Fiscal Note & Local Impact Statement

127 th General Assembly of Ohio

Ohio Legislative Service Commission
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BILL: **Sub. H.B. 545** DATE: **May 14, 2008**

STATUS: **As Reported by Senate Finance and Financial Institutions** SPONSOR: **Rep. Widener**

LOCAL IMPACT STATEMENT REQUIRED: **No — Minimal cost**

CONTENTS: **Revises Ohio's consumer finance lending laws and makes other changes**

State Fiscal Highlights

STATE FUND	FY 2009	FY 2010	FUTURE YEARS
General Revenue Fund – Treasurer of State			
Revenues	- 0 -	- 0 -	- 0 -
Expenditures	Increase up to several hundred thousand dollars	Increase up to several hundred thousand dollars	Increase up to several hundred thousand dollars
Consumer Finance Fund (Fund 5530) – Department of Commerce			
Revenues	Potential loss of up to $807,000 in transfers to the Financial Literacy Education Fund	Potential loss of up to $267,000 in transfers to the Financial Literacy Education Fund	Potential loss of up to $267,000 annually in transfers to the Financial Literacy Education Fund
	Potential loss in license fees	Potential loss in license fees	Potential loss in license fees
Expenditures	Potential decrease in administrative costs	Potential decrease in administrative costs	Potential decrease in administrative costs
Financial Literacy Education Fund (New Fund) – Department of Commerce			
Revenues	Potential gain of up to $807,000 in transfers from the Consumer Finance Fund	Potential gain of up to $267,000 in transfers from the Consumer Finance Fund	Potential gain of up to $267,000 annually in transfers from the Consumer Finance Fund
Expenditures	Increase for program operation	Increase for program operation	Increase for program operation

Note: The state fiscal year is July 1 through June 30. For example, FY 2009 is July 1, 2008 – June 30, 2009.

Department of Commerce – Division of Financial Institutions

- ***Consumer Finance Fund revenue*.** FY 2007 revenue from check-casher and check-casher lender license fees was $1.6 million. The changes in the bill will cause payday lenders to adjust their business plans, either by leaving the loan market or modifying their loan products to comply with the new lending requirements in the bill. These changes will affect license revenue deposited in the Consumer Finance Fund (Fund 5530).

- ***Administrative costs*.** The bill requires the Division of Financial Institutions (DFI) to examine the records of short-term loan licensees at least annually and publish certain reports. These requirements may increase administrative workload, as check-cashers and check-casher lenders make up about 22% of the active consumer finance licenses that DFI oversees. However, the administrative burden could actually decrease if current licensees opt out of the short-term loan market.

- ***Financial Literacy Education Fund*.** The bill requires the Department of Commerce to provide adult financial literacy programs to consumers. In order to fund such programs, the bill creates the Financial Literacy Education Fund and capitalizes it with a one-time transfer of 5% of the cash balance of the Consumer Finance Fund. Based on the current cash balance in that fund, this would yield $540,000 in start-up funding. The new fund would be supplemented by quarterly transfers of 5% of all charges, penalties, and forfeitures deposited in and transferred from the Consumer Finance Fund. That revenue could be up to $267,000 based on current estimates, but would depend on how the industry responds to the new requirements.

Treasurer of State

- ***Short-term installment loan linked deposit program*.** The creation of the Short-Term Installment Loan Linked Deposit Program would not have any impact on state revenues, but could increase the Treasurer of State's GRF expenditures by approximately $325,000 annually. The creation of the new linked deposit program also requires an additional $20,000 one-time cost to set up a new database.

Local Fiscal Highlights

LOCAL GOVERNMENT	FY 2008	FY 2009	FUTURE YEARS
Counties and Municipalities			
Revenues	Potential minimal gain	Potential minimal gain	Potential minimal gain
Expenditures	Potential minimal increase	Potential minimal increase	Potential minimal increase

Note: For most local governments, the fiscal year is the calendar year. The school district fiscal year is July 1 through June 30.

