family income of payday borrowers was $32,614 in 2007.[7] In other words, the average payday borrower is a member of the working poor- their income is too much to be eligible for public benefits and they make too little to cushion their families from the sort of financial shocks, like medical expenses, that are common in our economy.

Because of consumers' need for short-term credit and a lessening of restrictions on payday lending in many states, payday lending has exploded. In the 1990s, payday lending was a somewhat rare phenomenon. Today, there are now more payday lenders in the United States than McDonald's, Burger King, Sears, J.C. Penney, and Target stores combined. [8] The growth in payday lending is mirrored by a growing discontent about the economic effects of these high cost loans on consumers. In particular, payday lending is suspected of having its greatest impact in segregated neighborhoods of color- where individuals have historically had a hard time accessing traditional credit and where people are most vulnerable to economic upheaval. State payday lending regulations and the geography of metropolitan regions can lead to a greater or lesser concentration of payday lenders in a metropolitan region. Past research has indicated a correlation between race and the use of payday lenders.[9]

This research looks at the geographic and legal landscape of payday lending in the three largest metropolitan regions in the North West Area Foundation's service area: Minneapolis-St. Paul, Seattle, and Portland. While none of the states encompassing these metropolitan regions allows unfettered payday lending, none completely bans it either. Likewise, the three metros differ by income and race- leading to differential access to both credit and payday lending across the metropolitan regions.

II. Small, High Priced Consumer Loans: Payday Loans and Check Cashing

A. Payday Borrowers

The vast majority of low income Americans have bank accounts. About 75 percent of families earning less than $18,900 and about 87 percent of families earning between $18,000 and $33,900 per year have bank accounts.[10] These banked households, however, face a banking and credit system that is poorly equipped to help them manage their family finances. The financial services that low income households with bank accounts receive are expensive—families often pay very high overdraft and minimum balance fees because low income families have constrained family incomes and a limited supply of credit.[11] Even low income families with bank accounts often turn to high-cost alternative financial services providers, such as pawnshops, payday lenders,

[6] Logan and Weller (2009) (4) Data from the Federal Reserve's triennial Survey of Consumer Finances.
[7] Iid at 7. The median income was $30,892. The Mean and median family incomes for non-payday borrowers were $ 85,473 and $ 48,397 respectively.
[8] Karger, 2005.
[9] Stegman and Faris, 2001, 2005, also King, Li, Davis, and Ernst (2005); Mahon (2005).
[10] Bucks (2006)
[11] See Barr (2008) at 6.

rent-to-own stores, and tax refund lenders to fulfill their day-to-day banking needs, such as cashing checks and paying bills.

Alternative financial services providers provide banking services to banked and unbanked people who are poorly served by the traditional banking structure. These families are, by definition, low income, have few assets and many have poor or no credit, meaning that they have little money to invest in banks and lenders see them as high risk. When these families experience financial shortfalls, because of unexpected bills (usually car repairs or medical expenses) or unexpected income short falls (job loss or hour reduction), they are often unable to meet all of their financial obligations. For these families, the tradeoffs become untenable: Pay for the car repair (otherwise, I cannot get to work), pay for the electric bill (or my power will be shut off), or pay my rent (or I will be evicted). For the working poor who are facing impossible financial decisions, payday lending seems like a rescue plan.

In truth, however, most payday borrowers have several options other than payday loans, including negotiations with utility companies, loans from friends or family, or even pay advances from their employers. Payday lending is often, however, the most convenient, albeit the most expensive, method of overcoming financial shortfalls. The problem is that these loans usually often become middle-to-long term debt, with disabling costs. The average borrower pays back about $793 for a $325 loan.[12]

B. The cost of payday lending

Payday loans are, by definition, small consumer loans; state law usually sets the maximum loan amount. Loans generally range from $300 to $500. In exchange for the loan the borrower turns over a postdated check for the amount of the loan and fee. The fee for a typical $325 payday loan is set by state law, but averages about $52.[13] Because most borrowers turn over their loans, the average payday borrower enters a cycle of at least five loans prior to default or payoff. As a result, that fee gets paid many times while renewing the same loan.[14]

Loan turnover occurs because borrowers cannot afford to pay back the loan in its entirety when it becomes due. Payday customers are often unable to repay loans when they come due. This is not surprising given the very short term of the loan and the financial profile of the borrowers. In some states, borrowers can pay another finance fee and renew the loan. In states that ostensibly prohibit turnover, borrowers repay the entirety of the loan; the payday lender then reissues the loan and returns the money with subtraction of additional finance charges.[15]

For example, when a customer takes out of $325 payday loan, she writes a $325 postdated check to the lender and receives $273 (the amount minus the finance charges). She then comes back in two weeks, when the loan is due, with another $325, and receives $221. In two weeks, she again brings in $325 and receives $169. When she attempts the seventh turnover, she can no longer get

[12] King et al. (2006)
[13] Logan and Walker (2009) at 2.
[14] Center for Responsible Lending (2009);
[15] Occasionally there is a twenty-four hour or more waiting period. Research shows that even in states with waiting periods, payday loans are often renewed because borrowers simply cannot afford to pay them off.

any money back- the finance charge is larger than the loan principle, she has paid $312 and still owes $325.

The Center for Responsible Lending estimates that of the 17 million payday borrowers, 12 million became trapped in a cycle of repeat loans for at least five lending periods. The Center calculated that this amounts to $4.2 billions dollars in excess fees every year.[16]

Payday borrowing is associated with delayed medical care,[17] increased evictions,[18] credit card delinquencies,[19] involuntary bank account closures,[20] and bankruptcy.[21] For example, Paige Skiba of Vanderbilt law school and Jeremy Tobacman of the Wharton School found that receiving a payday loan for the first time increases a borrower's risk of entering bankruptcy by 2.48 percentage points.[22] Likewise, Michael Barr of Michigan Law School found that payday borrowers, compared to similarly-situated non-payday borrowers, were three times more likely to enter bankruptcy, twice as likely to be evicted, and three times more likely to have their utilities shut off.[23]

Research conducted using the records of a large Texas payday lender found that over half of payday borrowers default- although most paid fees equaling 90 percent of their loan principle plus the principle itself.[24] Payday lenders argue that high default rates justify the high costs of these loans. In fact, payday lending may be no more profitable than any other business – even with high fees and large profits margins on a product with little overhead.[25] However, the argument that extremely high interest rates are needed assumes that default rates would not be substantially lower if interest costs were lower. If it is the high rates and fees themselves that cause the high default rates (by generating exorbitant costs above and beyond the principle and normal interest), then the same set of loans might be supportable at a lower interest rate with lower default rates. Experimental programs like North Carolina State Employee Credit Union's Salary Advance Loan program (described below) could be used to test this proposition.

C. The regulation of payday lending

As recently as the 1980s, payday lending was effectively banned in most states. The ban on payday loans arose in the first part of the twentieth century in an effort to control loan sharking. Loan sharking was the practice of issuing short-term, high cost loans, with triple digit interest rates. These loans often became long-term, debt. While loan sharks usually did not resort to violence to secure repayment of these loans, they did turn to the courts to force repayment. These

[16] King, 2006.
[17] Melzer (2008).
[18] Barr 2008)
[19] Aragwal et al. (2009)
[20] Campbell at al .(2008).
[21] Skiba and Tobacman (2008).
[22] Skiba and Tobacman (2008).
[23] Barr (2008).
[24] Skiba and Tobacman (2008).
[25] De Young and Phillis (2009).

lenders used a variety of fictions to make the loans, and often characterized them as "salary assignments."[26]

The practice of salary assignment and loan sharking was largely eliminated by the Russell Sage Foundation's Small Loan law, which was adopted by most states. Under the law, states licensed small consumer lenders and allowed both small lenders and mainstream lenders to make short term loans with interest rates ranging from 24 to 42 percent per year. These regulations stayed in place through the 1970s. After the Supreme Court's decision in National First Bank v. Omaha Service Corporation, however, federal and state chartered banks were effectively no longer constrained by usury laws.

State usury laws still constrained small consumer lenders. These lenders began to lobby state legislators to legalize very high interest rates on payday loans. Payday loans are, effectively, salary assignments, the borrower promises to turn over future earnings for a present loan. Salary assignment, however, is illegal under federal law.[27] State legislators, instead legalized a form of salary assignment where borrowers give lenders a post-dated check, rather than a promise of future earnings to secure the loan. Further, instead of legalizing triple-digit interest rates, states legalized fees on loans that amounted to triple-digit interest rates.[28]

Payday lenders argue that high maximum APRs on payday loans should not worry states because the high loan rates will be driven down by market competition. Research, however, has shown that this is not the case. Payday loan fees (or interest rates) usually end-up with loan prices near the statutory maximum- even when there is ample market competition.[29]

Minnesota

Minnesota has allowed payday lending since 1995, albeit with somewhat more restrictive interest requirements than many other states.[30] Minnesota's payday lending law has a complex tiered system of fees.[31] The maximum allowed fee under the small loans statute depends on the amount of the loan, and is a percentage of the loan plus an add–on fee. Overall, for a loan of $325, the law allows a finance charge of $24.50, which translates in to a 197 percent annual percentage rate (APR) on a loan with a term of two weeks.[32]

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[26] National Consumer Law Center (1995)
[27] 16 C.F.R. § 444.2(a)(3).
[28] Peterson (2008).
[29] Further, in places with high concentrations of payday lenders in Colorado, loan fees (and APRs) were highest. In places with fewer payday lenders, loan prices were somewhat lower- indicating that payday lenders compete with other sources of credit and not necessarily with each other. DeYoung and Phillips (2009)
[30] 1995 Minnesota Session Laws, Chapter 202, Article 3, Section 2.
[31] Loans up to and including $50, can be assessed up to $5.50 in fees, amounts to an APR of 287% on a loan of $50. Loans between $50 and $100 can incur a fee of ten percent of the loan plus a $5 fee, this allows of $15 fee on $100 which is a 390 percent APR on a two week loan. Loans between $ 100 and $250 can be assessed a seven percent plus $5 fee, amounting to $22.50 on a $250 loan and 192 % APR. For loan between $250 and $350, a six percent plus $5 fee can be assess, this is a $26 fee on an amount of $350 and an APR of 193 %.
[32] We use Annual Percentage Rates (APR) to calculate the total cost of loans because it is a standard measure that allows us to compare the relative cost of one loan to another.

Minnesota's law originally required a 30 day loan.[33] This meant that initially, payday loan costs in Minnesota were quite a bit lower. For example, a finance charge of $24.50 on a $325 loan on a month-to-month term would be an 82 percent APR. The year after payday lending was legalized in Minnesota, the law was changed to require a 30 day *maximum* loan period.[34] In comparison to the rest of the country, these payday loan APRs are relatively low and may account for the slower growth of payday lending in the Twin Cities region. Payday lending, however, is now growing rapidly. This is a result of larger market players entering the Minnesota market and lenders' use of a different statute, to conduct higher-fee payday lending.

As payday lenders reach total market saturation in some states or are legally barred from operating in other states, national payday lenders have taken a greater interest in entering the Minnesota market. Advance America, the South Carolina-based lending mammoth has been steadily lobbying for higher fees and interest rates in order to facilitate its spread into the Minnesota market.[35] One national Chain (Ace Cash Express) is now present in Minnesota. Technically, however, Ace Cash Express is an Industrial Thrift and it makes industrial consumer loans rather than payday loans. This means that these stores can charge more for loans (and thus make greater profits) and make loans for more than $350.

Industrial consumer loans and payday loans (small consumer loans) are very nearly the same thing- both carry extremely high APRs and are usually issued for a term of around two weeks. The difference is in the total amount that the lender can lend and the total fees the lender can charge. Several years ago, payday lenders in Minnesota began reorganizing as state-chartered "industrial thrifts," a loophole in state regulation that allowed them to charge more for payday loans. This increased both the cost of payday loans to borrowers and the profits of lenders.

Industrial thrifts are allowed to assess a finance charge of 21.75 percent APR or, 33 percent APR on amounts less than $750, and 19 percent APR on the balance over $750. Added on to this finance charge, which is calculated as APR, are other fees that Minnesota law defines are not part of the finance charge. These fees include an annual charge of $50 per loan,[36] a $30 charge for obtaining a cash advance,[37] and a $25 administrative fee.[38]

Different industrial thrifts seem to interpret these add-on fees differently. For example, Payday America, a Minnesota Industrial Thrift appears to charge about 33.5 percent interest on amounts up to $900, plus a $25-$30 "advance charge," plus an annual fee between $2 and $50.[39] This amounts to APRs, as stated by the company, between 262 and 737 percent. (In this case, the company seems to be using interest, plus the open ended credit fees). The Unloan company on the other hand, also a Minnesota industrial thrift, charges 33 percent APR on loans up to $500, plus a $25 dollar administrative fee.[40] While Unloan does not calculate the APR,[41] it amounts to

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[33] 1995 Minnesota Session Laws Chapter 202, Article 3, Section 2.
[34] 1996 Minnesota Session Laws, Chapter 414, Article 2, Section 7.
[35] H.J. Cummins, "Legislators Seek to Curtail "Payday Lending" Practices," Star Tribune Feb. 23, 2008.
[36] Minnesota Statues Section 47.59 subdivision 6 (c) (1)).
[37] Minnesota Statutes, Section 47.59 subdivision 6 (c)(4)).
[38] Minnesota Statutes, Section 47.59, subdivision 6 (d).
[39] *www.payday America.net* last accessed 05/21/2009
[40] *www.unloan.com/howitworks2.asp* last accessed 05/21/2009.

about $33.94 on a $325 two-week loan, which is about a 272 percent APR. In this case, it appears that the thrift views payday loans as "close-ended credit."

Regardless of the type of payday loan, small consumer or industrial consumer, payday loan companies in Minnesota will generally not "rollover" loans- meaning that the payday customer has to bring in the amount of money owed on the date that is it due. The lender will then issue a new loan for the same amount of money. Minnesota does not allow rollovers, although the small consumer loan law does allow the company to charge a 5 percent interest rate on a past due loan.[42] Likewise, an industrial consumer loan could be extended at the appropriate APR. The reason why lenders generally do not offer this option to customers is that it is less profitable. In renewing rather than extending the term of the loan, the companies get to recharge the finance fees.

Oregon

Payday lending in Oregon was licensed by the state in 2001, and became a $250 million dollar industry by 2004. In 2004, the Oregon Division of Finance and Corporate Security conducted a survey of payday borrowers and an examination of payday lenders. This examination found that Oregonians were using payday loans to purchase food and pay basic bills, that the average borrower took out nine loans per year from single lenders, and that payday borrowers were paying over 500 percent APR on an average $380 loan.[43] Consumer advocacy groups, such as OSPIRG (Oregon State Public Research Group) did further consumer studies and publicized the high payday APRs and the fact that Oregonians were using these loans to pay for basic necessities, such as food. In response, numerous cities, including Portland, Gresham, Silverton and Eugene, passed ordinances in 2005 and 2006 which limited the ability of payday lenders to operate within city limits.

In 2006, Oregon passed comprehensive payday lending reform.[44] Oregon law now caps all consumer loans, including payday and title loans. For loans with a term of 31 to 60 days, the interest rate is capped at 36 percent per year plus a one time fee of $30 or $10 for every $100 of the loan, whichever is less.[45] Interest rates on consumer loans over 60 days are capped at 30

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[41] The Industrial Thrift Act specifically exempts these additional finance fees from calculation into APR. (Minnesota Statutes Section 47.59 subdivision 3 (d)(2). The law does require industrial thrifts to warn customers that they have been assessed additional fees, outside of the APR. Minnesota Statutes, Section 47.59. Subdivision. 12..

[42] Minnesota Statues, Section 47.57, subdivision 6 (4).

[43] Oregon Division of Finance and Corporate Securities, "Payday Loans in Oregon." Available at http://dfcs.oregon.gov/cf/fact_sheet.html (2006).

[44] The law took effect in 2007.

[45] Oregon Revised Statutes, section 725.615. After the Oregon Legislature passed this legislation, 91 of the state's 354 payday lenders applied for a "conventional" license, in an attempt to circumvent the payday lending restrictions. Oregon Department of Consumer and Business Services, press release, "Oregon takes additional steps to protect consumers from high-cost loans" Sept. 21, 2006. To prevent lenders from evading the new interest rate caps, OSPIRG worked together with groups such as Our Oregon, AARP, SEIU Local 503, Lutheran Advocacy Ministry, Ecumenical Ministries, and Oregon Law Center to advocate a package of bills to extend the interest rate caps to all consumer finance lending. (cite) Oregon both adopted rate caps for all small consumer loans and defined payday lenders as lenders who make ten percent or more of their loans are for durations of less than 60 days. Oregon Revised Statute section 725.600.

percentage points above the Federal Reserve's discount rate.[46] This means a borrower pays a maximum of $39.94 for a $325 payday loan. If the term of the loan is the 31 day statutory minimum, the APR on this loan is 147 percent.[47]

The new law allows a lender to renew an existing payday loan up to two times after the first loan is made.[48] Lenders are allowed to charge interest on the renewal, but they may not charge any additional origination fees. Lenders may not make new payday loans (other than renewals) the day the loan expires or during the six days before and the six days after the date on which a payday loan expires. This prohibition on the issuance of new loans should effectively prevent side-door loan turnovers—where consumers (and lenders) avoid restrictions on turnovers by requiring borrowers to “repay” the loan and then immediately reissuing the loan. Without this prohibition, side-door turnovers could, because of new origination fees, lead to higher cost loans than intended by statute. The law does not require lenders to renew loans, but if a borrower did renew a $325 loan, she would pay $9.94 for the first renewal, and $9.94 for the second renewal, at which point she would be prohibited from taking renewing again.[49] The total amount owed in fees and interest would be $59.82, along with a principle of $325. The APR on this loan is 72 percent.[50]

Washington

In 2005, the major newspaper in the Seattle region, the Post-Intelligencer, released a series of news reports and analysis on payday lending in the Seattle-Tacoma area.[51] The report found payday lenders clustered near neighborhoods with high concentrations of poverty, high concentrations of Blacks, and near the Fort Lewis Military Reservation. Statistical analysis found that controlling for population, income, poverty rates, and education, there was a pattern of association between places where Blacks and military employees lived and payday lenders.[52]

Nonetheless, efforts to reign-in Washington States’ burgeoning payday lending business have accomplished little and the number of loans made to Washington consumers has increased steadily. In 2007, payday lenders made nearly $1.5 billion dollars worth of loans.[53] An analysis by the Washington Department of Financial Services (DFI) found that about 80 percent of Washington payday borrowers took out more than one payday loan and more than 50 percent of borrowers took out five or more payday loans from any one lender.[54] The average payday loan

[46] For loans with a term of greater than 60 day, the federal reserve interest rate was 0.44, so these loans were capped at 36 percent.
[47] The highest maximum APR is on a loan of 300, that APR would be 157 percent. (300(.36)) Interest for payday loans is computed on a 365-day factor or, in a leap year, a 366-day factor. Oregon Administrative Rules 441-730-0160 and 441-730-0270.
[48] Oregon Revised Statutes, section 725.622.
[49] Oregon Administrative Rule 441-730-0270 prohibits compounding interest on payday loans.
[50] (((59.82/91)365)/325))= 0.72
[51] Phong Cat Le, “Payday Loans Offer Fast Help – at a Price” Seattle Post Intelligencer, May 24, 2005.
[52] Ibid
[53] Washinton State Department of Financial Institutions, 2007 Payday Lending Report p 3.
[54] Washington State Department of Financial Institutions, 2007 Payday Lending Report pp. 4-5. This data was based on information collected from Washington’s 20 licensees that has more than 10 million in loans and were required to provide data and 14 licensees who provided data voluntarily. These 34 companies

was $424.39, and 82 percent of loans were less than three weeks in duration. Forty-eight percent of loans were 14 days or less in duration.[55]

Payday borrowing restrictions in Washington cover the gamut of possibilities. However, the state allows fairly high interest rates, about 390% APR on a $300-two week loan. Payday loans in Washington must be accompanied by a written note giving the customer a calculation of interest in terms of APR, as defined by the Truth in Lending Act. The maximum aggregate payday loan is $700 plus fees, the maximum loan term is forty-five days, and there is no minimum loan term.[56] Payday loan fees are capped at 15 percent of the first $500 –$45 on a $300 dollar loan and $75 on a $500 loan.[57] For amounts in excess of $500, the fee cap is 10 percent.[58] This means that a maximum loan of $700 can carry up to a $95 fee. This amounts to 390 percent APR on a typical $424- two week payday loan.[59]

Payday lenders are prohibited from rolling-over loans.[60] Customers have the right to covert their loan into a repayment plan after four successive loans, but prior to default.[61] Payday lenders are obligated to provide customers notice of their right to repayment plan which, under the statute lasts for 60 days and provides for at least three payments, spaced at substantially equivalent intervals.[62] The lender is allowed to charge the customer a one-time fee for the payment plan of the amount equivalent to the fee for taking out a payday loan of the same amount.[63] This means that the fee to convert a payday loan into a payment plan can be up to $63 on a $424 loan, equivalent to a 90 percent APR.[64] If the customer defaults on a payment plan, the lender is entitled to charge an additional $25 and to initiate collection action.[65] Customers must also be notified of their right to rescission—the right to terminate the loan within a certain amount of time . Nonetheless, only 13 percent of Washington borrowers used repayment plans in 2007.