- ***Civil justice considerations*.** Current law, mirrored by the bill, provides civil remedies that the Attorney General and the consumer may use to pursue violations committed by check-casher lenders through the Consumer Sales Practices Act (CSPA). While the bill contains new prohibitions and requirements on short-term lenders, very few payday lenders have been found to have violated the law. In view of this and the potential of the bill to significantly decrease check-casher lender licensure activity, it is unlikely that the overall impact of the new prohibitions and requirements on local civil justice costs would be any more than minimal.

- ***Local criminal justice costs*.** In addition to the civil remedies available, the bill, mirroring current law, also imposes a first-degree misdemeanor (M1) criminal penalty for short-term lender violations. As a result of the new requirements, some additional persons could be prosecuted and sanctioned, thereby increasing local criminal justice expenditures. It appears that the number and any associated expenses are likely to be minimal. Some of these costs would be offset by court costs and fees assessed on violators.

Detailed Fiscal Analysis

Overview

This bill makes a number of changes to Ohio's lending laws, particularly those for so-called "payday loans." Specifically, the bill caps interest on a short-term loan at 28% per year, reduces the maximum short-term loan amount to $500, creates the Financial Literacy Education Fund, increases the license fee amounts for check-casher lenders that would seek short-term loan licenses, and creates a statewide database to determine the eligibility of borrowers. In addition, the bill creates a new small loan linked deposit program through the Treasurer of State (TOS) that would enable lending institutions to offer short-term installment loans to consumers through certificates of deposit placed by the Treasurer at up to 3% below current market rates.

Short-term loan licenses

***License fees*.** Currently, in order to originate what are commonly referred to as "payday loans" in Ohio, a payday lender must be licensed as a check-casher and a check-casher lender. Check-cashers and check-casher lenders each pay a $500 license fee upon application for an initial license and a $500 annual renewal fee. Check-cashers and check-casher lenders also pay one-time investigation fees between $200 to $250. These fees are deposited in the Consumer Finance Fund (Fund 5530).

The bill would require only a single license to make what are termed "short-term loans." Short-term loan license applicants would be charged initial license and annual renewal fees of $1,000 for each business location along with a $200 one-time investigation fee. These fees would continue to be paid into the Consumer Finance Fund. The bill also requires short-term loan licensees to obtain and maintain a surety bond of at least $100,000, which would be for the exclusive benefit of a borrower injured by a violation of the bill's prohibitions.

***Loan terms*.** Current law requires the loans made by check-casher lenders to be made under a written contract, not to exceed $800, and not to have a duration of more than six months. Licensees are permitted to charge a loan origination fee and interest at not more than 5% per month or fraction of a month on the unpaid principal balance of the loan.

The bill reduces the maximum loan amount to $500 and specifies a minimum loan term of at least 31 days. It also requires short-term lenders to consider various underwriting criteria before making short-term loans and to provide borrowers with an extended payment plan at any time before the maturity date of the loan. The bill limits the interest (which would now include fees, service charges, renewal charges, credit insurance premiums, and so on) that may be charged on a payday loan to an annual percentage rate (APR) of 28%. This would translate to a maximum finance charge of approximately $2.38 on a 31-day $100 loan.[1] The table below

[1] This is calculated by dividing the APR by the number of 31-day periods in one year to find the APR's 31-day equivalent. So, 0.28/(365/31) = ~ 0.0238, which would equate to an approximate interest rate of 2.38% for 31 days.

illustrates how finance charges are calculated at various loan amounts both under current law and under the bill under a 31-day loan model.

Table 1: Payday Loan Finance Charge Crosswalk		
Loan Amount	**Current Law[2]**	**Proposed Changes in H.B. 545**
$500 or less	$5 loan origination fee for every $50 borrowed plus 5% interest per month or partial month	28% Annual Percentage Rate (includes all fees and charges other than check collection charges for bounced checks)
	Example of $100 loan for 14 days: $100 + $10 loan origination fee + $5 in interest = **$115 (APR = 391.07%)[3]**	**Example** of $100 loan for 31 days: $100 + $2.38 in finance charges = **$102.38**
	Example of $500 loan for 14 days: $500 + $50 loan origination fee + $25 interest = **$575 (APR = 391.07%)**	**Example** of $500 loan for 31 days: $500 + $11.90 in finance charges = **$511.90**
More than $500 but up to $800	5% interest + $5 loan origination fee for every $50 for the first $500 and $3.75 loan origination fee for every $50 above $500	N/A
	Example of $800 loan for 14 days: $800 + $72.50 ($50 for the first $500 and $22.50 for the last $300) in loan origination fees + $40 in interest = **$912.50 (APR = 366.63%)**	N/A