In May of 2009, the Washington legislature passed new restrictions on payday lending. This bill ties the length of the loan term to the individual's pay date, effectively setting a minimum loan period of seven days.[66] The maximum loan is set at $700 or 30 percent of the borrower's gross monthly income.[67] Lenders are now prohibited from lending to borrowers who have taken out eight payday loans from any lender in a 12 month period, who are on a payment (installment) plan or who have defaulted on a payday loan in the last two years. Most significantly, the bill

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[55] DFI 2007 (from 88% percent of licensees).
[56] Revised Code of Washington , section 31.45.073 (2)
[57] Revised Code of Washington, section 31.43.073(3). The statute caps "interest or fees" and allows the director of The Washington Department of Financial Institutions to determine which fees are not subject to the interest/fee cap.
[58] Revised Code of Washington, section 31.45.073(3).
[59] (63.60(52/2))/300 = 390
[60] Revised Code of Washington, section 31.04 . In fact, lenders are prohibited from issuing loans to pay back loans even from other lenders, and Washington keeps a database of loans.
[61] Revised Code of Washington, section 31.45.084
[62] Revised Code of Washington, section 31.04 et seq.
[63] Revised Code of Washington , section 31.45.084
[64] (63.60 X (360/60))/300 = 0.90
[65] Revised Code of Washington, section 31.45.084. Lenders are, however, prohibited from charging any fee for the dishonored or "bounced" check. Ibid.
[66] If the next pay date is less than seven days away, the law requires the loan's due date to be the borrower's second pay date.
[67] Washington House Bill 1709 (2009)

changes the terms of repayment plans, eliminating the fees and extending the payment period to ninety days for loans up to $400, and 180 days for larger loans.[68] Equally significantly, the new bill does not lower payday lending fees.[69]

Cross-state Comparisons

Washington allows the highest charges and interest rates for payday lenders of the three states. A fee on a $325 loan is $48.75 and the APR for a two week loan is 348 percent, twice that of Oregon. (Table 1) Oregon has the most stringent requirements for payday lenders of the group. Minnesota has lower fees that the other two states, but has larger APRs than Oregon. In Minnesota small lenders that are regulated as industry and thrifts actually charge a higher fee and have much higher APRs than regulated small lenders. Payday lenders also do not have minimum loan terms required by the State of Minnesota.

Table 1: Fees and Interest Rates of Payday Lenders

	Fee on a $325 Payday Loan	Minimum loan term	APR 2 week loan
Minnesota	$ 24.50 (small lender)	none	197 %
	$ 33.94 (thrift)		272 %
Washington	$ 48.75	7 days	348 %
Oregon	$ 39.94	31 days	149 %

Minnesota, Oregon, and Washington all require lenders to comply with federal Truth-in Lending disclosures. In all states, this includes informing the customer of the APR, through posted signs, materials given to consumer at the time of the loan or both. Minnesota even requires lenders to tell borrowers that they could get the same loan for less elsewhere. Yet, the number of payday lenders—and payday borrowers—is steadily increasing.

The impact that state law and regulation has on the how many payday lenders there are in a region and how they are distributed across neighborhoods becomes more complex in areas that are near state borders. For instance, the Portland, Oregon metropolitan region straddles the State of Washington and more lenient payday lender regulations in Washington has led to a proliferation in payday lenders in the Washington State portion of the Portland region. Lenient payday lending regulation can also lead to a proliferation in payday lending stores in areas that lack conventional lenders such as banks and credit unions. In such cases, payday lenders could be more apt to locate in places that lack conventional lenders, such as low-income neighborhoods and neighborhoods that are predominately people of color.

[68] The bill also changes the term "payment plan" as well, converting it into "installment plan."
[69] The original version of the bill set a minimum loan term of 60 days, lowered the fee to 10% of the amount loans. This amounts to $30 on a $300 loan and 60% APR- the reduction in APR is mostly due to the extended loan term. The original bill seems to be substantially altered by a substitute bill offered by the same authors as the original bill.

III. Analysis of Lender Locations

A leading reason people choose a lending establishment is location. According to the Federal Reserve Board's Survey of Consumer Finances, in 2007 almost half of those surveyed said that the location of the institution was the top reason for choosing a place for their main checking account, a reason that has increased in importance over the last ten years.[70] Surveys of people using non-traditional lenders, such as check cashers, also often reported using an establishment because of its convenient location.[71]

Given that people often choose lenders according to their location, it is important to consider whether different types of lenders are distributed evenly across a region or whether they favor certain neighborhoods. This study compares three metropolitan areas--Minneapolis-St. Paul, Portland and Seattle and analyzes the distribution of lenders according to the income and racial composition of neighborhoods.

The analysis shows that segregated communities of color have poor access to neighborhood banks and have far more non-conventional types of lenders that charge much higher rates for small loans. Racially segregated communities of color tend to have fewer banks, more check cashers and payday lenders, especially in Minneapolis-St. Paul where non-white segregated census tracts are more numerous and concentrated in the lower-income core of the region. In contrast, there are fewer segregated neighborhoods in Portland and Seattle, and racially integrated areas, places with an abundance of banks.

Low income neighborhoods have an abundance of all types of lenders, both bank and payday establishments. The abundance of lenders in low income neighborhoods is due in large part to their central locations near regional job centers and in areas near or accessible to higher income neighborhoods. This is particularly true in Portland and Seattle. The advantages of a central location, however, diminish when potential high income customers are distant from the core of the region. This is the case in Minneapolis-St. Paul where there are far fewer banks in the residential portions of the central cities and low income neighborhoods.

The regulation of small loan establishments also greatly impacts the number and distribution of payday stores in a region. The State of Washington has more leniently regulated payday lenders and as a result, Seattle has many more payday establishments than credit unions; twice as many per capita payday lenders as Portland and four times as many as Minneapolis-St. Paul.

The leniency of regulation in Washington has also affected the distribution of payday lenders in Portland, which is partly in the state. The Washington portion of the Portland metropolitan area contains only 18 percent of the region's population, but over 57 percent of the region's payday lenders. Notably, payday lenders in all three metropolitan areas are located nearby major highway corridors, in an attempt to service residents from distant communities.

[70] Federal Reserve Board (2009),.
[71] Seidman, Hababou and Kramer (2005.

A. Methods

This work uses 2008 lending establishment data from Reference USA for the Minneapolis-St. Paul, Portland and Seattle metropolitan areas. Establishments were selected in Reference USA using the primary standard industrial classification (SIC) code for banks, credit unions, check cashing services, pawnshops and loan services. Payday lenders were determined by cross referencing data from Reference USA with the state regulated small lender lists in Minnesota, Oregon and Washington.[72]

Business establishments in Reference USA are coded by latitude and longitude. This location data was used in geographic information systems (GIS) to map the bulk of establishment locations. There were a few occurrences where the regulated small lender lists yielded records not found in Reference USA. In such cases the records were added to the data set used in the analysis. There were also some cases where check cashers and pawnshops in Reference USA listed "loans" as a secondary industry classification. In such cases a web-search was performed and the establishments were included with the bulk of the records when they advertised payday loans on their website.

The study mapped the location of *conventional lenders,* such as banks and credit unions and *non-conventional lenders*, such as payday lenders, other check cashing services and pawnshops. U.S. Census data for the household income, racial demographics and census tract boundaries were used to generate statistics combining lender data with population data. GIS was used to overlay the locations onto census tracts in order to determine the share of the establishments in low- to moderate income and racially integrated and segregated neighborhoods.

Lending establishments and population demographics of central business districts (CBDs) were not analyzed in the report. The assumption is that banks in the CBDs are more likely oriented towards businesses and workers than residents, and thus are categorically different from banks servicing residential areas. Additionally, CBDs have dramatically disproportionate shares of banks and would skew the neighborhoods analysis.[73]

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[72] Small lender lists were collected from the Minnesota Department of Commerce, the Oregon Department of Consumer and Business Services and the Washington State Department of Financial Institutions. In Minnesota we cross-referenced the small lender list and industry and thrift to select payday lenders.

[73] For instance, Seattle's CBDs have 2% of regional population and 18% of the region's banks. There were also large discrepancies between different neighborhood types. For instance, in Minneapolis-St. Paul census tracts with 30 to 50 percent people of color, 69% of banks were in the CBDs, compared to only 7% of the tracts' population.

B. Map Analysis

In this section, median household income, percentage people of color and lending establishments are mapped for each metropolitan area. This analysis focuses on the location and share of lenders within different types of neighborhoods in each of the metros.

Neighborhood (census tract) incomes are scaled by regional household income to control for the fact that the three regions differ by income. Low income neighborhoods (defined as census tracts with less than 80 percent of the regional median income) are the focus of the analysis.[74] These types of Low income tracts are more likely to have households facing financial difficulties and households receiving assistance through government programs. For comparison purposes, tracts with 80 to 100 percent of regional median income are also assessed.

Neighborhoods are also classified by race for the analysis. Racially integrated neighborhoods are defined as tracts with 30 to 49 percent people of color. Racially segregated neighborhoods are those with more then 50 percent people of color. Racially segregated neighborhoods have faced lending discrimination and neighborhood disinvestment, and are often the lowest income areas in metropolitan areas. They merit attention for civil rights and fair lending reasons. Integrated neighborhoods are also given attention because they are often in transition, experiencing re-segregation and economic disinvestment.

Finally, the distribution of lenders across different types of municipalities is examined. The community classification groups municipalities based on their fiscal characteristics, including tax base, poverty, population density, jobs per household, age of the housing stock and population growth. The characteristics were chosen to provide a snapshot of communities in two dimensions—the ability to raise revenues from local tax bases and the costs associated with its social and physical needs of residents.[75]

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[74]The 80 percent cut-off is higher than that used in most work. Low income was initially defined as 50 percent or less of regional median income, but this yielded few neighborhoods for analysis.

[75] The characteristics used to group the municipalities were property tax base per household (2003), poverty rate (2000), household growth (1993 to 2003) and household density (2003), jobs per household (2003), and median age of the housing stock (2000). All variables were standardized--expressed as the number of standard deviations from the mean--to minimize scale effects. Grouping was accomplished using the K-means clustering procedure in SPSS. For more on cluster analysis in general, and K-means clustering in particular, see StatSoft, Inc. Electronic Statistics Textbook (Tulsa, OK: StatSoft, 2002) at www.statsoft.com/textbook/stathome.html.

1. Minneapolis-St. Paul

Low income households and people of color are concentrated in the core of the Minneapolis-St. Paul region. These areas have a smaller share of the region's banks, but had much greater shares of non-conventional lenders, including payday lenders, check cashers and pawnshops. Racially integrated and non-white segregated neighborhoods have disproportionately few banks—their shares of regional banks are generally less than half their population shares. Non-white segregated neighborhoods show very high shares of non-conventional lenders, especially check cashers. Similarly, central cities and fiscally stressed or at-risk suburban areas also have smaller regional shares of banks than people, but have larger shares of non-conventional lenders.

Income- In Minneapolis-St. Paul low income neighborhoods (tracts with median income less than $43,400) are concentrated in the central cities and in several inner ring suburbs. (Map 1) There are also some lower income neighborhoods in the rural periphery of the metropolitan area but they represent relatively few households. An important characteristic of the overall pattern is that most low income tracts are distant from higher income tracts, which are very sparsely represented in the central cities and inner suburbs.

Race- Census tracts with high proportions of people of color are largely concentrated in the cities of Minneapolis and St. Paul. (Map 2) There are also concentrations of people of color to the north of Minneapolis in Brooklyn Center and Brooklyn Park, and to the south of Minneapolis in Richfield and Bloomington. Integrated neighborhoods often surround segregated neighborhoods, and most are rapidly transitioning into segregated neighborhoods.[76] There are more non-white segregated tracts (68) than integrated tracts (51) in the two cities.

Conventional Lenders- Banks and credit unions cluster near the CBDs and near major highways. (Map 3) It is noteworthy that there a relatively few banks and credit unions north of the Minneapolis CBD, south of the Minneapolis CBD along the 35W corridor, and east of the St. Paul CBD, all places with lower incomes and higher percentages of people of color.

Non-Conventional Lenders- Non-conventional establishments are more centrally located than banks and credit unions, with only a scattering of payday lending establishments in the periphery of the region. (Map 4) Most of these non-traditional lenders are located in the cities of Minneapolis and St. Paul, although there is a cluster of payday lenders in the southern suburbs, lining up south of Minneapolis along the 35W corridor and in the north in Fridley and Blaine.

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[76] See Orfield, Gumus-Dawes, Luce and Finn, (2009).

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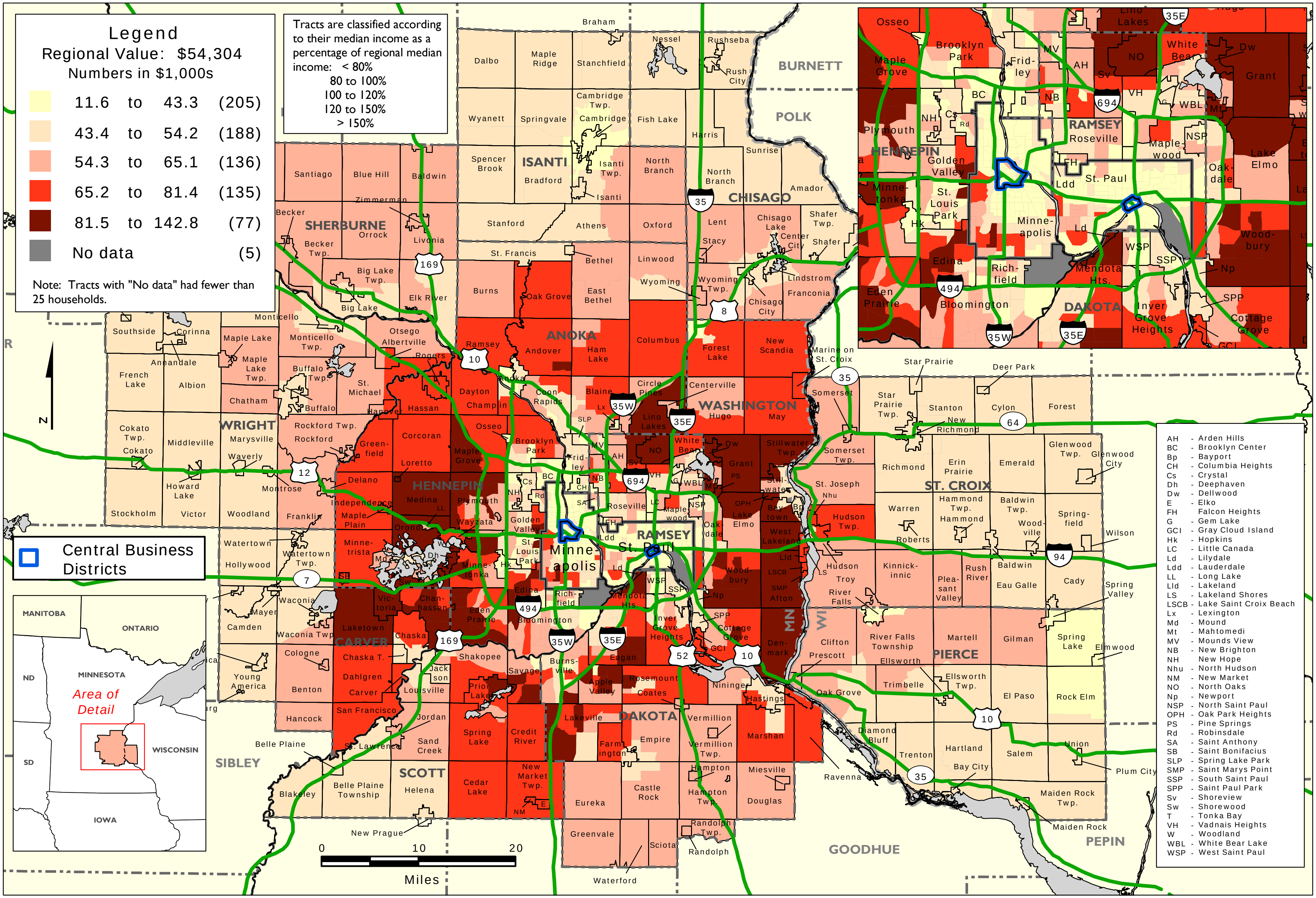
Map 1: MINNEAPOLIS - SAINT PAUL REGION
Median Household Income by Census Tract, 1999



Data Source: U.S. Census Bureau

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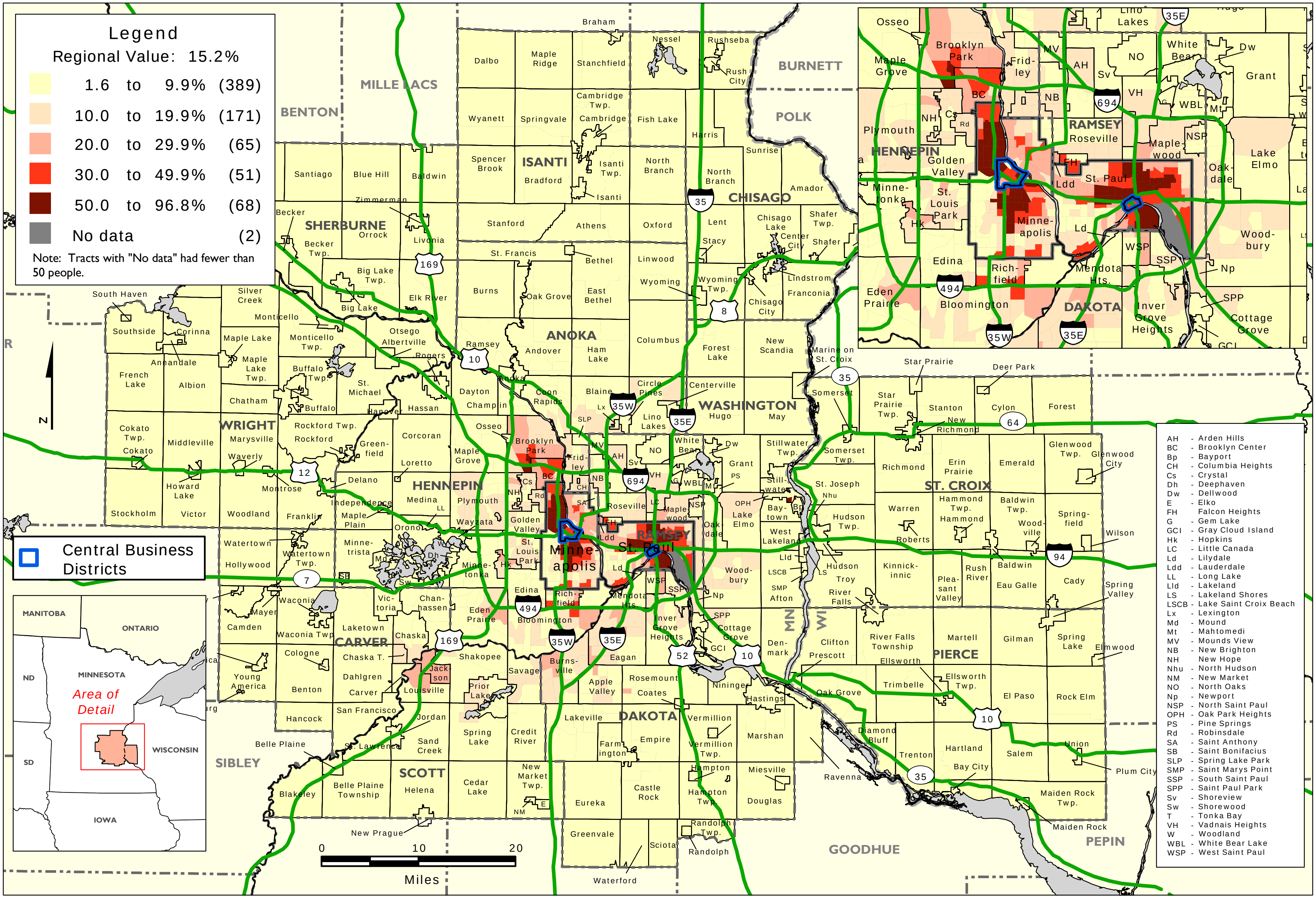
Map 2: MINNEAPOLIS - SAINT PAUL REGION
Percentage People of Color by Census Tract, 2000

People of Color include all populations except single race non-Hispanic whites.



Data Source: U.S. Census Bureau

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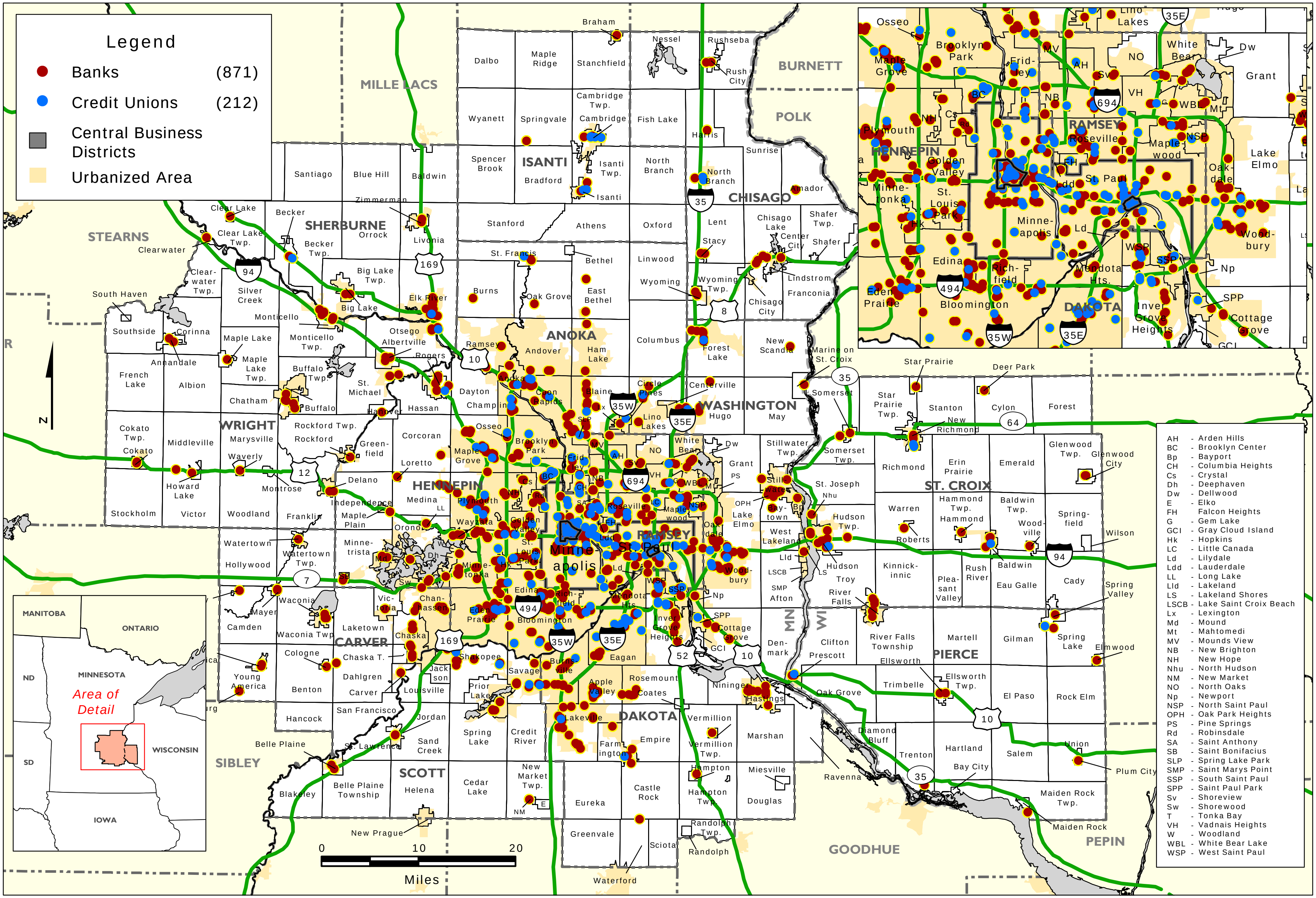
Map 3: MINNEAPOLIS - SAINT PAUL REGION
Banks and Credit Unions by Location, 2008



Data Source: Reference USA

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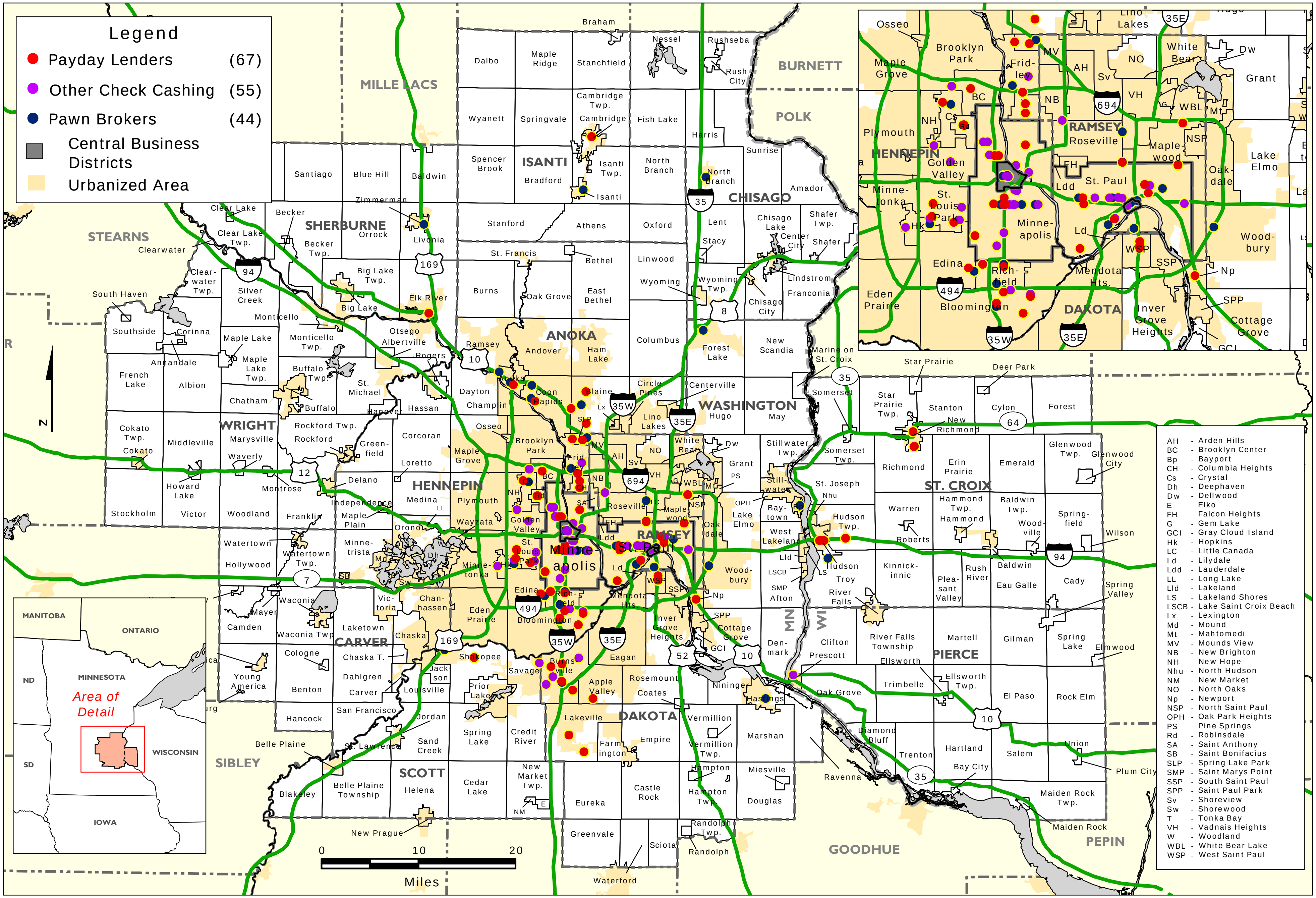
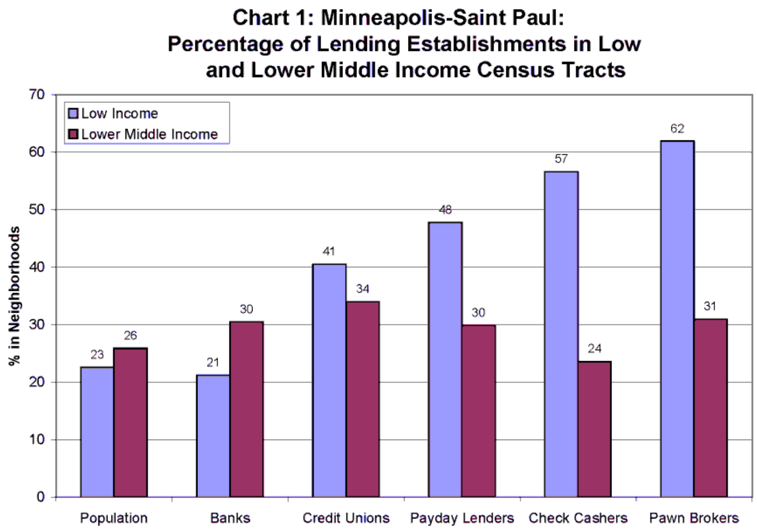
Map 4: MINNEAPOLIS - SAINT PAUL REGION
Payday Lenders, Other Check Cashing and Pawn Brokers by Location, 2008



Data Source: Reference USA, MN Department of Commerce

Lenders in Low and Lower-Middle Income Areas:
Low income neighborhoods have much larger regional shares of non-conventional lenders than of banks. While lower income neighborhoods in the region have 23 percent of the regions population, they have 21 percent of the regions banks, as illustrated in chart 1. In contrast, lower income neighborhoods have 48 percent of the region's payday lenders, 57 percent of check cashers and 62 percent of pawn brokers.[77] Lower middle income neighborhoods have greater shares of banks and much smaller shares of non-conventional lenders than low income neighborhoods. Low income neighborhoods do benefit from having 41 percent of the region's credit unions.



Lenders in Racially Integrated/Segregated Areas:
There are relatively few banks in the region's integrated and non-white segregated neighborhoods, compared to their population shares. While about six percent of the region's population live in integrated neighborhoods and about seven percent live in non-white segregated neighborhoods, only three percent of banks are located in each neighborhood type. (Chart 2)

On the other hand, both integrated and non-white segregated neighborhoods have disproportionate shares of credit unions. Non-white segregated neighborhoods however, have much larger shares of non-conventional lenders. Segregated neighborhoods have 13 percent of the region's payday lenders, 12 percent of all pawnshops and nearly 30 percent of check cashers.

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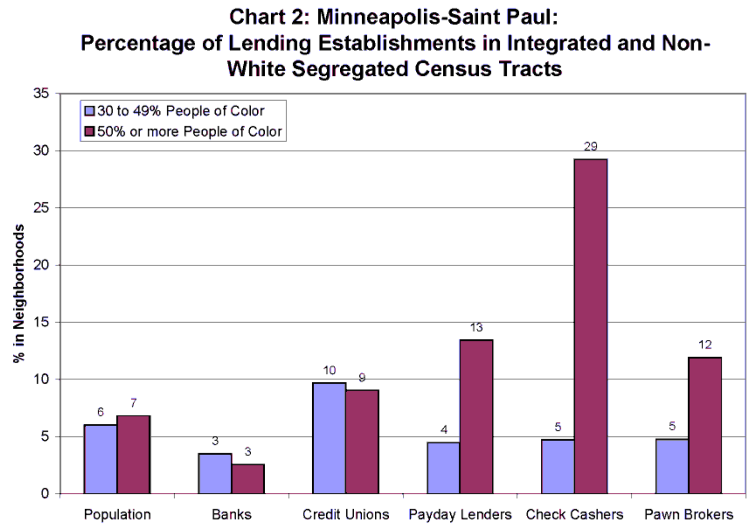
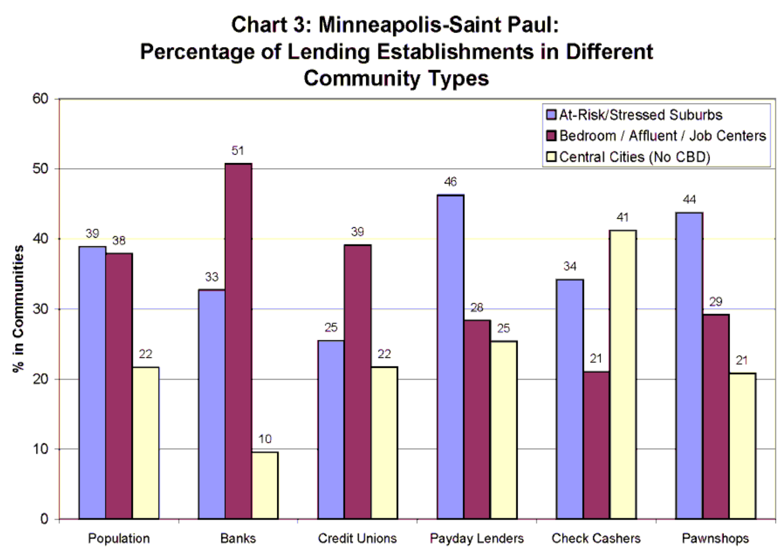
[77] In the neighborhoods charts, payday lenders often include check cashers and pawnshops, and check cashers and pawnshops include payday lenders. However, not all check cashers and pawnshops are payday lenders, and not all payday lenders are check cashers or pawnshops.



Lenders in Different Fiscal Community Types:
There are relatively few banks in the region's central cities (excluding CBDs), compared to their population shares. While about 22 percent of the region's population lives in the central cities, those places contain only ten percent of the region's banks. (Chart 3)

Fiscally at-risk and stressed suburbs also contain a smaller regional share of banks (33 percent) than population (39 percent), but larger shares of payday lenders (46 percent) and pawnshops (44 percent). More fiscally strong suburban job centers, affluent and bedroom communities, on the other hand, have disproportionate shares of banks and have smaller shares of non-conventional lenders.



2. Portland

Portland is a compact and relatively racially integrated region. Concentrations of lower income residents and people of color are less pronounced. In addition where low income neighborhoods do exist, they are not as underserved by banks as they are in Minneapolis-St. Paul. However, as in Minneapolis-St. Paul, these areas tend to be over-served by non-conventional lenders, and racially segregated census tracts, though less numerous than integrated tracts, tend to lack both conventional and non-conventional lenders (with the exception of pawn shops).

The relationship between community type and lenders is not as strong in Portland as in the Twin Cities. Nevertheless, the city of Portland (outside the CBD) has disproportionately few conventional banks and greater shares on non-conventional lenders.

Income- Low income neighborhoods in Portland are located in the northern and eastern portions of the city, and across the Columbia River in Vancouver, Washington. (Map 5) There are also stretches of lower income tracts in the suburbs west of Portland, from Beaverton to Forest Grove. In Portland, many low income tracts are in close proximity to high income tracts located near the CBD and in inner suburbs like Beaverton.

Race- Communities of color are located along the northern edge of the city of Portland, north of the Portland CBD and clustered along the suburban corridor from Beaverton to Forest Grove. (Map 6) Portland is less racially segregated than many metropolitan areas, and has only ten census tracts with 50 percent or more people of color, compared to 50 racially integrated tracts (with 30 to 49 percent people of color). Most integrated tracts are near to predominately white neighborhoods, reflecting a somewhat decentralized spatial pattern of racially diverse areas in Portland.

Conventional Lenders- Banks and credit unions are scattered across the region, including along the lower income Beaverton-Forest Grove suburban corridor. (Map 7) There are, however, relatively few banks in the racially segregated census tracts north of the Portland CBD.

Non-Conventional Lenders- The most distinctive feature of the distribution of non-conventional lenders is the relatively high concentration on the Washington side of the region. (Map 8) Though the Washington portion of the metropolitan area contains only 18 percent of the region's population, it has 57 percent of the region's payday lenders. The strong presence of payday lenders in Washington State is indicative of the more lenient state law and regulation towards payday lenders in Washington, in comparison to Oregon.

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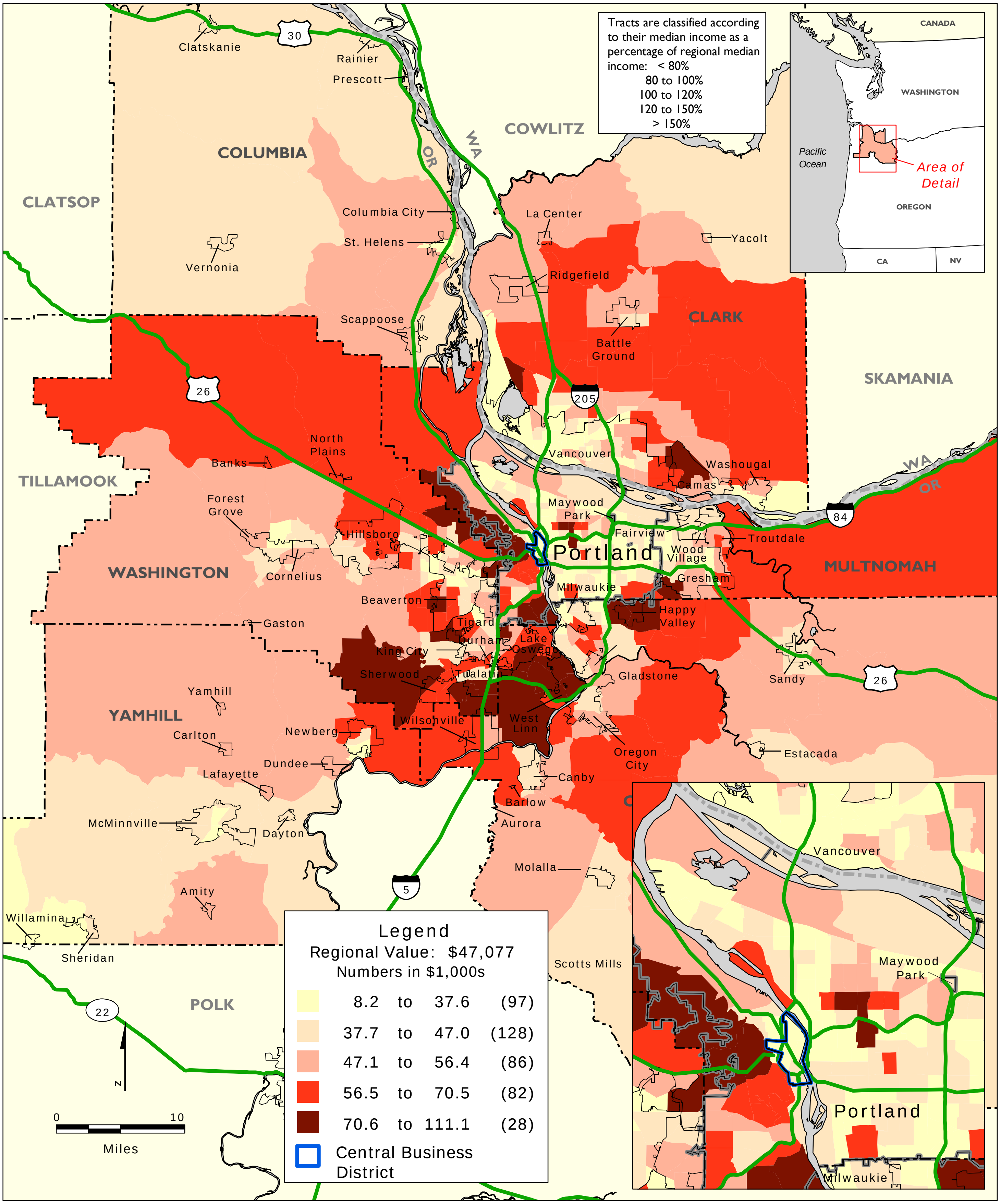
Map 5: PORTLAND PRIMARY REGION: Median Household Income by Census Tract, 1999



Data Source: U.S. Census Bureau

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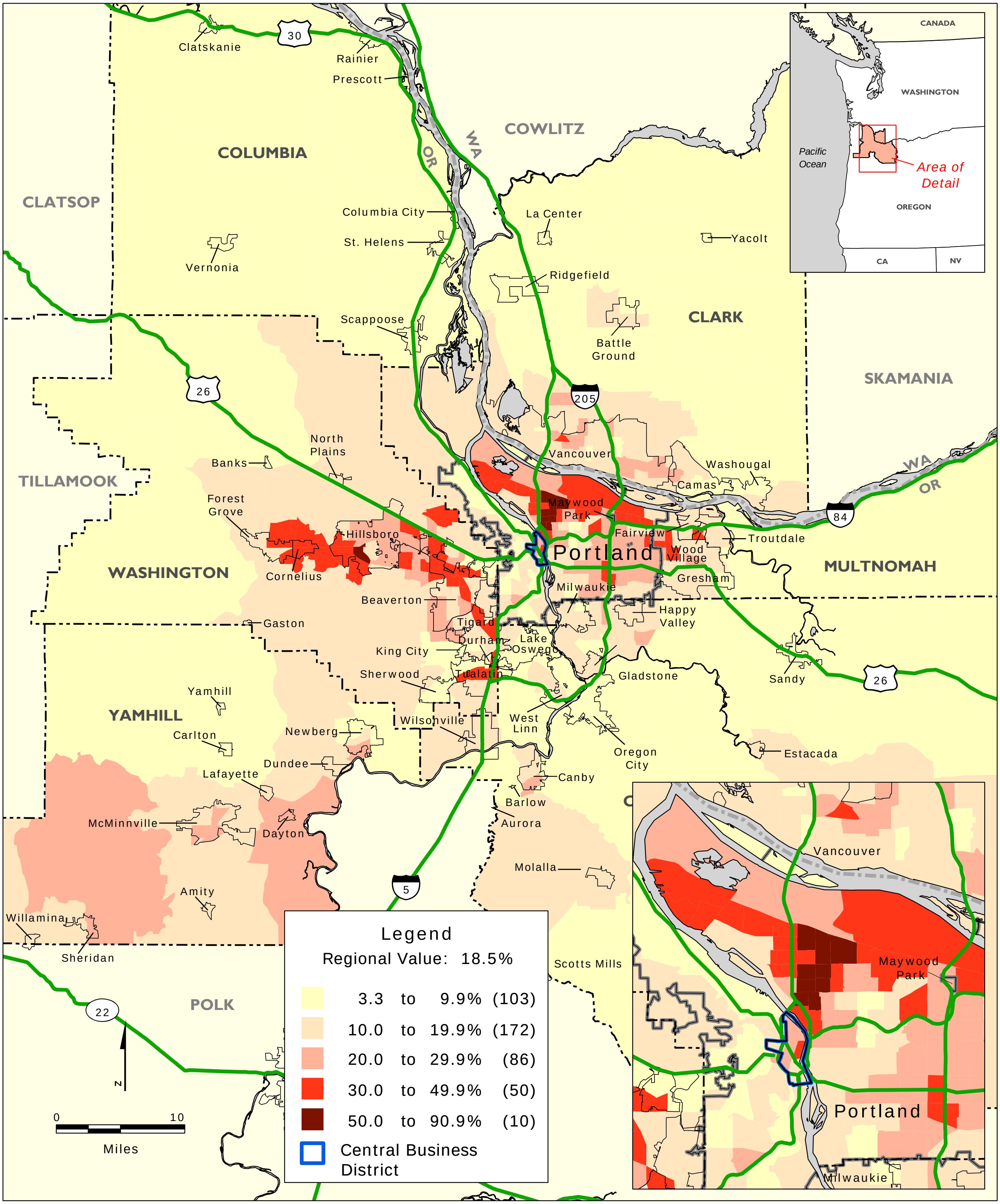
Map 6: PORTLAND PRIMARY REGION: Percentage People of Color by Census Tract, 2000

People of Color include all populations except single race non-Hispanic whites.