Much of the direct fiscal effect of the interest rate cap will depend on how the payday lending industry in Ohio reacts to the revised statutes, and how many currently licensed check-casher lenders opt for licensure as short-term loan operators. For background on this issue, including national research and case studies from other states that have implemented changes in their payday lending laws, please consult the back of this analysis.

***Impact on license fee revenue*.** As of May 5, 2008, the Department of Commerce's Division of Financial Institution's license roster listed 1,581 check-casher lender licenses and 1,684 check-casher licenses in Ohio (for a total of 3,265 licenses).[4] Given that certain payday lending companies have indicated that they no longer do business in states and cities that have restricted payday loan origination fees and interest charges, it seems reasonable to assume that some check-cashers and check-casher lenders licensed in Ohio might choose not to continue business in the state using the short-term loan license. If so, license fee revenue to the Consumer Finance Fund from short-term lenders and check-cashers would decrease.

Revenue from license fees from check-cashers and check-casher lenders was approximately $1.6 million in FY 2007. While it is uncertain how many check-cashers and check-casher lenders would discontinue operations, if a significant portion were to do so, the Consumer Finance Fund could experience a loss in revenue in the hundreds of thousands of dollars, and perhaps over $1 million if the vast majority were to leave the industry in Ohio.

[2] Ohio Department of Commerce, Office of Consumer Affairs "Payday Loans" publication.
[3] The formula to calculate the APR is as follows: APR = [(advance fee/principal borrowed) x (365/14)] x 100. We divide 365 by 14 to obtain the number of 14-day periods within a year and multiply that number by the finance charge percentage for the loan period to annualize the cost of credit. So, [(15/100) x (365/14)] x 100 = 391.07%.
[4] Accessed through the Ohio eLicense Center at http://www.com.state.oh.us/dfi/elicense.aspx.

However, as the growth in the payday lending industry would seem to show, there is a high demand for the short-term, small dollar loan products these businesses provide. If the interest rate caps in the bill make payday lending in its current form an unprofitable venture, Ohio licensees may instead develop alternative, short-term loan products in some way to remain profitable while keeping check-casher and short-term lender licenses. Other industry operators might simply seek licensure under another licensure category, such as Ohio's Small Loan Act, which allows lenders to offer higher principal loan products, including open-ended lines of credit. Small loan licensees pay license fees of $250 into the Consumer Finance Fund and initial investigation fees of $200. To the degree that an increase in small loan licensure occurs, this might limit potential revenue losses to this fund. However, it is important to note that the bill limits the license fee of any current check-casher lender licensee applying for a license under the Small Loan Act for the 2008 licensing period ending June 30, 2009 to one-half of the current small loan license fee, which would be $125.

Specifically, under the Small Loan Act, no person may make loans of $5,000 or less without being licensed under the Small Loan Act. Various financial institutions and lenders, who are otherwise licensed or authorized to lend money, are exempt from the licensing requirement under the Small Loan Act. A small loan licensee may charge up to 28% interest per year on the unpaid principal balances of up to $1,000 and 22% per year on the unpaid principal balances above $1,000. On loans of $500 or less, a small loan licensee may charge an origination fee of up to $15. On all other loans, a licensee may charge an origination fee of $30 or 1% of the principal loan amount, whichever is greater. As of this writing, there are currently 48 active small loan licensees.

***Administrative costs*.** The Division of Financial Institutions (DFI) in the Department of Commerce oversees the administrative work of approximately 15,000 active consumer finance licenses, with check-cashers and check-casher lenders comprising about 22% of that number. DFI's Consumer Finance program, which employs 39 people, also regulates other consumer finance occupations and companies such as mortgage brokers, loan officers, second mortgage companies, and small loan companies. None of these employees works exclusively on check-casher or check-casher lender issues. Rather, DFI assigns these employees by function. So, field examiners perform examinations of mortgage brokers, check-cashers, check-casher lenders, pawnbrokers and so forth, while licensing staff work on all license types.