Data Source: U.S. Census Bureau

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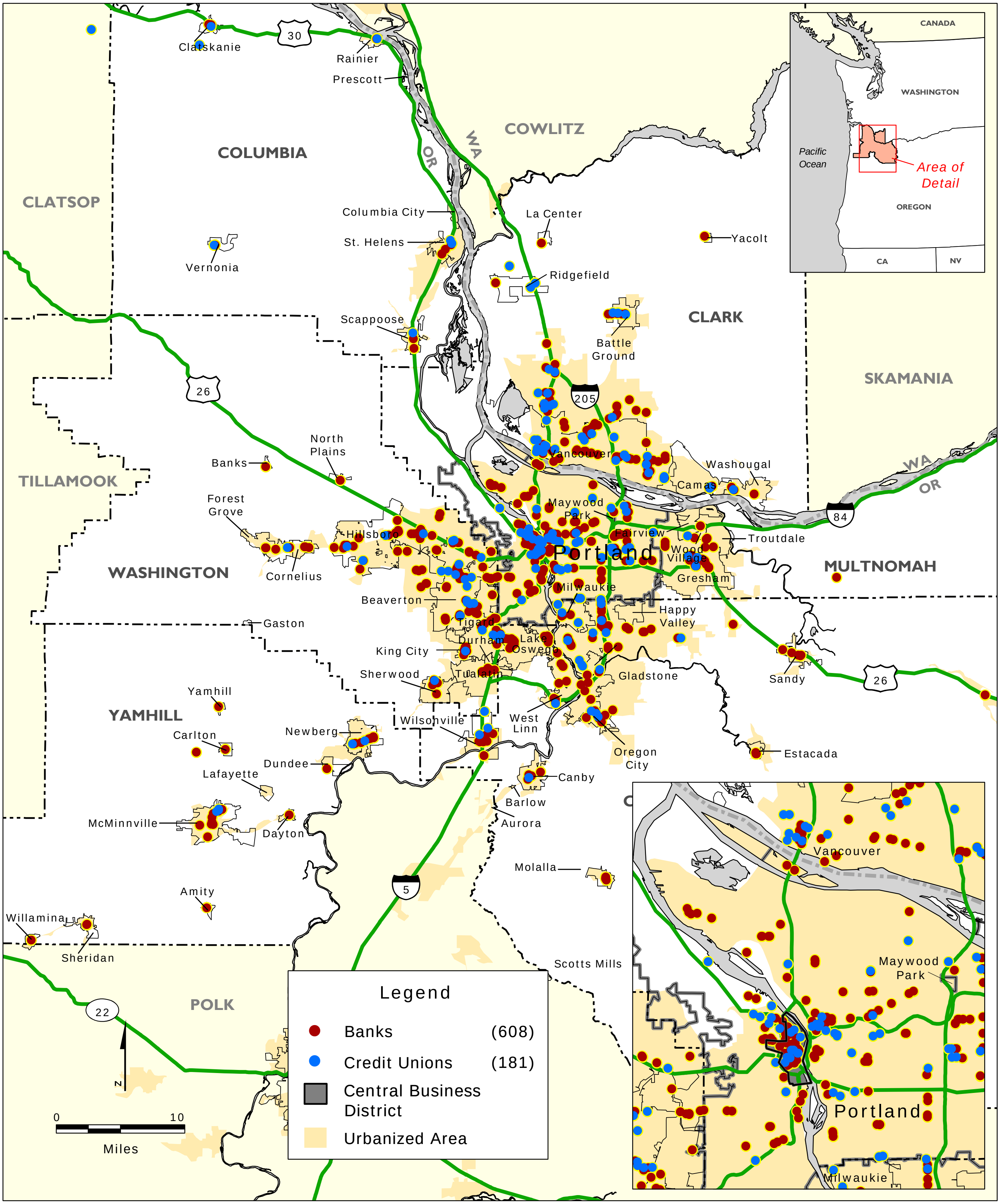
Map 7: PORTLAND PRIMARY REGION: Banks and Credit Unions by Location, 2008



Data Source: Reference USA

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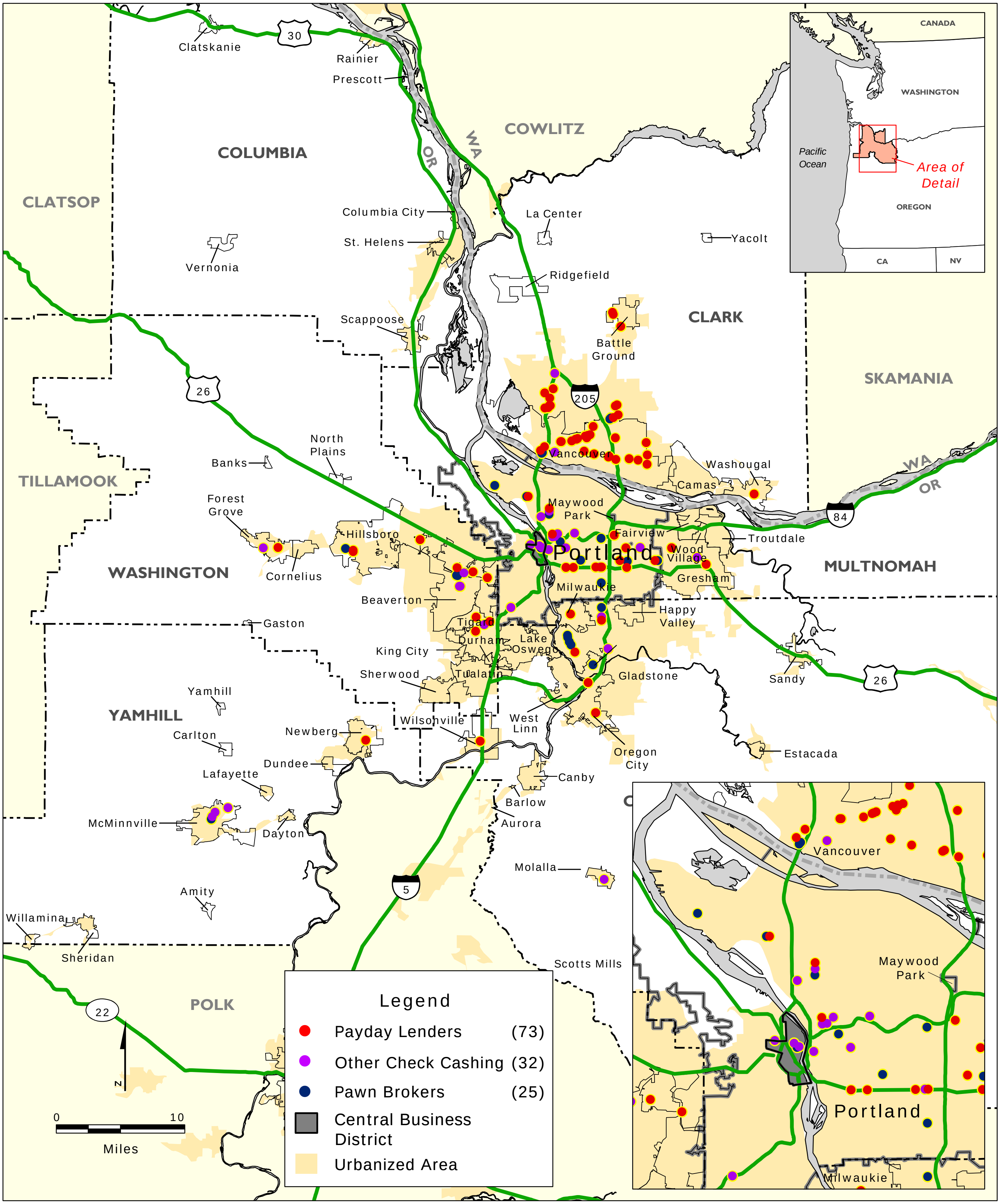
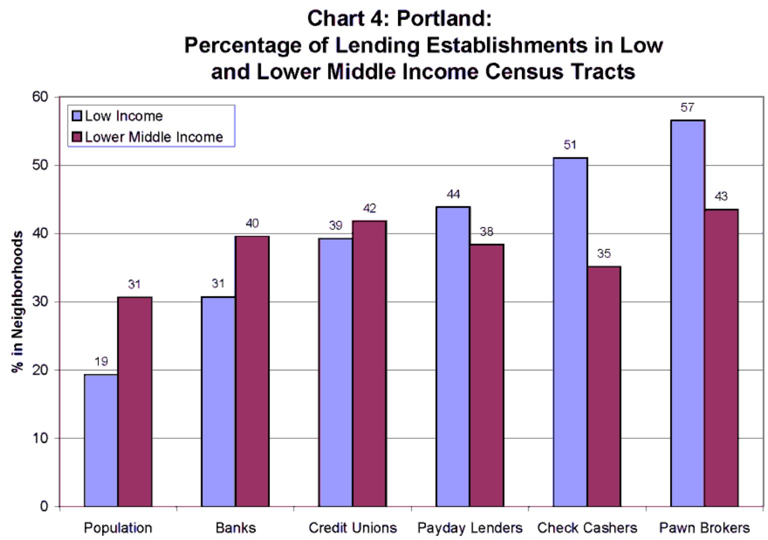
Map 8: PORTLAND PRIMARY REGION: Payday Lenders, Other Check Cashing and Pawn Brokers by Location, 2008



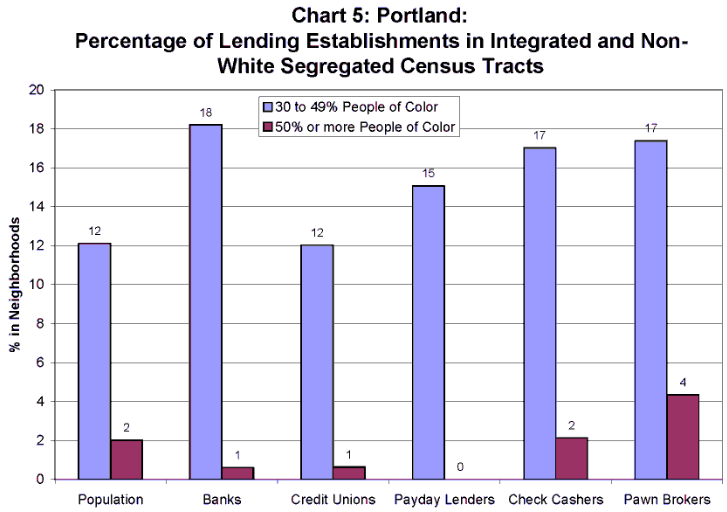
Data Source: Reference USA, Oregon Division of Finance and Corporate Securities, Washington State Department of Financial Institutions

Lenders in Low and Lower Middle Income Areas:
In Portland both low and lower middle income neighborhoods are well served by banks and credit unions. (Chart 4) Low income neighborhoods, for instance have 19 percent of the region's population, 31 percent of the region's banks and 39 percent of the credit unions. Unlike moderate income areas, however, lower income neighborhoods tend to have even larger shares of non-conventional lenders. Low income neighborhoods have twice the share of payday lenders (44 percent) and check cashers (51 percent) and three times as many pawnshops (57 percent) as they have population (19 percent). The concentration of non-conventional lenders in low income parts of Vancouver, Washington, undoubtedly influences the trend of unconventional lenders in the region's low income neighborhoods.

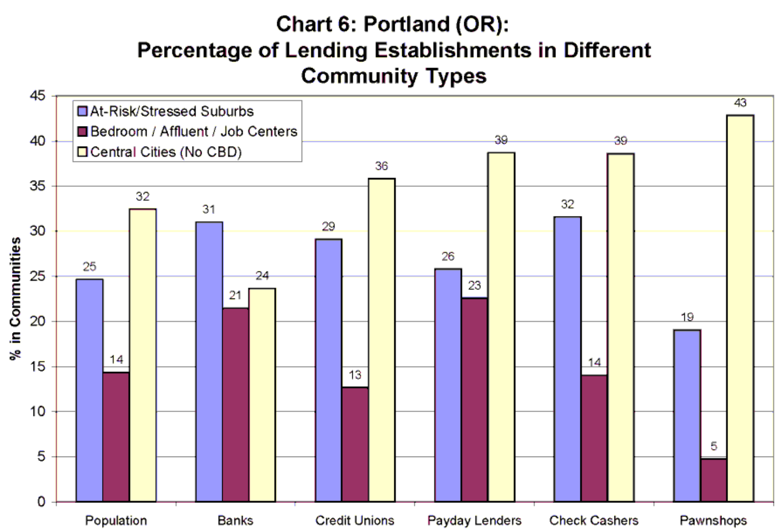


Lenders in Racially Integrated/Segregated Areas:
Integrated neighborhoods in the Portland region tend to have slightly more lenders of all types, while segregated neighborhoods tend to lack lenders of all types. (Chart 5) Racially integrated tracts in Portland contain 12 percent of the region's population, the same share of credit unions and 18 percent of the region's banks. The shares of non-conventional lenders in integrated neighborhoods are roughly proportional to the population share and do not differ much from the shares of conventional lenders.

The share of people living in Portland's segregated neighborhoods is very small (just two percent) and the neighborhoods have even smaller shares of most types of lending institutions. Only pawn shops show a share greater than two percent.



Lenders in Different Fiscal Community Types:
Banks in the Portland region are more concentrated in suburban areas than the central cities. While the city of Portland has 32 percent of the region's population it contains only 24 percent of the banks. (Chart 6) Conversely, the city of Portland has larger shares of non-conventional lenders, especially check cashers, 41 percent of which are in Portland. The city also has a slightly larger share of credit unions than population. Suburban areas have greater regional shares of banks than population, but also have some larger shares of non-conventional lenders. For at-risk and stressed suburbs, there are larger shares of check-cashers (32 percent) than population (25 percent); and for suburban job centers, affluent and bedroom communities, the regional share of payday lenders (23 percent) is larger than the share of population (14 percent)



Note: because of the small number of communities in the Washington portion of the Portland metropolitan area, only the Oregon portion of the state is included in the analysis. Shares in the charts do not add up to 100, because there are unincorporated areas in Portland that were not categorized under the community classification.

3. Seattle

Seattle is also a relatively compact and integrated region, and in areas where there are higher percentages of low income residents and people of color, there are also relatively large shares of lenders. Low income neighborhoods show disproportionate shares of all types of lenders, with slightly greater shares of non-conventional lenders than conventional ones. Both racially integrated and segregated neighborhoods show lender shares similar to their population shares. Most noteworthy in Seattle is the sheer number of payday lenders, which far outnumber the region's credit unions.

The relationship between community type and lender locations is mixed. Both non-conventional and conventional lenders are over-represented in at-risk and stressed suburbs while central cities had smaller shares of lenders of every type and more affluent suburbs had larger shares of every type.

Income- Low income neighborhoods in Seattle tend to form a band across the isthmus that contains the city of Seattle, including parts of the city and suburbs directly to the north (e.g. Everett) and south (e.g. Kent). (Map 9) Lower income tracts tend to be relatively close to upper income tracts, while lower income neighborhoods on the southern part of the isthmus are separated from wealthy suburbs by Lake Washington. The north side of Seattle city has a mix of low, middle and high income census tracts.

Race- In a manner similar to income, racially integrated neighborhoods tend to form a band across the isthmus that contains Seattle and into suburbs to the north and south of the city. (Map 10) Additionally, there is a band of integrated tracts in wealthier sections of the region on the east side of Lake Washington. Many of these neighborhoods are in close proximity to predominately white neighborhoods.

Seattle also has a cluster of segregated tracts on the south side of the city, surrounded by integrated tracts. Although there are more segregated tracts in Seattle than in Portland, Seattle has less than half the number of segregated tracts (34) as integrated tracts (82), a much smaller ratio than in Minneapolis-St. Paul.

Conventional Lenders- Conventional lenders cluster in a north-south orientation mirroring the built up portions of the region. (Map 11) However, there are areas where conventional lenders are absent, notably in the wealthier eastern fringes of the urbanized area and in the low income southwest section of the city of Seattle. Regionally, there are many fewer credit unions (132) than banks (812).

Non-Conventional Lenders- Seattle has many payday lenders. Though they are distributed throughout the region, they tend to cluster closer to major highways than do banks. (Map 12) Notably, there are many more payday lenders in the region (204) than in Minneapolis-St. Paul (67) or Portland (73).

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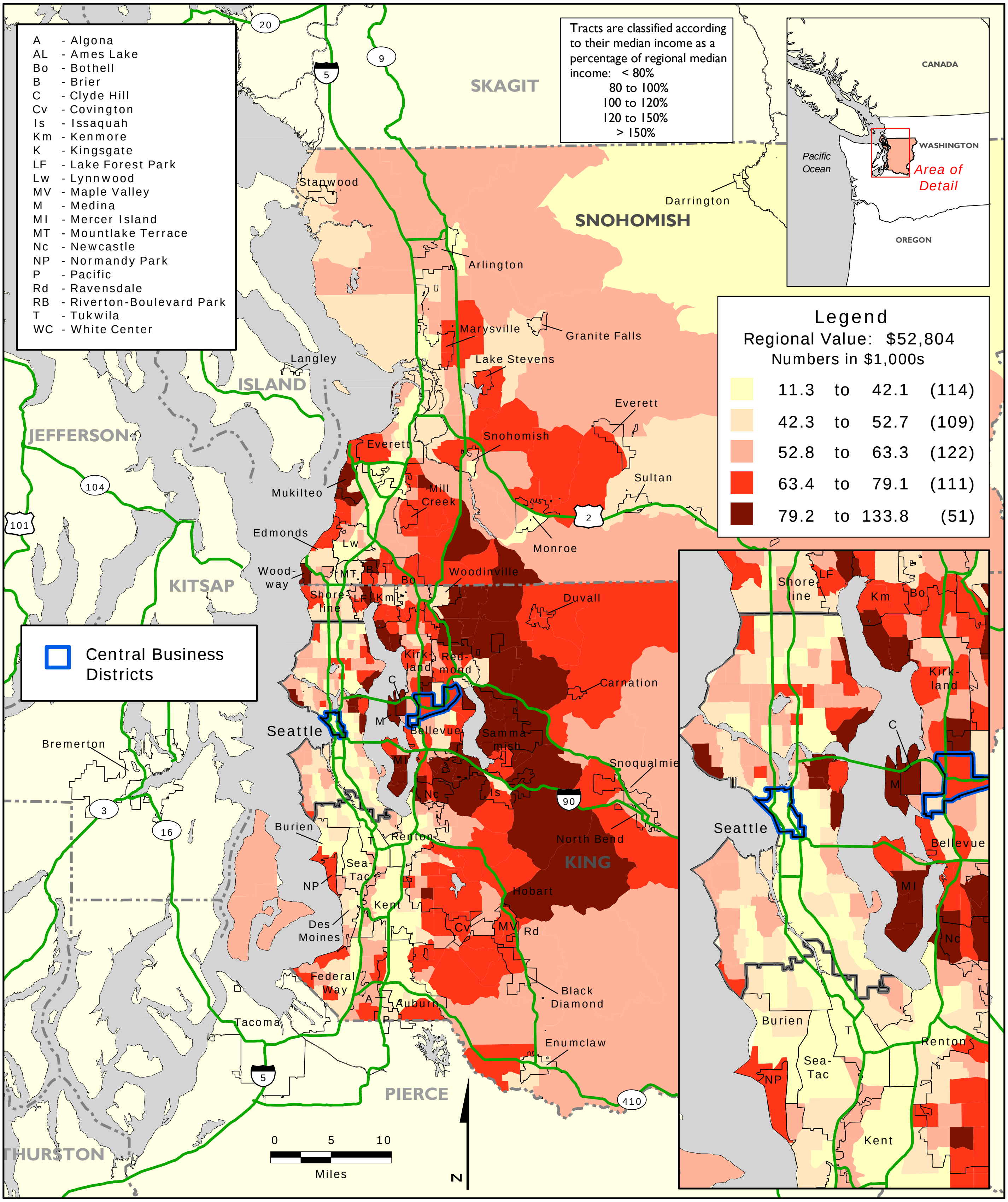
Map 9: SEATTLE PRIMARY REGION
Median Household Income by Census Tract, 1999



Source: U.S. Census Bureau

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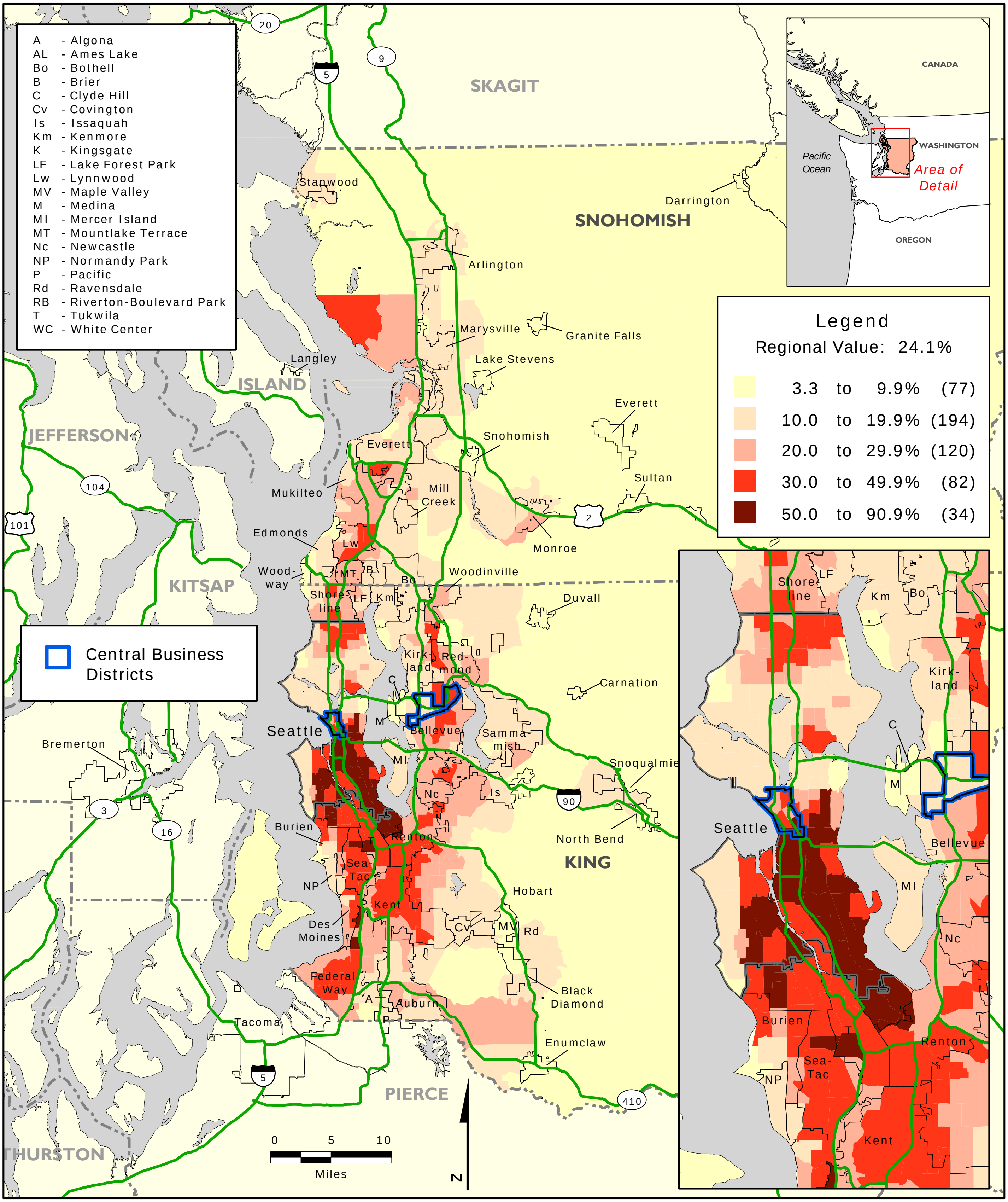
Map 10: SEATTLE PRIMARY REGION
Percentage People of Color by Census Tract, 2000

People of Color include all populations except single race non-Hispanic whites.



Source: U.S. Census Bureau

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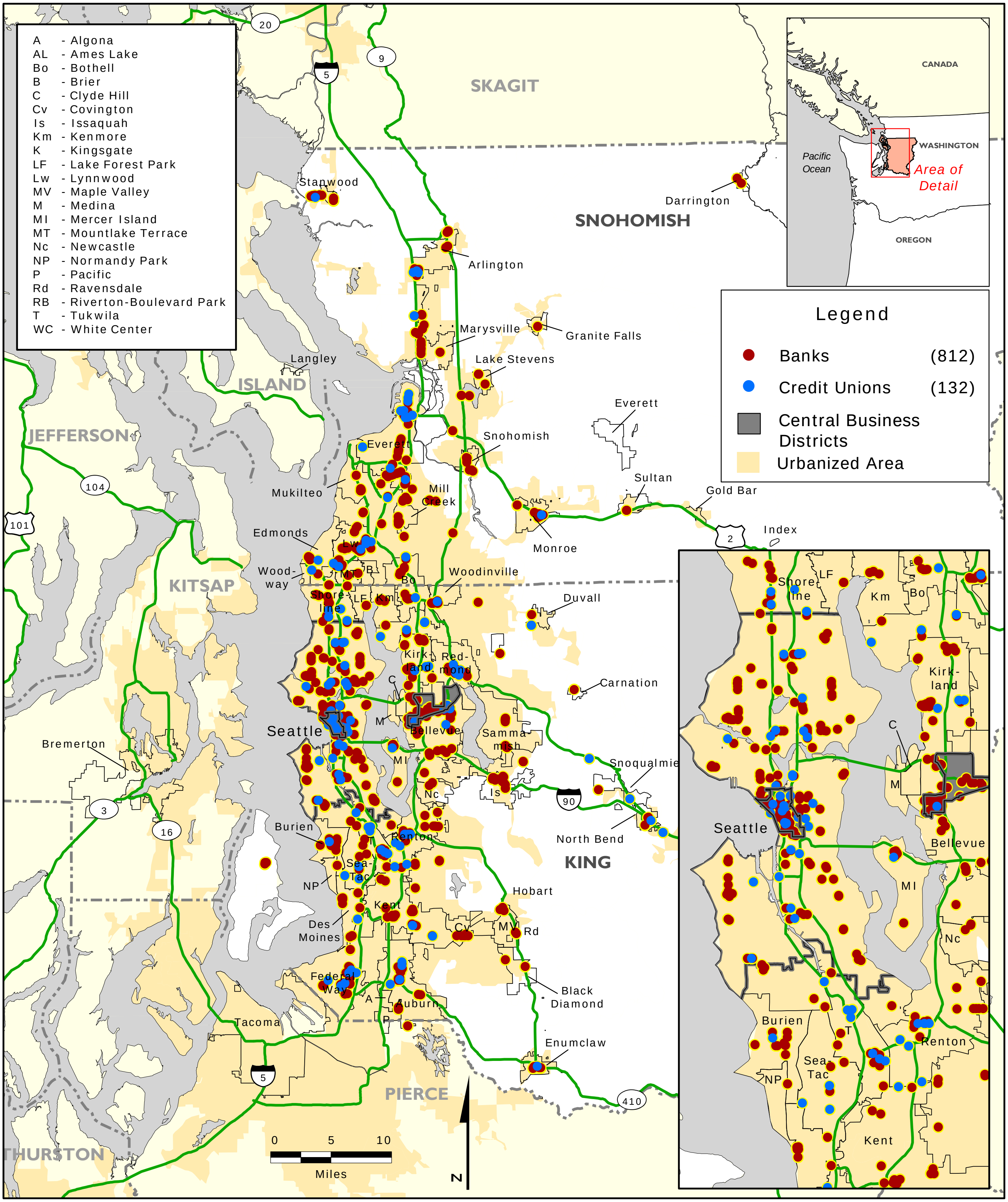
Map **11**: SEATTLE PRIMARY REGION Banks and Credit Unions by Location, 2008



Source: Reference USA

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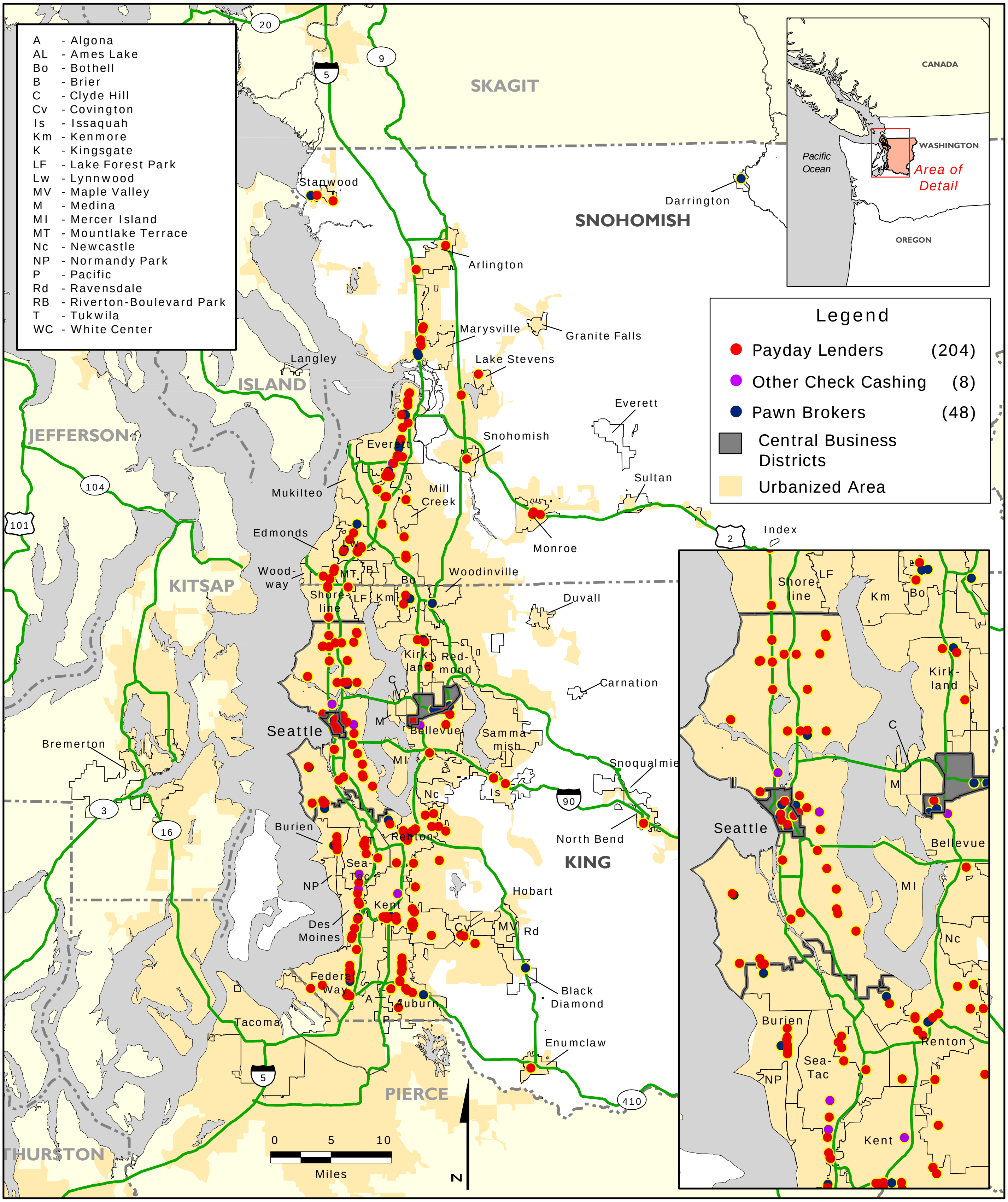
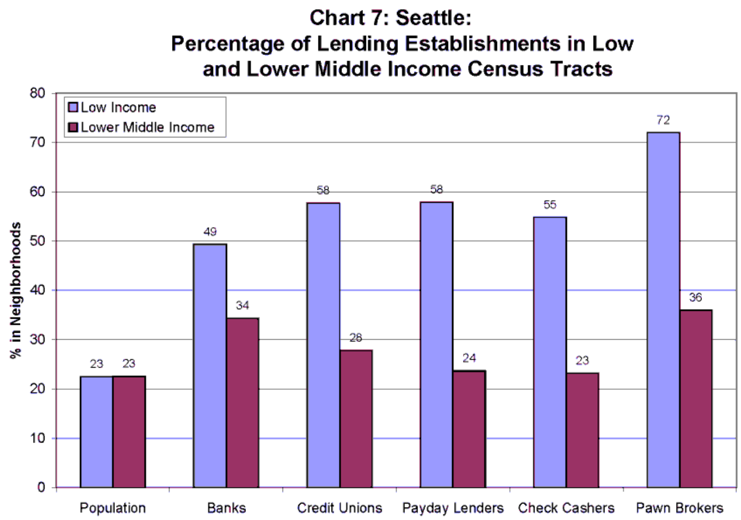
Map 12: SEATTLE PRIMARY REGION
Payday Lenders, Other Check Cashing and Pawn Brokers by Location, 2008

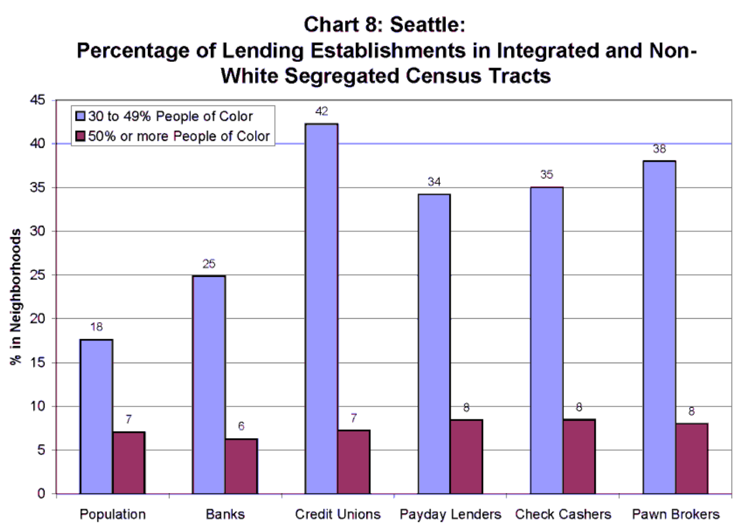


Source: Reference USA, Washington State Department of Financial Institutions

Lenders in Low and Lower Middle Income Areas:
In Seattle low income neighborhoods contain disproportionate shares of all types of lenders. (Chart 7) However, the largest shares in lower income areas are for non-conventional lenders, especially pawnshops. While low income areas contain 23 percent of the population in the region, they contain 55 to 72 percent of non-conventional lenders. Lower middle income neighborhoods, on the other hand, show roughly proportionate shares of lending establishments, with somewhat greater shares of both banks and pawnbrokers.



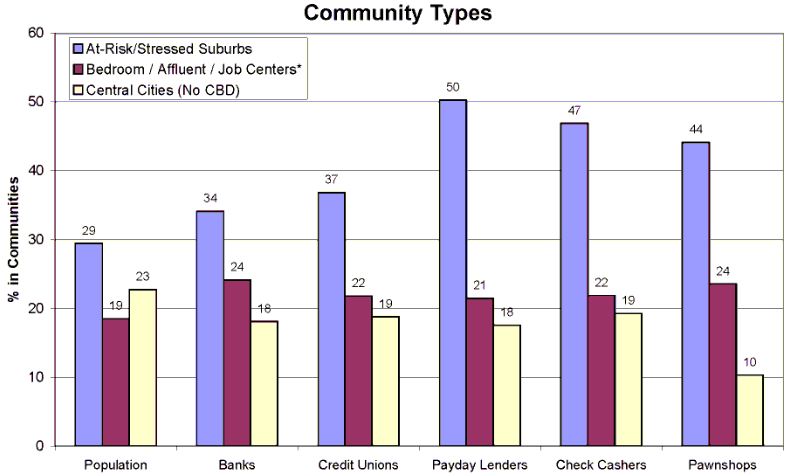
Lenders in Racially Integrated/Segregated Areas:
Seattle's integrated neighborhoods also show disproportionate shares of every type of lender, but particularly non-conventional lenders. Segregated neighborhoods, on the other hand, show roughly proportionate shares. (Chart 8) While integrated neighborhoods have 18 percent of the regions population, they have 25 percent of banks, 42 percent of credit unions, 34 percent of payday lenders, 35 percent of check cashers and 38 percent of pawnshops.



Lenders in Different Fiscal Community Types:
There are relatively smaller shares of lenders of all types in the City of Seattle. While Seattle has 23 percent of the region's population it has only 18 percent of the region's banks and payday lenders, 19 percent of the region's credit unions and check cashers and ten percent of the region's pawnshops. (Chart 9) More fiscally strong suburban job centers, affluent and bedroom communities, on the other hand, have slightly larger lender shares of all types compared to the their share of population.

There are much greater shares for all types of lenders, especially non-conventional lenders, in Seattle's at-risk and stressed suburbs. These suburbs have 29 percent of the region's population, 34 percent of the region's banks and 37 percent of the region's credit unions. Much larger are the shares of payday lenders (50 percent), check cashers (47 percent) and pawnshops (44 percent) in at-risk and stressed suburbs.

Chart 9: Seattle: Percentage of Lending Establishments in Different Community Types



Shares in the charts do not add up to 100, because there are unincorporated areas in Portland that were not categorized under the community classification.

C. Comparisons across the Metropolitan Areas

There are major differences across the three regions in the neighborhood shares of lenders by income and race. Lower income neighborhoods in Portland and Seattle showed much greater access to conventional lenders than in Minneapolis-St. Paul. However, non-conventional lenders tend to be disproportionately in lower income neighborhoods in all three metros.

The fact that there is more urban sprawl and social separation in Minneapolis-St. Paul helps to explain the difference in shares of banks in the regions' low income neighborhoods. In Portland and Seattle, banks gain an accessibility advantage by being centrally located. While those central locations are often in lower income neighborhoods where many customers have smaller borrowing capacity, they are in close proximity to higher income neighborhoods where there are more credit worthy customers. In Minneapolis-St. Paul the advantage of being centrally located is offset by the fact that central locations are often distant from higher income neighborhoods.

Sprawl and social separation in Minneapolis-St. Paul also contribute to racial biases in accessibility of conventional credit. There are disproportionately small shares of banks and disproportionately large shares of non-conventional lenders in Minneapolis-St. Paul's non-white segregated neighborhoods, tracts that also are more numerous than in Portland or Seattle. In comparison, Portland had very few segregated tracts and Seattle's segregated tracts, also less numerous, had similar shares of population and lenders of all types.

There were some similarities between the metros when considering neighborhood shares of lenders. In all three regions, low income neighborhoods have larger regional shares of non-conventional lenders than conventional lenders. For conventional lenders, there were larger shares of credit unions than banks in all three metros' low income areas. This was also true in racially integrated and segregated non-white neighborhoods in the Twin Cities, where regional shares of credit unions were larger than the shares of banks or population.

Lending Establishments Per Capita

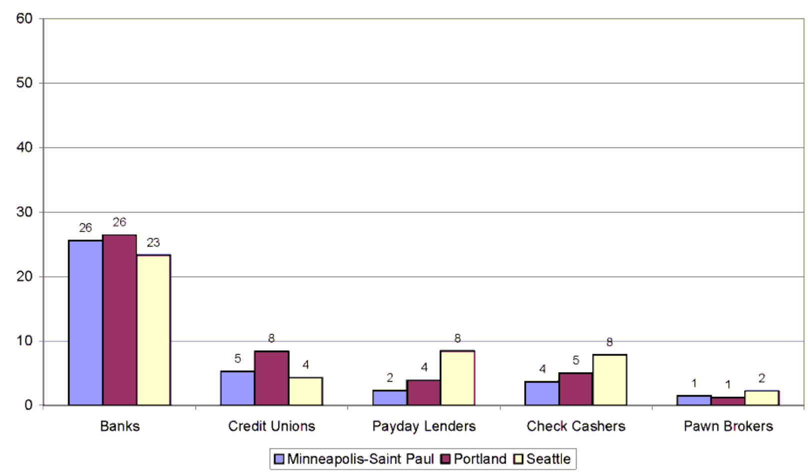
When considering the sheer number of establishments in different neighborhoods it's clear that there are differing levels of access to lenders. In all three metros racially segregated neighborhoods have few overall lenders, and the number of non-conventional lending establishments meets or exceeds the number of banks and credit unions. Conversely, low income neighborhoods tend to have more lenders, particularly in Portland and Seattle, and have more banks and credit unions than non-conventional lenders.

To understand lending patterns in metropolitan areas it is important to know how many lenders there are per population in an area. Neighborhoods that have a large share of lenders in a region could have small per capita rates of lenders, that is, few lenders per resident, if there are few overall lenders in the region.

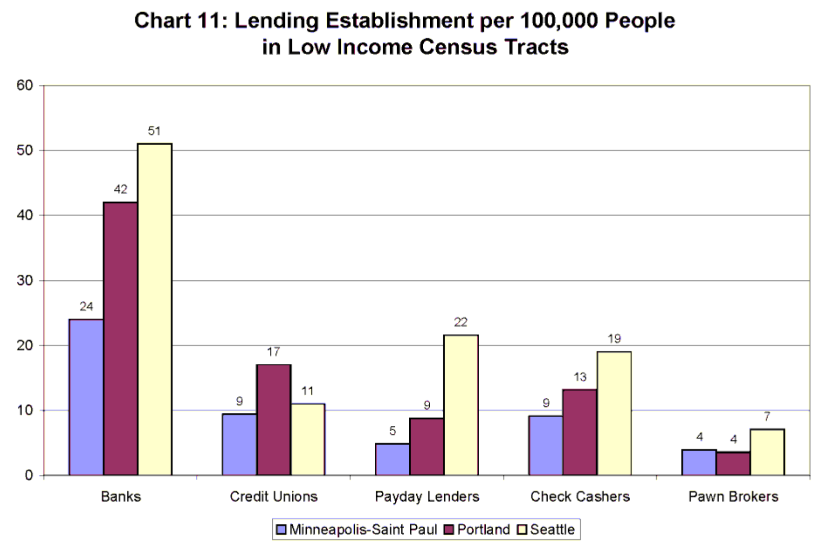
The per capita measure used in this study is crucial for comparing the regions to one another, because there were differences in the number of lenders in the regions. Seattle, for instance, has many more payday lenders than do Minneapolis-St. Paul, even though Seattle has a smaller population. In this case, neighborhoods with a small share of payday lenders in Seattle would have more per capita payday lenders than neighborhoods with the same small share of lenders in Minneapolis-St. Paul.

Regional Lenders Per Capita
In all three metropolitan areas there are more banks per 100,000 persons than all other types of lenders combined. (Chart 10) Of the three metros, Seattle has the smallest number of banks per capita. Seattle also has fewer credit unions per capita and greater numbers of non-conventional lenders per capita than Minneapolis-St. Paul or Portland. Seattle has 8 payday lenders per 100,000 persons, two times the per capita rate of payday lenders in Portland and four times the rate of Minneapolis-St. Paul. Seattle also has about twice the rate of check cashers and pawnshops than Minneapolis-St. Paul and Portland.