The bill changes the frequency with which DFI must examine licensee records. Current law requires DFI to examine the records of check-cashing lenders as often as DFI considers necessary. The bill requires DFI to examine the records of a licensee at least annually. The bill also requires DFI to publish an annual analysis of the reports short-term loan licensees are required to file concerning their operations for the preceding calendar year as well as a semi-annual report to the Governor and the General Assembly with respect to enforcement actions for violations of the short-term loan law, including short-term loan license suspensions, revocations, and denials. Although these requirements could increase DFI's administrative burden, the higher short-term lender license fee would offset any new administrative expenses. However, if a significant number of licensees were to allow their licenses to lapse, payroll and other costs charged to the Consumer Finance Fund and the Financial Institutions Fund (Fund 4X20), which also pays for a portion of the Consumer Finance program, may decrease due to a reduction in licenses to oversee. The magnitude of any effect will depend upon how licensed check-cashers and check-casher lenders respond to the requirements of the bill.

Disciplinary actions

While the bill applies many of the provisions authorizing the Superintendent of Financial Institutions to perform investigations and suspend or revoke a check-casher lender license to short-term lender licensees, the bill adds the authority to impose a fine of up to $1,000 for each violation by a short-term lender licensee. This may increase revenue to the Consumer Finance Fund to the extent that such violations occur.

Financial Literacy Education Fund

The bill creates the Financial Literacy Education Fund to support various adult financial literacy education programs developed or implemented by the Director of Commerce. At least half of the programs must be presented or made available at public community colleges or state institutions throughout the state. These activities and the status of the fund must be summarized in an annual report.

The bill directs the Director of Budget and Management to make a one-time transfer of 5% of the balance of the Consumer Finance Fund to this new fund. The current cash balance in the Consumer Finance Fund is approximately $10.8 million. Allocating 5% of this amount would provide approximately $540,000 for the Financial Literacy Education Fund in FY 2009. In addition to this one-time transfer, the bill provides an ongoing revenue source: 5% of all charges, penalties and forfeitures received by the Fund 5530. This amount is to be transferred on, at least, a quarterly basis.

Annual revenues accruing to the Consumer Finance Fund averaged approximately $5.34 million from FY 2004 to FY 2007. Assuming charges would include all fees received by Fund 5530 and revenue is comparable to prior years, annual transfers to the Financial Literacy Education Fund would amount to approximately $267,000. However, if a significant reduction in check-casher lender/short-term lender licensure occurs as a result of the bill, this amount would be considerably smaller.

Short-term installment loan linked deposit program – Treasurer of State

The bill authorizes the Office of the State Treasurer to establish a Short-Term Installment Loan Linked Deposit Program for the purposes of providing short-term installment loans to eligible individuals. These short-term installment loans are not to exceed a principal amount of $800 and must have a duration of at least 90 days and six installments. The APR on these loans is not to exceed 28%. The bill also indicates lenders' responsibilities and authorizes the Treasurer of State to use state funds to purchase certificates of deposit equaling the total amount of money lent by eligible lending institutions to the individuals participating in the Short-Term Installment Loan Linked Deposit Program.

Under the proposed Short-Term Installment Loan Linked Deposit Program, an eligible lending institution may enter into a deposit agreement with the Treasurer of State. Subsequently, if its short-term installment loan linked deposit loan package is approved, the public depository will receive a linked deposit in the form of a certificate of deposit (CD) at up to 3% below

current market rates.[5] In return for the reduced interest earnings on the state's certificates of deposit, the eligible lending institution makes short-term installment loans to eligible individuals. The bill specifies that the State Treasurer must develop guidelines necessary to implement the new Short-Term Installment Loan Linked Deposit Program.

In general, the bill creates a new category of linked deposit program, but does not change the current interest rate requirements on the CDs for linked deposit programs or the current aggregate percentage of state funds that the State Treasurer may invest in all linked deposit programs. Therefore, the creation of the Short-Term Installment Loan Linked Deposit Program would not have any impact on the state's earnings on investments and revenues. However, the Treasurer of State's expenditures would increase by approximately $345,000 annually. According to the Treasurer's office, its expenditures would increase by $200,000 for salaries and benefits to hire three additional employees for monitoring and reporting of the new linked deposit program, $25,000 in marketing fees, and $100,000 increase in annual banking fees.[6] In addition, there will be a one-time cost of about $20,000 to set up a new database to implement the new program.

The Treasurer of State is also required to produce an annual report on the Short-Term Installment Loan Linked Deposit Program to be submitted to the Governor, Speaker of the House of Representatives, and President of the Senate. The report must set forth the linked deposits made by the Treasurer during the year, the number of short-term installment loans made by each institution, categorized by postal zip code, and a representation of the number or percentage of loans pursuant to the program that were paid late or are in default. Essentially, the bill extends current annual report requirements on established linked deposit programs to the Short-Term Installment Loan Linked Deposit Program.

Credit union lending option

As a result of Sub. H.B. 81 of the 126th General Assembly, which became effective in April 2007, credit unions are empowered to make loans for up to $1,000 for up to 30 days. All interest, fees, and other loan costs cannot exceed 10% of the principal amount for this loan product. The bill eliminates the authority of credit unions to make these loans.

The Ohio Credit Union League is unsure of how many credit unions are offering this loan product or how many credit union patrons have secured such a loan in the short time that the law has authorized the product. However, a number of credit unions offer a similar payday advance product called StretchPay, which is a line of credit offering borrowers the ability to take advances of $250 or $500 with annual fees of $35 and $70, respectively, on a 30-day repayment term with finance charges at up to 18% APR. This product does not fall within the small loan product created in Sub. H.B. 81. Overall, it does not appear as if this provision will have a significant fiscal effect on gross asset assessment revenue DFI receives from credit unions.

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[5] Current linked deposit programs require the same rates. Hence, the amount of interest earnings that the state would give up on the CDs under the bill, in exchange for savings to the eligible lending institutions that provide small loans at a lower interest rate for the Short-Term Installment Loan Linked Deposit Program participants, would also remain the same.

[6] Assuming 10,000 individuals participate in the new linked deposit program. Costs per person are estimated at $10.

Statewide consumer eligibility database

If more than 400 persons are licensed under the short-term loan law at any point after September 1, 2009, the bill requires DFI to make available a statewide database accessible to short-term lenders to determine a borrower's eligibility for a short-term loan. The bill does not permit short-term lenders to charge consumers any part of this fee, which is payable to the database operator (which can be either the Superintendent of Financial Institutions or a third-party) for the actual costs of entering, accessing, and maintaining data in the database. DFI would likely require a third-party to set up and operate the database in order to comply with this added responsibility. If such a database is not developed due to a lack of licensees, the bill requires each licensee to use an electronic database tracking service that permits the licensee to determine whether the borrower has an outstanding unpaid check or debit authorization that is, or reasonably appears to be, connected to a short-term loan.

Other states such as Michigan, Indiana, Oklahoma, Illinois, and Florida have implemented similar borrower eligibility databases with database fees being between $0.43 and $1.00 per transaction.[7] Assuming the Department of Commerce contracts with a vendor such as Veritec, which currently offers statewide eligibility databases to the above states, DFI would incur no "hard" cost for the database since the vendor would be compensated through the transaction fees paid by consumers. There might, however, be some intangible costs related to working with the vendor to set up and maintain the database, resolving any database issues, and so forth.

Consumer Finance Education Board

The bill expands the authority of the Consumer Finance Education Board to include the analysis and investigation of the policies and practices of state agencies, nonprofit entities and businesses inasmuch as those policies and practices address small loan counseling and education for borrowers. The bill also allows the Board to coordinate and provide resources to state agencies, nonprofit entities, and businesses to improve small loan counseling and education for borrowers in addition to the other areas that the Board can coordinate and provide resources to under current law. As of this writing, original appointments to the Board have not yet been completed and the Board has not met. However, the expansion of the Board's duties may increase the Board's costs over what they would have been absent the bill's enactment.