Chart 10: Lending Establishment per 100,000 People

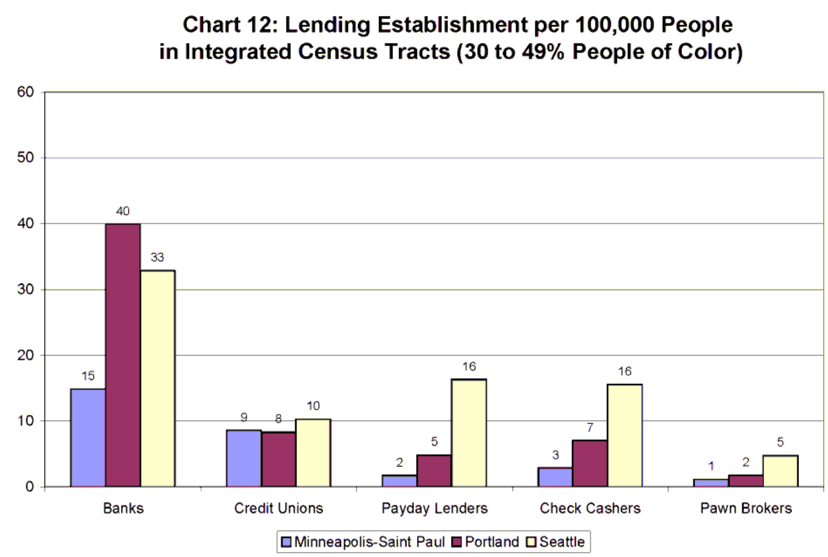


Lenders Per Capita in Low Income Neighborhoods
There are a disproportionate per capita number of all types of lenders in low income areas compared to the regional total in Portland and Seattle. (Chart 11) In Minneapolis-St. Paul there are roughly the same number of banks per capita number in low income neighborhoods as in the region as a whole. Non-conventional lenders were especially common in Seattle's lower income neighborhoods, with an even greater rate of payday lenders and rate of check cashers than credit unions. Still, there were more than twice as many banks as payday lenders and check cashers in Seattle's low income neighborhoods. In Minneapolis-St. Paul and Portland, banks were also much more prevalent on a per capita basis than non-conventional lenders in low income neighborhoods.



Lenders Per Capita in Racially Integrated Neighborhoods
Portland's and Seattle's integrated neighborhoods have more lenders per capita than average for their regions, but fewer lenders than their low income neighborhoods. (Chart 12) For instance, in Seattle there were 33 banks per 100,000 people in integrated neighborhoods, compared to 23 per 100,000 in the region as a whole and 51 per 100,000 in lower income areas. Portland also had slightly fewer per capita banks in integrated neighborhoods than in low income neighborhoods.

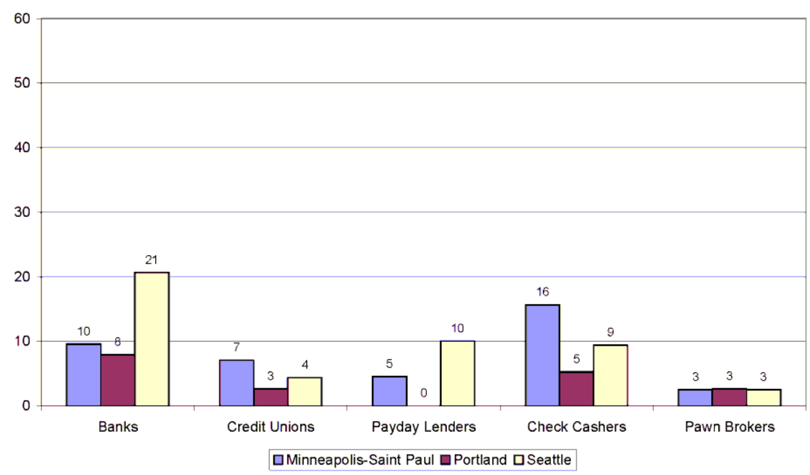
Minneapolis-St. Paul's integrated neighborhoods, however, had very few banks. While there were 26 banks per 100,000 people in the region as a whole, there were only 15 in racially integrated neighborhoods. Minneapolis-St. Paul also had relatively few non-conventional types of lenders in integrated neighborhoods.



Lenders Per Capita in Racially Segregated Neighborhoods
Non-white segregated neighborhoods in all three metros lacked conventional lenders. (Chart 13) Seattle had the largest number of banks in segregated neighborhoods of the three metros with 21 per 100,000, but this was still less than the regional rate of 23. Seattle also had a slightly higher rate of non-conventional lenders than the region as a whole. In Portland, there were relatively few lenders of any type in segregated neighborhoods.

Segregated neighborhoods in Minneapolis-St. Paul lack conventional lenders, but have high rates of non-conventional lenders. In fact, there were almost as many check cashers per capita (16 per 100,000) as banks and credit unions combined (17 per 100,000). The area also had 2.5 times the number of payday lenders per capita in segregated neighborhoods as the region as a whole. The lack of conventional lenders and presence of non-conventional lenders in Minneapolis-St. Paul's segregated neighborhoods is especially troubling, given that segregated neighborhoods are more prevalent there than in the other two metros.

Chart 13: Lending Establishment per 100,000 People in Segregated Census Tracts (> = 50% People of Color)



IV. Analysis of Borrower Access to Prime Mortgage Lenders

The prior section shows the disparities within and across the three metropolitan areas in the availability of lenders of various types. Compared to other types of neighborhoods, access to conventional lenders in lower income and integrated neighborhoods was clearly better in the Portland and Seattle metros than in Minneapolis-St. Paul. In the two western metros, these types of neighborhoods contained disproportionate shares of conventional banks. In Minneapolis-St. Paul, on the other hand, integrated and non-white segregated neighborhoods were particularly disadvantaged in this regard.

This section explores how these differences affect consumer access to conventional, or prime, lenders. The analysis compares how often borrowers in different types of neighborhoods actually use prime lenders, according to neighborhood income and racial diversity. The necessary data for small loans needed to fully examine the use of non-conventional lenders are not available. The analysis therefore focuses on conventional lenders—banks—and home mortgage borrowing patterns.

Similar to the division of small loan establishments into conventional and non-conventional lenders, home mortgage lenders are divided into two types—prime and sub-prime lenders. Prime lenders typically make lower interest loans through bank branch locations while subprime lenders usually make higher interest loans working through mortgage brokers. To determine how lender services are available to borrowers in different types of neighborhoods, this section compares usage rates for prime lenders to neighborhood characteristics, including income and race.

The analysis shows clear-cut relationships in each of the metros between usage rates of prime lenders and the racial make-up and income of areas. Prime lending application rates are lower in areas with more people of color and lower incomes. The patterns are particularly stark in Minneapolis-St. Paul where prime lender application rates fall off more dramatically as neighborhood income falls or as neighborhood non-white shares increase.

A. Data and Methods.

This section analyzes Home Mortgage Disclosure Act (HMDA) data to derive how often borrowers access prime lenders in Minneapolis-St. Paul, Portland and Seattle. This work uses HMDA data for 2004 through 2006. HMDA was enacted in 1975 by the U.S. congress in response to the exclusion of racial minorities in the marketing and lending of home mortgages. HMDA requires a large majority of lending institutions (about 80 percent) to report their loan application transactions. The data are collected and recorded in an electronic database; and stored by the U.S. Federal Financial Institutions Examination Council (FFIEC).

HMDA records show mortgage application data matched with the race and income of the applicants, the purpose of the loan, the outcome, the name of the mortgage lender and the location of the borrower. HMDA was amended in 2004 to address the increasing rate of high-cost loan activity in the mortgage market to require identification of loans that are three percentage points above the prevailing quarterly treasury rate. This work uses this flag to identify subprime loans.

Other HMDA information include whether the mortgage was a first or second lien mortgage; if the loan request was for an owner or rental unit; whether the mortgaged property was a 1-4 unit, manufactured or multifamily property; and if the loan was a conventional or government-backed loan. Only records for first-lien, conventional, 1-4 unit owner properties were included for this analysis. HMDA records that were determined by FFIEC to have edit quality issues were also excluded.

Mortgage lenders tend to specialize either in prime lending or subprime lending. For the purposes of this work, a prime lender was defined as a bank issuing more than 90 percent prime loans. A subprime lender as a bank issuing more than 50 percent subprime loans.

B. Results

In this section neighborhood level prime-lender application rates are compared to neighborhood racial and income characteristics to evaluate whether there are relationships between lending behavior and neighborhood attributes in the three metropolitan areas. Overall, prime-lender application rates decline as income declines and as non-white population shares increase in each of the metropolitan areas. However, the underlying neighborhood characteristics and the strengths of the various relationships vary from metro to metro. The trade-offs between prime-lender rates and neighborhood characteristics are sharpest in Minneapolis-At. Paul.

1. Minneapolis-St. Paul

There is a strong relationship between prime lender application rates, the income and racial composition of neighborhoods in Minneapolis-St. Paul. Application rates to prime lenders are sharply lower in census tracts with greater shares of people of color and lower incomes.

People of color in segregated neighborhoods are especially affected by lack of access to prime lenders. This mirrors the results from the prior section that showed excessive numbers of payday lenders and an absence of banks in segregated communities of color. In Minneapolis-St. Paul the social separation of higher income households from the core of the region, spawned by urban sprawl, may contribute to the lack of conventional banks in neighborhoods of color in the core of the region.

Prime Lender Application Rates and Race
The relationships between prime lender application rates, race and income are shown in Tables 2 and 3. Application rates are very sensitive to the racial mix of neighborhoods. The prime lender share drops by about five percentage points for every 10 point increase in the population share for people of color. In non-white segregated neighborhoods—tracts with a non-white share above 50 percent—less than a quarter of applications were to prime lenders.

Table 2:
Race and Application Rate of Census Tracts in Minneapolis-Saint Paul

Percentage People of Color in Census Tract:	Population	Number of Applicants	Percentage Applying to a Prime Lender
0 to 9	1,653,923	312,967	54.4
10 to 19	708,977	106,475	51.6
20 to 29	205,962	30,776	40.9
30 to 39	103,192	14,797	35.4
40 to 49	71,831	11,634	32.4
50 or more	198,216	28,772	24.4
Total	2,942,101	505,421	50.2

Note: Does not include census tracts in central business district

Prime Lender Application Rates and Income

Prime lender rates are equally sensitive to neighborhood incomes. In neighborhoods with median household incomes between $40,000 and 80,000, a $10,000 difference in income is associated with a three to four point difference in prime lender application rates. Just one-third of applications in the poorest neighborhoods—tracts with median household incomes less than $40,000—were to prime lenders.

Table 3:
Income and Application Rate of Census Tracts in Minneapolis-Saint Paul

Median Household Income in Census Tract (in $1000s):	Households	Number of Applicants	Percentage Applying to a Prime Lender
Less than 40	185,884	60,936	33.7
40 to 49	242,649	98,083	44.9
50 to 59	272,802	126,725	48.5
60 to 69	189,421	95,891	53.5
70 to 79	103,384	60,873	57.5
80 or more	127,177	62,894	65.8
Total	1,121,317	505,402	50.2

Note: Does not include census tracts in central business district

Geographic Patterns

These relationships translate into a very clear geographic pattern. (Map 13) Prime lending application rates are very clearly highest in the region's higher-income second ring suburbs. Lowest rates are concentrated in large parts of the two central cities, inner suburbs northwest and south of Minneapolis, and many northern and northwestern outer suburbs.

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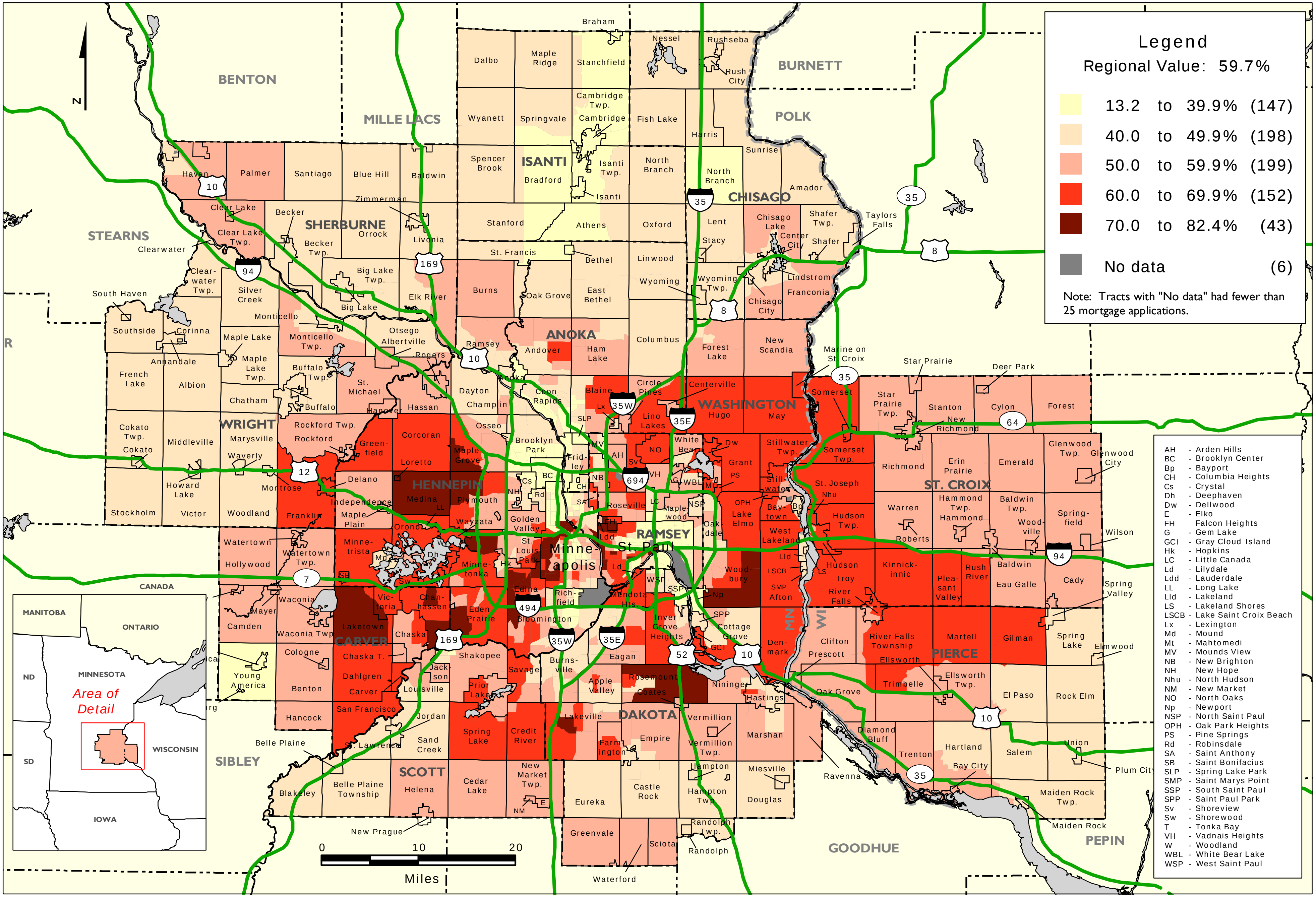
Map 13: MINNEAPOLIS - SAINT PAUL REGION
Percentage of Applicants Applying at Prime Lenders by Census Tract, 2004-2006



Data Source: FFIEC, Home Mortgage Disclosure Act

2. Portland

The Portland metro also shows clear relationships between prime lender application rates, income and racial composition. As in Minneapolis-St. Paul, application rates to prime lenders are notably lower in census tracts with greater shares of people of color and lower incomes. However, there are distinctly fewer tracts with very low prime lender application rates in Portland.

Prime Lender Application Rates and Race

Although there is a clear relationship between race and prime lending rates in Portland metro neighborhoods, the tradeoff is not nearly as severe as in Minneapolis-St. Paul. Prime application rates are clearly higher in more diverse neighborhoods, but the difference between the most diverse group and the least diverse is just 13 percentage points—46 percent compared to 59 percent. The equivalent range in Minneapolis-St. Paul is 30 percentage points—54 percent compared to 24 percent. In addition, because there are fewer non-white segregated tracts in Portland, the number of affected applications is considerably lower—17,500 total applications in the two highest diversity categories of Table 4 (Portland) compared to 40,400 applications in those categories of Table 2 (Minneapolis-St. Paul).

Table 4:
Race and Application Rate of Census Tracts in Portland

Percentage People of Color in Census Tract:	Population	Number of Applicants	Percentage Applying to a Prime Lender
0 to 9	457,316	86,829	59.3
10 to 19	785,092	142,307	56.7
20 to 29	386,532	66,075	52.8
30 to 39	173,496	25,140	53.4
40 to 49	60,819	10,359	45.6
50 or more	37,882	7,138	46.3
Total	1,901,137	337,848	55.8

Note: Does not include census tracts in central business district

Prime Lender Application Rates and Income

The application rate-income relationship in Portland is also clear and looks much like that seen in Minneapolis-St. Paul. (Table 5) The range of prime lender rates is a bit narrower—a difference of 26 percentage points between the highest and lowest categories compared to 32 points in the Twin Cities—and prime lender rates are higher on average in Portland, but the relationship is equally clear.

Table 5:
Income and Application Rate of Census Tracts in Portland

Median Household Income in Census Tract (in $1000s):	Households	Number of Applicants	Percentage Applying to a Prime Lender
Less than 40	199,055	72,596	49.0
40 to 49	217,744	92,501	52.6
50 to 59	172,174	92,248	56.4
60 to 69	82,367	44,877	60.9
70 to 79	38,168	23,480	67.0
80 or more	22,405	12,146	75.1
Total	731,913	337,848	55.8

Note: Does not include census tracts in central business district

Geographic Patterns

There is also a distinct geographic pattern to prime application rates in Portland. The highest rates are concentrated in a band of suburban areas along the west bank of the Willamette River west and south of the city of Portland. (Map 14) Areas with lower prime application rates can be found across the region but are particularly concentrated on the north and east sides of Portland city. The clear difference between Portland and Minneapolis-St. Paul is the smaller number of tracts with very low prime lender rates in Portland.

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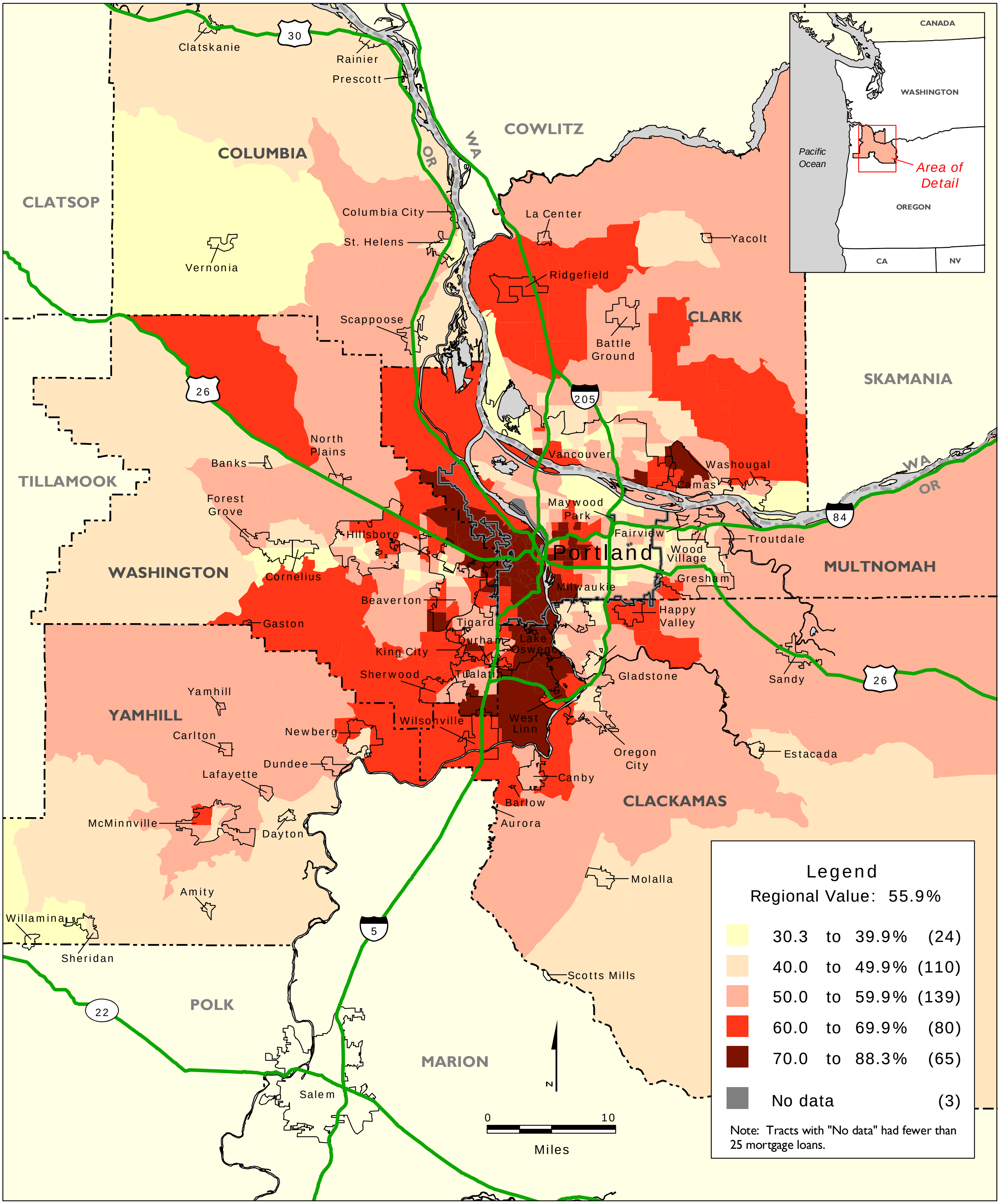
Map 14: PORTLAND PRIMARY REGION: Percentage of Applicants Applying at Prime Lenders by Census Tract, 2004-2006



Data Source: FFIEC, Home Mortgage Disclosure Act

3. Seattle

As expected, the Seattle also shows relationships across neighborhoods between prime lender application rates, income and racial diversity. As in the other metros prime lender application rate are lower in low income areas and more racially diverse areas. However, the relationships are not as strong in Seattle as in the other metros.