Local fiscal effects

Current law, mirrored by the bill, provides civil remedies that the Attorney General and the consumer may use to pursue violations committed by short-term lenders through the Consumer Sales Practices Act (CSPA). While the bill contains new prohibitions and requirements on short-term lenders (including new prohibitions on debt collections practices), a review of DFI enforcement actions since August 2006 indicates that very few payday lenders have been found to have violated the law. According to the Department of Commerce, most violations are minor and are immediately corrected or are handled through DFI enforcement actions, with the Attorney General's office rarely involved in payday lender violations.

[7] Florida and Oklahoma receive a portion of the fee to pay for regulatory efforts and consumer credit counseling, respectively.

The bill also permits borrowers to bring a civil action for recovery of damages against a short-term loan licensee if the licensee does not abide by certain duties and standards of care. Damages awarded may not be less than all compensation paid directly or indirectly to a licensee from any source, plus reasonable attorney's fees and court costs. In addition, the borrower may be awarded punitive damages. In view of this and the potential of the bill to significantly decrease check-casher lender licensure, it is unlikely that the overall fiscal impact of the new prohibitions and requirements on local civil justice operations would be any more than minimal.

In addition to the civil remedies available, the bill (mirroring current law) also imposes a first-degree misdemeanor (M1) criminal penalty for violations, carrying a maximum jail term of 180 days and a maximum fine of $1,000. As a result of the new requirements and prohibitions in the bill, some persons who may not have been successfully prosecuted and convicted under existing law could be prosecuted and sanctioned. This could in turn increase local criminal justice expenditures. By the same token, local fine and court cost revenue may increase, offsetting some or all of any additional criminal justice costs. If additional criminal cases are created, there is also the possibility that the state may gain a negligible amount of state court cost revenue to the GRF and the Victims of Crime/Reparations Fund (Fund 4020). For misdemeanors, the GRF receives $15 per case and the Victims of Crime/Reparations Fund receives $9 per case.

Background on the payday lending industry

Current payday lender costs and profits. There is limited publicly available data in regard to payday lender operating costs and profits. An often-cited source is Flannery and Samolyk's 2005 working paper for the Federal Deposit Insurance Corporation's (FDIC) Center for Financial Research. Their study examined proprietary store-level data from two large payday lending firms to study store costs and profitability.[8] This study included data on a random sample of 600 stores operating in 22 states and found a relatively high average cost of originating payday loans. Specifically, Flannery and Samolyk found that average costs for a store open at least one year to loan $100 were between $11 to $14, depending on the age of the store; these are figures the authors contend are not that out of line with the size of advance fees (the average advance fee in the study ranged from $14.32 to $18.30 depending on store age).

Flannery and Samolyk found that the average store's operating margin – the ratio of operating income-to-store revenue which measures how much revenue is left over after store operating costs are deducted – to be 33.2%. However, this margin does not account for shared administrative (or "G&A") and interest expenses allocated by the payday lending firm at the corporate level, which, when accounted for, reduce true store profitability. The table below summarizes Flannery and Samolyk's findings for stores open at least one year. As the table demonstrates, the study found that older stores are more profitable due to greater loan activity. In sum, the study's authors concluded that fixed operating costs and high loan loss rates account for a large part of the high APR charged on payday advance loans.

[8] Flannery, Mark and Katherine Samolyk, "Payday Lending: Do the costs justify the price?" FDIC Center for Financial Research Working Paper 2005-09, June 2005.

Table 2: Payday Lending Industry Profitability				
	Young Stores (1-4 years) Avg. Loan Size = $257.72		Mature Stores (>4 years old) Avg. Loan Size = $227.54	
	$ per loan	$/$100 advanced	$ per loan	$/$100 advanced
Avg. Total Store Revenue	$45.94	$17.83	$43.82	$19.26
Avg. Total Store Operating Costs	$36.10	$14.01	$25.10	$11.03
Avg. Store Operating Income	**$9.84**	**$3.82**	**$18.72**	**$8.23**
Avg. G&A and Interest Expenses	$12.84	$4.98	$7.47	$3.28
Avg. Pre-tax Store Income	**($3.00)**	**($1.16)**	**$11.26**	**$4.95**

Source: Flannery and Samolyk

Another source of information concerning the profitability of payday lenders comes from the quarterly Securities and Exchange Commission (SEC) filings of seven publicly traded payday lending companies (some of these companies also engage in pawn business). An August 2006 study in the Fordham Journal of Corporate and Financial Law reviewed these documents (which includes data from nearly 8,000 payday lending stores) and came to a similar conclusion as Flannery and Samolyk: that payday loan firms are not "overly profitable."[9] While average store operating margins were comparable to those reported by Flannery and Samolyk (24.64%), the average profit margin – the percentage of gross revenue that remains after subtracting out all associated costs for the period – was 7.63% when including companies that, while pawn is their primary business, also make payday loans. This study also noted that the average profit margin was less than Starbucks (a little over 9%), a company with a similar business-franchising model as firms in the payday lending industry.

Also among the findings was a contention that the industry's average profit margin is attributable to high operating costs, which are driven by longer business hours (leading to higher wage costs) and a large number of stores (leading to high occupancy or rent costs) that are needed to drive loan volume and thus profitability.[10] The high cost of loan losses also contribute heavily to a store's operating costs, further reducing profitability (around 25% of store operating costs in both studies); however, the Fordham study indicated that loan losses for payday lenders are not unusual in comparison to commercial lenders.

***Case studies*.** The recent experience of other states with similar payday lending rate caps is also instructive. An August 2001 Indiana Supreme Court ruling limited payday loan finance charges to 72% APR by applying Indiana's loan-sharking law to payday lenders.[11] After this, the number of entities licensed and the number of branch locations decreased. According to Indiana Department of Financial Institutions (IDFI) annual reports, at the end of CY 2000, Indiana had 119 payday lender companies registered with 463 branch locations. By the end of CY 2003, there were 44 companies registered with 313 branch locations, amounting to a 63.0% reduction in the number of companies and a 32.4% reduction in the number of branch locations.

[9] Huckstep, Aaron, "Payday Lending: Do Outrageous Prices Necessarily Mean Outrageous Profits?" Fordham Journal of Corporate and Financial Law, October 2006, Volume XII, pages 203-231.

[10] Flannery and Samolyk cite another study indicating a high concentration of storefronts is necessary in the payday lending industry since competition appears to revolve around customer convenience rather than price.

[11] Janet Livingston, et al. v. Fast Cash USA, Inc., Case Number 94S00-0010-CQ-609.

An IDFI official noted that most of the larger payday lending companies continued to operate under the 72% rate cap under the industry's expectation that a new law authorizing the practice with sufficient fees would be passed. This occurred in March 2002 through a bill that specifically provided for the existence of payday lending in Indiana after several disputes, including the Indiana Supreme Court case above, about the issue of payday lending in that state. The March 2002 law limited payday loans to $401 and the associated finance charge to $35, but was amended in July 2004 to revise the allowable finance charges according to a scale that reduced the percentage charged on the loan as the principal amount increased. By the end of CY 2006, the number of companies and branch locations increased to 47 and 543, respectively.

Another more recent example comes from Oregon, which, effective July 1, 2007, changed its payday lending laws to limit origination fees to $10 per $100 advanced (in other words, a 10% origination fee) and interest to 36% APR, with a minimum loan term of 31 days. Including the origination fees, this amounts to an APR of 153% for a 31-day loan. An LSC review of recent SEC filings by the publicly-traded payday lending companies indicated that, in some cases, these firms cited the new origination fee and interest caps as reasons for closing some or all of their payday loan outlets in Oregon. Advance America, the country's largest payday cash advance company by stores operated, closed all 45 of its stores in Oregon. QC Holdings has already closed all eight of its stores, and First Cash Financial Services has closed two of its seven stores in the state and has noted in recent SEC filings that Oregon's new regulations had a significant negative effect on the company's revenues in that state.

First Cash Financial Services also noted that the District of Columbia's 24% APR cap on short-term loans, which became effective in January 2008, resulted in the closing of all nine of its payday loan locations in that area.

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