Prime Lender Application Rates and Race

Although racially diverse areas tend to show lower prime application rates in Seattle, the tradeoff is not as distinct as in the other metros. The spread from most diverse to least diverse areas is less than 10 percentage points and the application rates do not uniformly decline as neighborhood diversity increases. (Table 6) Prime lender rates are actually higher, for instance, in neighborhoods with non-white shares between 10 and 20 percent than in areas with non-white shares less than 10 percent.

Table 6:
Race and Application Rate of Census Tracts in Seattle

Percentage People of Color in Census Tract:	Population	Number of Applicants	Percentage Applying to a Prime Lender
0 to 9	290,836	54,892	49.9
10 to 19	904,928	147,900	54.9
20 to 29	545,655	82,705	50.8
30 to 39	279,387	39,869	42.7
40 to 49	123,028	14,136	42.3
50 or more	159,623	23,521	41.6
Total	2,303,457	363,023	50.5

Note: Does not include census tracts in central business district

Prime Lender Application Rates and Income

The range of prime lender application rates is also comparatively narrow across most of the income distribution in Seattle. (Table 7) The range from the lowest income group—less than $40,000—to the second highest group is just 10 points. The jump from the second highest to the highest income group *is* significantly greater in the Seattle metro but it involves relatively few applications.

Table 7:
Income and Application Rate of Census Tracts in Seattle

Median Household Income in Census Tract (in $1000s):	Households	Number of Applicants	Percentage Applying to a Prime Lender
Less than 40	158,956	41,551	45.1
40 to 49	201,519	72,502	44.4
50 to 59	209,390	85,848	47.8
60 to 69	193,125	89,746	52.0
70 to 79	78,310	39,580	55.7
80 or more	73,808	33,796	67.1
Total	915,108	363,023	50.5

Note: Does not include census tracts in central business district

Geographic Patterns
Seattle's home mortgage borrowers tend to apply more often at prime lenders in the center of the region and less often in the northern and southern reaches of the area. (Map 15) The northern and southern portions of Seattle's isthmus, areas with many of the region’s lower income households and people of color, show the lowest prime lender rates.

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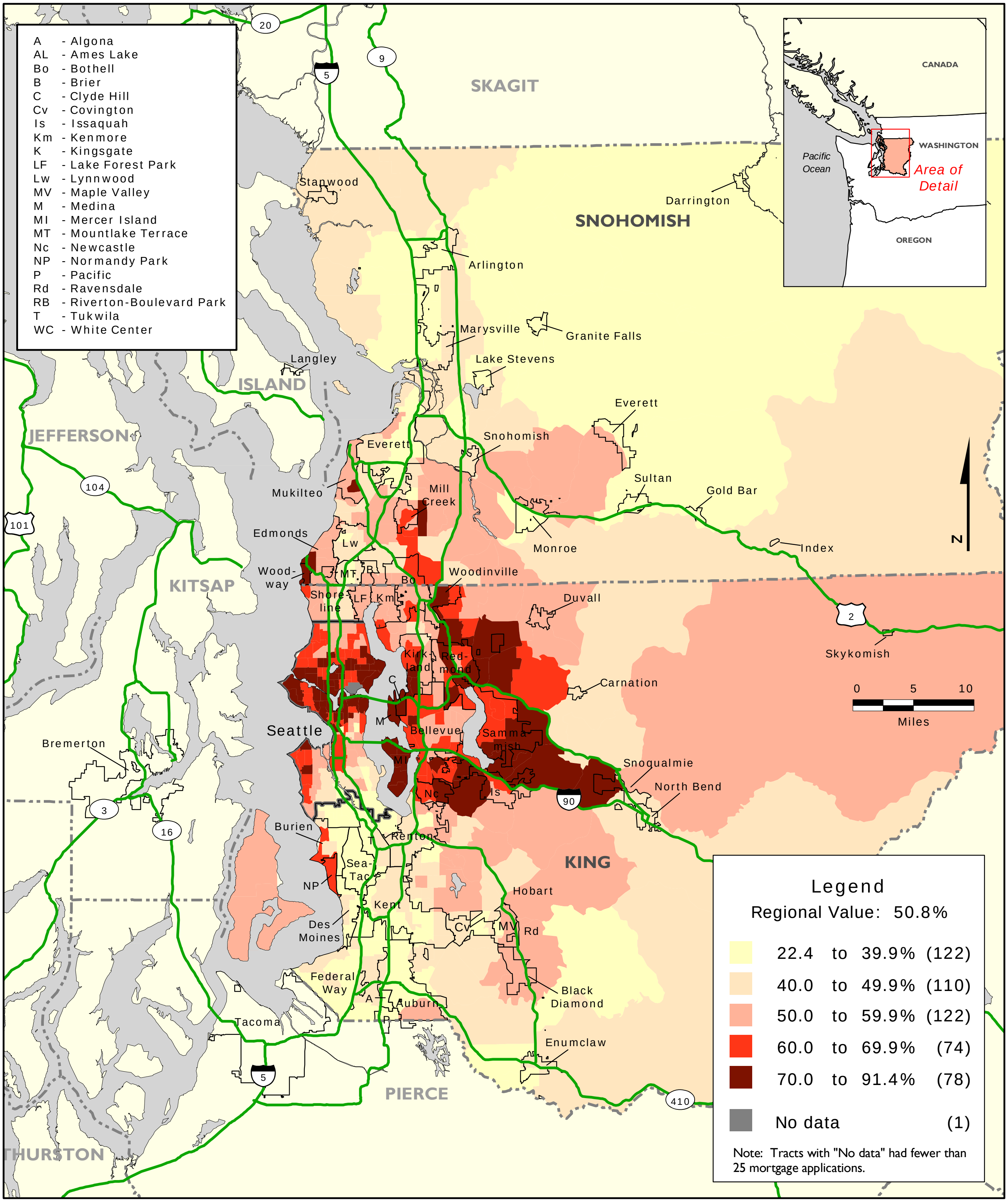
Map 15: SEATTLE PRIMARY REGION
Percentage of Applicants Applying at Prime Lenders by Census Tract, 2004-2006



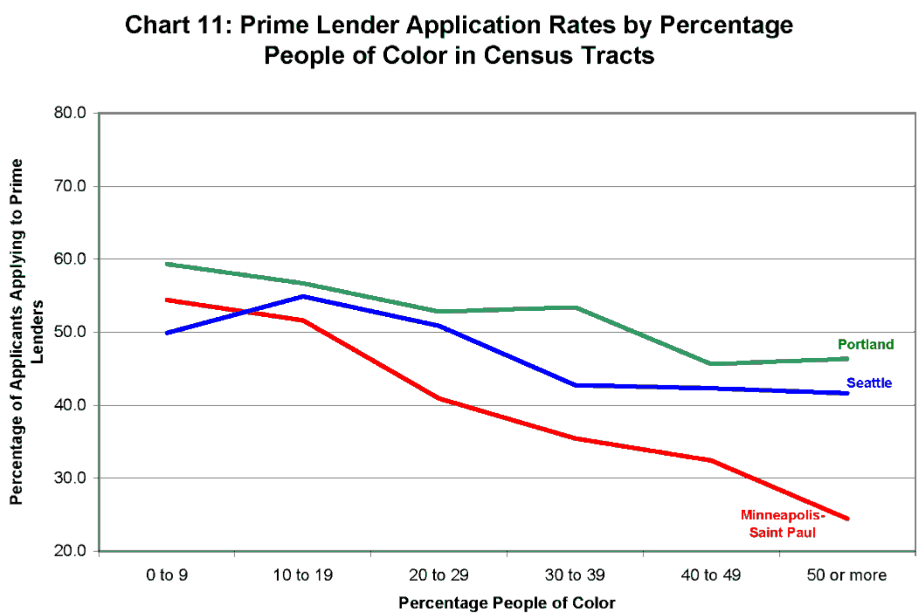
Source: FFIEC, Home Mortgage Disclosure Act.

C. Comparisons across the Metropolitan Areas

As noted in the previous section, the relationships between prime lender application rates and neighborhood demographics tend to be most distinct in Minneapolis-St. Paul. However, this does not mean that the relationships do not exist in the Portland and Seattle areas. There are relatively clear application rate differences across neighborhood types in each of the metros, with areas that have lower incomes and higher shares of people of color in the comparison.

Neighborhood Prime Lending and Race

The Minneapolis-St. Paul metro shows a trade-off between neighborhood diversity and prime lender application rates that is clearly stronger than in the other two metropolitan areas. (Chart 11) The difference lies largely in the region's neighborhoods with the highest non-white shares. Prime lender rates are similar across the metros at high incomes, but the rates decline much more sharply as racial diversity increases in the Twin Cities. The result is that prime lender application rates are distinctly lower in Minneapolis-St. Paul than in the other two metros in non-white segregated neighborhoods.



Neighborhood Prime Lending and Income

The three metros look much more similar when comparing the relationship between prime lender application rates and income. (Chart 12) The application rate trade-offs with income—the slopes of the three lines—are very similar, except that Minneapolis-St. Paul shows a much steeper drop-off in prime lender rates in the lowest income category.

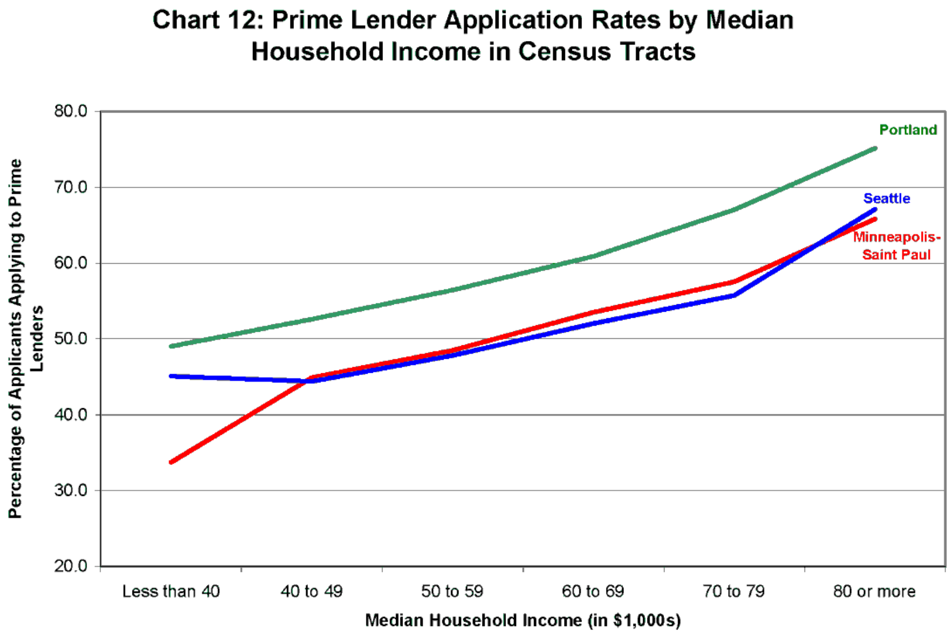


Chart 12: Prime Lender Application Rates by Median Household Income in Census Tracts
Percentage of Applicants Applying to Prime Lenders
80.0
70.0
60.0
50.0
40.0
30.0
20.0
Portland
Seattle
Minneapolis-Saint Paul
Less than 40
40 to 49
50 to 59
60 to 69
70 to 79
80 or more
Median Household Income (in $1,000s)

V. Equal Access to Credit

Families living in segregated communities of color are disproportionately unlikely to apply for prime loans, to live near a traditional bank, and disproportionately more likely to live near a non-conventional or payday lender. The racial composition of neighborhoods is related to access to good, affordable credit. In low income communities of color, high cost loans— both in the home mortgage market and small consumer loan market—are much more common than they are in white and middle-class communities. Poor people of color pay more for loans—an extra cost that many families can ill-afford. Some of this cost can be attributed to the higher risk involved in lending to some low income people. However, civil rights laws are implicated in this lending to the extent the banks make their services less available or market higher cost loans specifically marketed to communities of color. One civil rights law, the Community Reinvestment Act, can be used proactively to encourage banks to make low-cost loans available in communities of color.

Federal Fair Lending Regulation

In 2005, the FDIC issued draft guidelines on payday lending. One of the dangers to the financial stability of banking institutions involved in payday lending was the potential for lawsuits for violations of anti-discrimination and consumer protection law. The draft guidelines directed examiners to "determine to whom the products are marketed, and how the rates or fees for each program are set, and whether there is evidence of potential discrimination."[78]

While some of the racial disparities in the location of payday lenders described in the previous section may be related to nondiscriminatory market forces, the fact remains that large racial disparities in lending should not exist. Years of housing discrimination and redlining led to an impressive body of anti-discrimination law, most of which applies to equal access to fair credit, including the Equal Credit Opportunity Act (ECOA)[79] and the Community Reinvestment Act.

Racially targeted subprime or predatory loans obviously invoke civil rights laws, most notably the Fair Housing Act and the Equal Credit Opportunity Act. Likewise, racially targeting of high-cost payday loans, including location decisions based on neighborhood racial demographics could violate the ECOA. The ECOA bans discrimination against applicants in respect to any credit transaction on the basis of race, color, religion, national origin, sex or martial status or age.

The lack of traditional banks lenders in communities of color could also positively violate the ECOA. Traditional banks, such as Bank of America and Wells Fargo, extend lines of credit to payday lenders.[80] These lines of credit allow payday lenders to, in turn, make loans. This arrangement is similar to banks' extension of credit to mortgage brokers—federal regulators

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[78] FDIC FIL-14-2005, "Guidelines for Payday Lending," (Feb. 25, 2005) available at http://www.fdic.gov/news/news/financial/2005/fil1405a.html (last visited July 15, 2009).

[79] Equal Credit Opportunity Act, and Sections 1981 and 1982 of the Civil Rights Acts when their actions make housing, credit, or contract rights unavailable because of the plaintiff's protected class.42 U.S.C. §§ 3601-3619 (2006); 15 U.S.C. § 1691 (2006); 42 U.S.C. § 1981 (2006); 42 U.S.C. § 1982 (2006); 42 U.S.C. § 1983 (2006); 12 U.S.C. §§ 2901-2908; See Schemm, (1995).

[80] National Consumer Law Center (2007). These loans and lines of credit are also available in publicly traded Payday lenders SEC filings.

have warned banks that this practice could violate fair lending laws.[81] Federal antidiscrimination law holds these secondary market participants liable for condoning discrimination in the primary market. While the official staff commentary to the ECOA regulation B expressly indicates that secondary market participants' *purchase* of loans can violate the ECOA insofar as the purchaser influences the outcome of the loan. However, under the ECOA "term creditor includes all persons participating in the credit decision,"[82] which should include the bank that made the line of credit available to the payday lender. To the extent that traditional banks make lines of credit available to payday lenders that they know target communities of color, the elderly, disabled, or women for high cost or otherwise predatory loans, these banks might violate the ECOA.

Further, anti-discrimination law can be violated when a bank has both payday and other short term lending programs that carry considerably dissimilar rates of interest or pricing structures.[83] For instance, banks decisions not to enter the lending market in a community of color, but to provide a line of credit to payday lenders that do –effectively leading to one sort of credit for communities of color and another for white communities—could be argued violate the ECOA.

The Community Reinvestment Act

In 1977, Congress passed the Community Revitalization Act (CRA), which was designed to eliminate redlining and encourage investment in impacted communities by "encourag[ing] regulated financial institutions to help meet the credit needs of their entire communities, including low- and moderate-income neighborhoods, consistent with safe and sound operations."[84]

In the home mortgage market, research finds that CRA covered institutions are much less likely to make high-cost loans to low-moderate income borrowers than lenders that are not covered by the CRA.[85] Moreover, communities with more CRA-covered lenders (usually traditional banks) experience more prime lending and fewer foreclosures than communities with few covered lenders.[86] In other words, research suggests that federal laws that put pressure of traditional lending institutions to make good-quality, affordable loans to LMI families actually work.

In recent years, federal agencies have become more interested in promoting affordable small, short terms loans though the CRA.[87] In 2008, the FDIC launched the Small Dollar Loan Pilot program. The program rewards banks that make payday-sized loans at affordable interest rates. The APR on these loans is capped at 36 percent and must contain an automatic savings component. The FDIC states that lending programs that help move families away from payday loans "would be considered particularly responsive to community needs."[88]

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[81] 42 U.S.C. §§ 3601-3619 (2006); 15 U.S.C. § 1691 (2006); 24 C.F.R. § 100.125(b) (2007); 12 C.F.R. § 202.2(l), Official Staff Commentary § 202.2(l).
[82] Official Staff Commentary § 202.2 2(l) 1.
[83] ECOA regulation B.
[84] 12 U.S.C. § 2903(a) (2005).
[85] Paying More for the American Dream III (2009)
[86] FDIC Issues Final Guidelines on Affordable Small-Dollar Loans, June 19, 2007.
[87] Affordable Small-Dollar Loan Guidelines, available at http://www.fdic.gov/SmallDollarLoans/.
[88] Ibid.

VI. Payday Lending Reform

At its worst payday lending is comparable to early twentieth century loan sharking. at its best, it is comparable to micro finance projects carried out in the global South.[89] While the practice is not exactly loan sharking—no one will actually come break your legs if you do not pay back your payday loan (although they may harass you and/or take you to court)—the practice is also far from the microfinance model which is intended to allow families to start businesses and increase their long-term standard of living. Payday lending is associated with a host of public and private costs including an increased risk of bankruptcy.[90]

In the 1990s, the Consumer Federation of America and USPIRG began to raise the alarm about the costs of payday lending.[91] These concerns and growing public discomfort about the debt-trap created by payday loans has led most states that permit payday lending to enact some sort of regulation. Several states, including Oregon, have capped the interest rate on payday loans. Others, like Washington, have attempted to limit rollovers. While the bans on roll-over and "cooling off" periods between payday loans tend to be easier to pass in state legislatures—these bills tend to be supported by the payday loan industry—rate caps are the most effective means of reducing the cost of payday lending.

State Regulation: Rate Caps

In 2001, North Carolina, one of the first states to legalize payday lending, became the first to re-ban it. In 2007, Oregon passed rate caps that effectively ban traditional payday loans. In the wake of these bans, several industry-sponsored studies examined their effects. These studies tended to find that consumers were worse off.[92] Studies by other academics and advocacy groups tend to refute the industry-sponsored studies and find that the rate-caps had little effect on the borrowing habits of consumers.[93]

North Carolina allowed its payday lending legislation to sunset in 2001, effectively capping the interest on small loans, those under $600, at 36%.[94] North Carolina's Attorney General then aggressively prosecuted payday lenders, such as Advance America, that continued to do business in the state.[95] By 2006, the last payday lenders operating in the state agreed to end operations.[96] Because North Carolina was a pioneer both with the advent of payday lending and its abolishment, and because the state has been particularly persistent about actually ending payday lending within the state, the state experience has been extensively studied. In fact, The Center for Responsible Lending, one of the advocacy groups that first blew the whistle on payday lending is

89 See Douglas McGray, Check Cashers, Redeemed., New York Times, Nov. 9, 2008.
90 Skiba (2008).
91 Consumer Federation of America (1998).
92 Donald P. Morgan and Michael R. Strain (2007).
93 Center for Community Capital (2007).
94 North Carolina Consumer Finance Act. N/C/G/S/ § 53-15.
95 North Carolina Attorney General, Press Release. March 1, 2006 "Payday Lending on the Way Out in North Carolina: AG Cooper says major payday lenders agree to stop loans."
96 Ibid.

located in Durham, North Carolina. In 2005, the Center released a report finding concentrations of payday lenders in communities of color in North Carolina.[97]

After the lending ban, advocacy groups, industry groups, and scholars examined the outcome of the payday loan ban for North Carolina consumers. The Center for Community Capital at the University of North Carolina examined the availability of credit for North Carolina families, and found that very few households were impacted by the end of payday lending.[98] The study also found that former payday borrowers were pleased with the payday ban.[99]

Donald Morgan Strain, a researcher affiliated with the Federal Reserve Bank of New York, and Michael Stain, however, found more bounced checks, complaints to federal authorities about lenders and debt collectors, and more federal bankruptcy filings in North Carolina and Georgia (both of which had payday bans) than in states that allowed high-cost payday lending.[100] The Morgan study has been criticized for failing to note that the regional check processing centers, where the researchers got their data on bounced checks, are regional processing centers.[101] This means that half the data on bounced checks used to illustrate the increase in bounced checks in North Carolina actually came from states that allow payday lending.[102]

Similarly, Morgan and Strain study's data concerning bankruptcy filings do not account for the broad changes in the bankruptcy code that occurred during the study.[103] The data about the increase in complaints about debt collectors was also problematic: the Fair Debt Collection Practices Act allows consumers to complain about third party debt collectors, but not about the lender.[104] Since many payday lenders keep their collection efforts in-house, these complaints were not collected by the FTC, the federal regulator.[105]

Overall, it seems that North Carolina's regulation has lowered the number of high cost loans taken out in the state without substantially increasing bank overdrafts or other problematic alternatives to payday loans.

State Regulations: Methods Other than Rate Caps

Other states, like Washington have implemented a bevy of payday lending regulations short of rate-caps. These regulations have included limits on the number of payday loans a borrower can have outstanding, cooling-off periods between loans, and lender disclosure requirements. Many of these reforms have been advocated by payday lenders as alternatives to rate-caps.[106] However,

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[97] Kind et al. (2005)
[98] Center for Community capital (2007).
[99] Ibid at 17.
[100] Morgan and Strain (2007)
[101] Center for Responsible Lending (December 10, 2007).
[102] Ibid.
[103] The study also only controlled the bankruptcy data for unemployment, and not for a host of other usually controlled, relevant factors, such as income, and health insurance rates. Ibid.
[104] 15 U.S.C. §§ 1692-1692
[105] Ibid.
[106] See Community Financial Services Association of America, "Best Practices for the Payday Advance Industry," available at http://www.cfsa.net/industry_best_practices.html.

research by the Center for Responsible Lending found that only interest rate caps at or around 36 percent, the amount set by North Carolina and the federal government's cap for lending to military families, prevents borrowers from becoming trapped in cycles of repeat borrowing or loan flipping.[107] Other measures, including those used in Minnesota and Washington, such as renewable bans, cooling-off periods, payment plans, loan caps based on borrower's income, state-wide databases, and regulations that narrowly target only payday loans have not stopped payday loan roll-overs.

Consumer Disclosures

Payday and other high cost lenders, along with some economists, often argue that regulation of loan terms and bank locations is unnecessary. The solution, they argue, is consumer education. Provide consumers with information about good and bad loans and rational consumers will make the choices that are best for their families. The purpose of the federal Truth in Lending Act (TILA) is to create informed consumers by requiring lenders to provide true estimates of loan costs. The act reads: "The informed use of credit results from an awareness of the cost thereof by consumers. It is the purpose of this title to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit, and to protect the consumer against inaccurate and unfair credit billing and credit card practices."[108] The act applies to most loans and requires disclosure of the cost of the loan in terms of APR.

Most payday lenders comply with TILA, and many state laws including the laws of Minnesota,[109] Oregon,[110] and Washington[111] either require TILA disclosures or require TILA plus even more disclosures. For example, Minnesota requires payday lenders to post signs stating that borrowers could get the same loan for less elsewhere.[112] All three states require conspicuous posting of fees and charges, both on websites and offices, as well as on customers' receipts. Payday lenders have largely supported these provisions, in part, perhaps, because they do not work.[113]

TILA and state laws exceeding TILA give consumers volumes of information about the cost of the respective loans and give information that creates the possibility of consumers comparison shopping for loans. However, there is little evidence that providing consumers with "disclosure and unfettered choice" leads to financially sound consumer choices.[114] While consumer disclosures appear to be a tool to strengthen consumer rights there is little evidence that either consumer disclosures or consumer education leads to better financial decision-making.[115]

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[107] Urian King and Leslie Parrish, Springing the Debt Trap (2007)
[108] 15 U.S.C. § 1601 et seq..
[109] 2008 Minnesota Statutes Section 47.60, subdivision 4(e).
[110] 2007 Oregon Revised Statutes section 725.345.
[111] Revised Code of Washington 31.45.060.
[112] 2008 Minnesota Statutes Section 47.60, subdivision 4(e).
[113] See Community Financial Services Association of America, "Best Practices for the Payday Advance Industry ," available at http://www.cfsa.net/industry_best_practices.html (last visited July 15, 2009).
[114] Willies (2008).
[115] Ibid., Barr et al. (2008).

In the case of payday lending, it is even less likely that in-store disclosures or consumer education campaigns will effectively steer families away from unaffordable payday loans. Consumers who seek payday loans are already facing serious, unexpected financial shortfalls. Even economists do not expect rational market decisions from payday borrowers[116]—payday borrowers borrow from these lenders because they overestimate their ability to repay loans.[117]

While requiring payday lenders to comply with federal truth in lending regulations may make states think that they are giving borrowers the tools to make sound decisions, the truth is that borrowers facing a financial shock are usually not in a position to effectively evaluate the relative costs and benefits of taking out these loans. The social costs of these debt-traps were the reason why salary assignments (otherwise known as loans sharking) were prohibited over 100 years ago in most states.

Effectively Unregulated: Internet Lending

While high-cost payday loans are generally unavailable at store fronts in many states, these high cost loans are available on the internet. Internet payday loans, tout fast-approval, no background checks, and immediate cash. A 2004 survey by the Consumer Federation of America of internet payday lenders found that internet disclosures often misstate APR's, do not include the finance fees in the APR, and generally make it difficult for consumers to access the true cost of the payday loan.[118] Many internet sites allow renewal without limits and some actually automatically refinance loans.[119]

Most states, including Oregon and Washington, in theory regulate payday lenders under the same rules as payday lenders within the state.[120] In practice, states have difficulty regulating payday lenders. While a few states have convinced courts to apply their consumer protection laws and payday lending regulations to payday lenders,[121] in practice internet payday lenders offer loans to consumers, even in states that ban payday lending.[122] In a few states, state attorney generals have gotten cease and desist orders against payday lenders. However, payday lenders, much like online gambling sites, continue to make loans to consumers in these states. While the loan companies may not be able to collect on these loans in court, most payday customers pay most of the loan and added fees before defaulting.[123] Further, since many of these on-line lenders have mandatory arbitration clauses in their consumer contracts and some even require consumers to

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[116] Elliehausen and Lawrence (2001)
[117] Skiba and Tobacman (2008)
[118] Consumer Federation of America (2004) at 23
[119] Ibid at 24.
[120] Revised Code of Washington, section 31.45.105 (1)(d). OR 725.602. Minnesota is one of the very few states that does not currently state that it regulates internet lending. The Minnesota Department of Commerce issued a notice stating its intent to regulate internet payday lending to Minnesota consumers in 2008. This regulation was struck down by an administrative law judge on the grounds that the agency did not go through the proper rulemaking procedure. Since this decision, the state has not attempted to regulate internet lenders.
[121] Note that attempts by payday lenders to get consumers to agree to the legal fiction that the loan in occurring in a different state than the state in which the consumer is located, have generally been unsuccessful.
[122] Jean Ann Fox, Anna Petrini, "Internet Payday Lending: How High-priced Lenders Use the Internet to More Borrowers in Debt and Evad4e State Consumer Protections," Consumer Federation of America, November 30, 2004 p. 21.
[123] Ibid.

agree not to participate in class action lawsuits against the lenders, it is difficult for individual consumers to challenge the legality of the lenders practices by filing restraining or other orders in courts.[124]

State-by-state attempts at regulating internet payday lending have been less than totally effective because of the pervasive nature of the internet. States' refusals to enforce payday lenders debt collection attempts can go part-way to ending payday lending over the internet, but federal laws regulating payday lending over the internet would be more effective. There is some strong recent precedent for federal regulation of certain types of payday lending. In 2006, the federal government banned payday loans with APRs exceeding 36 percent to active-duty military families (the regulation emerged from a finding by the Department of Defense that payday lending was hurting military readiness).[125]

VII. The Continued Need for Small Loans: Banks and Credit Unions

Banks and credit unions do provide an avenue for consumers to absorb financial shortfalls. A North Carolina survey found that over a three year period, 28 percent of respondents took out a bank loan during a recent financial shortfall and 23 percent took out overdraft protection loans, compared to 11 percent using a pawnshop and 8 percent using a payday lender. More than half of those surveyed, however, did not pay bills on time or at all.[126] For low income borrowers, there is an absence of small loan products to help with such shortfalls. Banks and credit unions have not often met this demand because their business models make it difficult to make such loans.

Banks do not typically make small personal loans to low income persons because they face stockholder pressure to increase their earnings. The drive to maximize profits impedes banks from developing customizable lower cost products and making localized risk assessments for low income persons. Technological advances in credit scoring also impede banks from making localized decisions about lending to low income persons, who often do not fit neatly into industry risk assessment categories such as home ownership, credit history, collateral, capital, etc.[127] The lack of institutional knowledge about underserved communities and the rise of automation and standardization of finance further institutionalizes bias against the historically underserved.[128]

Banks have also begun to rely on fee-based banking revenue whereby banks gain more revenue through fees and service charges, such as overdraft protection, than revenue collected from interest payments. Such fees fall outside of usury laws and truth in lending regulations. Fee-based banking has also turned customers with poor credit ratings from a liability into a commodity, with such products having some of the negative caveats of payday loans.[129] Banking

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[124] CFA 2004 at 25.
[125] Public Law 109-364, the John Warner National Defense Authorization Act for Fiscal Year 2007, Section 670, "Limitations on Terms of Consumer Credit Extended to ServiceMembers and Dependents," (October 17, 2006.)
[126] Center For Community Capital,(2006).
[127] Tansey, (2007).
[128] Listokin and Wyly 2000, 589-590
[129] Stegman, (2007).

institutions also do not nor clearly explain rates and fees. In some cases low income persons have a general mistrust of banks.[130] The mistrust of banks is particularly common with communities of color that have faced discrimination in lending.[131]

There are some examples of public-private banking initiatives, however, for making small loans to low income persons. In Chicago, ShoreBank provides banking services to low income families using bank debit accounts, originally based on public assistance deposits. Currently about half of customers also use the account for purposes other than public assistance, which can act as small loan provider. Governments have also created incentives for lenders to lend to low income people. For instance, the City of San Francisco provides free marketing to banks and credit unions that provide products and services to low income persons.[132]

Credit unions also have not often met the needs of low income borrowers, even though their original stated purpose was to serve persons with modest means. In 2006 only about 1,000 of the 9,000 credit unions in the U.S. had small loan products, alternatives to payday loans.[133] Some credit unions incorporate higher cost fee-based products like many banks do, while others have begun to more directly compete with payday lenders, providing low cost-products.

A major push to provide low cost small loan alternatives to payday loans was made by the North Carolina State Employees Credit Union (SECU). The credit union introduced the salary advance product, a short term loan with a 12 percent APR. To help its members absorb future financial shocks it puts five percent of salary advance loan proceeds into customers' savings accounts. SECU's salary advance has been highly successful making over 1,000,000 loans for a total of $397,497,122, with a modest 90-day delinquency rate of 0.65%.[134]

A joint partnership between Pennsylvania's Credit Union Association and the Pennsylvania State Department of Banking offers a similar savings component (18 percent APR) to small loans made through the credit union.[135] Other credit unions have subsequently set up lower cost small loan products, including in Ohio and Virginia.[136] Another credit union in Wisconsin makes use of a new small loan software program to expedite processing loans.[137]

While some credit unions have managed to serve low income communities with relatively low default rates they often struggle to gain a foothold in the market. In the 1990s, about half of credit unions serving low income communities failed and closed. Credit unions fail because they lack capital, liquidity and staffing, and consequentially only offer a limited range of services to customers. High default rates are not a leading reason why credit unions serving low income borrowers fail. One potential remedy for the shortage of capital and liquidity is for credit unions to partner with other conventional lenders, which could provide the credit union with capital to

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[130] Blank, (2008).
[131] Engel and McCoy, (2007).
[132]Blank(2008).
[133] Kirchoff, (2006).
[134] Center For Community Capital (2006): Kirchoff, (2006); Stegman, (2007).1
[135] Credit Union Journal, Pennsylvania CUs Offer 'Better Choice' As Alternative to Payday Loans, March 26th[h] 2007
[136] Credit Union Directors Newsletter, Payday Loan Alternatives Answer Members' Plea, October 2008.
[137] Credit Union Journal. Peoples Choice is Offering Solution To Combat Payday Lending, March 10thth 2008

make small loans, foster cross-referrals between the establishments and could help conventional lenders fulfill their Community Reinvestment Act (CRA) obligations.[138]

Financial institutions under the Federal Deposit Insurance Corporation (FDIC) are called to promote debt products that have affordable rates under the FDIC's Affordable Small-Dollar Loan Products Guidelines. The guidelines recommend underwriting that considers the ability to repay, working with other organizations, incorporating a savings component to small loans and providing assistance for the financial education of borrowers. Participation in such practices can qualify institutions for CRA credits.[139]

VIII. Beyond Banks: Fixing the Safety Net

*Do you have medical bills to pay, bills that were the result of an illness or injury that was completely unforeseen? A **cash advance** or a **payday loan** could be just what you need to help pay that hefty deductible. Medical bills are becoming more and more of an issue for working people as more and more procedures are not covered by a healthcare plan. At Speedy Cash we hope to help keep you covered by providing payday loans to get you through the healthcare crisis. Payday loans are a perfect fit for this situation as bank are very unlikely to help in this predicament, they only want to loan larger amounts of money, not smaller loans that are best handled by payday loans.*[140]

The income gap between the rich and the poor in the United States has been growing since the 1970s. While the income of the richest 25 percent of Americans has steadily increased, incomes for the bottom 25 percent have held steady.[141] The wealth gap, the gap in net household assets minus debts, is even larger. By 2004, the bottom quintile of American households had no net wealth.[142] Survey research conducted by the Kaiser Commission found that many low and middle income families had trouble affording basic necessities, such as food, transportation, child care, and housing.[143] The cost of household expenses combined with increasing income instability makes it difficult, if not impossible for households to generate enough savings to create a safety net.[144]

There is obviously a need for small consumer loans and short-term loans need to be somewhat costly in order for them to be economically feasible for business. The very fact, however, that large numbers of families turn to payday loans to pay basic expenses means that many families are living at the very edge of their budgets and unexpected expenses are sending families into long-term debt. For example, in 2004, the Oregon Division of Finance and Corporate Security found that Oregonians were regularly using payday loans to purchase groceries.[145] While this

[138] Tansey, (2007).
[139] Center For Community Capital, (2007). Affordable Small-Dollar Loan Products Final Guidelines. FIL-50-2007. June 19. ttp://www.fdic.gov/news/news/financial/2007/
[140] http://www.speedycash.com/blog/post/Help-with-Medical-Bills.html last accessed 05/29/2009
[141] Zhu Xiao Di (Feb. 2007).
[142] Ibid.
[143] Kaiser Commission (2009).
[144] Barr (2008).
[145] Oregon Division of Finance and Corporate Securities, “Payday Loans in Oregon.” (2004).

disclosure shocked many Oregonians, in truth many American families' paychecks do not cover household expenses, much less economic shocks like large medical bills or loss of employment. Simply making the debt less expensive will not stabilize these families.

High—or moderate—cost loans cannot resolve the problem of increasing economic security for lower and even middle income Americans.[146] Payday and other predatory lending and the attendant consequences for families and communities will remain until real fixes to the social safety-net are implemented. While many failures of the social safety net cause stress to low and moderate income families, the cost of health care emergencies appears to have a disproportionate and severe effect of families' financial stability.

The average payday borrower is low income, earning less than 200 percent of the federal poverty level for a family of four ($42,800 in 2008). Borrowers also tend to be young, unmarried women who have a have a high school, but not a college degree.[147] This is constant with the profile of the payday borrower who earns enough to warrant checking account—meaning that they are not the poorest of the poor, they are the working poor. These are the people who make too much money to qualify for Medicaid and who work in jobs that are relatively unlikely to come with good health insurance.[148]

[146]Historically, states have developed usury laws during times when the income inequality is high. Glaeser (1994).
[147] Logan and Weller (2009) (4) Data from the Federal Reserve's triennial Survey of Consumer Finances.
[148] Federal Medicaid is generally available for families earning less than 133% of the federal poverty level (FPL). In 2007, the federal poverty line for a family of four was $20,650. Data available at www.ssa.gov/policy/docs/statcomps/supplement/2007/medicaid.html.
State SCHIP programs offer expanded coverage, but even very generous programs limit eligibility to 250% of FPL for adults without children. Thirty-two thousand dollars is about 250% of the FPL for a family of two. Most uninsured single adults are ineligible for public coverage and have family incomes below 300% of poverty similarly; most uninsured parents have incomes below 300% of poverty. Dubay et al. (2006).

Table 8: Percentage Uninsured by Race and Income in Three States, 2005

Minnesota	Total	% of Poverty Line > 250%	% of Poverty Line <= 250%
Black	14.7	8.8	18.5
Hispanic	28.2	16.7	35.4
White	8.0	5.0	17.6
All Other Races	14.1	7.8	21.1
Total	9.5	5.5	19.6

Oregon	Total	% of Poverty Line > 250%	% of Poverty Line <= 250%
Black	22.0	13.5	28.7
Hispanic	37.8	22.0	44.9
White	15.6	9.1	28.0
All Other Races	21.8	13.1	32.7
Total	18.7	10.1	31.8

Washington	Total	% of Poverty Line > 250%	% of Poverty Line <= 250%
Black	17.5	12.1	22.8
Hispanic	28.8	17.5	35.3
White	12.0	7.3	23.8
All Other Races	16.6	10.1	26.2
Total	14.3	8.2	26.2

Source: U.S. Census Bureau, Small Area Health Estimates

According to the U.S. Census Bureau in Minnesota, 9.5 percent of the population is uninsured, while in Washington 14.3 percent and in Oregon 18.7 percent are uninsured. (Table 8) People with low to moderate incomes have even higher uninsured rates. For those with incomes less than 250 percent of the poverty line, 19.6 percent in Minnesota, 26.2 percent in Washington and 31.8 percent in Oregon are uninsured. There are also racial disparities, especially for Hispanics who are more than twice as likely to be uninsured than whites in all three states. In all three states, Blacks and Asians also lag behind whites in health insurance coverage. Being underinsured or uninsured is, of course, predictive of having difficulty paying medical bills and of acquiring medical debt.

Medical bills and medical debt are "tied to a market for a service that is often life-saving and for which the customer is, by definition, vulnerable."[149] The pressure to pay off medical bill is intense; consumers often believe that failure to pay medical bills will limit their access to future medical care.[150] In one national survey, one quarter of respondents had been unable to pay for food, heat, or rent because of medical debt.[151] The extreme financial pressures put on individuals as a result of medical debt, could lead people to take out exploitative or predatory loans, leading to a spiral of bad debt.[152]

Medical debt, and correspondingly, un-insurance and underinsurance are a driving part of American's need for small consumer loans and people's willingness to take-out extremely high-cost loans. The cost of health care and medical debt is a driving force in mortgage foreclosures, bankruptcy, and probably acquiring payday debt. While banning payday loans might turn the uninsured and underinsured to more affordable types of credit, medical debt for the working poor will continue to be a driving force in the acquisition of debt and a force that drives families to acquire predatory debt unless something is done to reduce the cost of healthcare for the working poor.

[149] Siefert (2004) at 789.
[150] Siefert (2004).
[151] Collins et al. 2004.
[152] Seifert (2004)

IX. Conclusion and Recommendations

Payday lending – entails a high costs for families and metropolitan regions. While there is a definite need for short term credit, payday lending practices have been shown to drive families deeply in debt. Payday lending is associated with a host of negative consequences, including delayed medical care,[153] increased evictions,[154] credit card delinquencies,[155] involuntary bank account closures,[156] and bankruptcy.[157]

The racial composition of neighborhoods is related to access to good, affordable credit. In the metropolitan areas of Minneapolis-St. Paul, Portland and Seattle, families living in segregated, communities of color are disproportionately unlikely to apply for prime loans, to live near a traditional bank, and disproportionately more likely to live near a non-conventional or payday lender. In low-income communities of color, high cost loans— both in the home mortgage market and small consumer loan market—are much more common than they are in white and middle-class communities. Poor people of color pay more for loans—an extra cost that many families can ill-afford.

Racially segregated communities of color tend to have fewer banks, more check cashers and payday lenders, especially in Minneapolis-St. Paul where non-white segregated census tracts are more numerous and concentrated in the lower-income core of the region. There are major differences across the three regions in the neighborhood shares of lenders by income and race. Lower income neighborhoods in Portland and Seattle showed much greater access to conventional lenders than in Minneapolis-St. Paul. However, non-conventional lenders tend to be disproportionately in lower income neighborhoods in all three metros.

While the bans on roll-over and "cooling off" periods between payday loans tend to be easier to pass in state legislatures—these bills tend to be supported by the payday loan industry—rate caps are the most effective means of reducing the cost of payday lending.

For low-income borrowers, there is an absence of small loan products to help with such shortfalls. Banks and credit unions do provide an avenue for consumers to absorb financial shortfalls. Banks and credit unions, however, have not often met this demand because their business models make it difficult to make such loans. High—or moderate—cost loans, however, cannot resolve the problem of increasing economic security for lower and even middle income Americans.[158] Payday and other predatory lending and the attendant consequences for families and communities will remain until real fixes to the social safety-net are implemented.

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[153] Melzer, (2008).
[154] Michael S. Barr 2008)
[155] Aragwal et al (2009)
[156] Campbell at al (2008).
[157] Skiba and Tobacman (2008).
[158] Glaeser (1994).

Recommendations

- **Effectively Regulate Payday Lending**

  - Rate caps are, by far, the most effective way to reign in the cost of payday lending: research by the Center for Responsible Lending has concluded that interest rate and fee caps are the most effective way to limit the cost of payday loans.
  - Federal regulation is necessary to regulate internet payday lending. States cannot effectively limit payday lending over the internet; therefore, federal action is necessary.
  - Minnesota needs to close its industrial thrift loophole: Minnesota's industrial thrift statute allows payday lenders to charge far in excess of the APRs contemplated by the Minnesota Legislature when it legalized payday lending. The Minnesota Legislature should act quickly to end the circumvention of its consumer regulation.

- **Encourage Programs that Provide Access to Affordable Credit**

  - Expand the CRA pilot program: The CRA small dollar loan pilot program is an excellent start in encouraging traditional lenders to make affordable, small loans to the working poor. This program should be expanded.
  - Establishments such as North Carolina State Employees Credit Union have shown that lower cost small loan products can be profitable. Credit unions provide small loans when supported by state agencies and other lenders. State and federal programs that aid the short-term needs of low income borrowers could increase this capability.
  - Credit unions that lack resources to provide small loan products can partner with other lenders through the CRA small dollar loan program.

- **Fix the Safety Net**

  - Support policies designed to lower the income gap between the richest Americans and the poorest Americans.
  - Support policies that ensure access to necessities for all Americans, including transportation, health care, and childcare.
  - Support for universal health care coverage with low individual premiums would curb some of the most severe burdens on the budgets of working families.
  - Federal and state poverty relief programs should cover the working poor—those making 150 to 300% of the Federal Poverty Level.

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