BANKING ON THE MARGINS

New Powers, New Responsibilities: A Guide for Municipalities on Payday Loan Regulation

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NEW PAYDAY LOAN LAWS GIVE NEW POWERS TO MUNICIPALITIES

Last year, the government of Ontario passed new regulations on payday lending. Most of those regulations pertained to payday lenders themselves and were concerned with interest rates, loan terms, disclosure, and other financial matters.

One of the new regulations, however, extended beyond the lenders themselves and gave new powers to Ontario municipalities to regulate, via zoning bylaws, the placement of payday loan stores within the municipal jurisdiction. Section 24(3) of the Payday Loans Act, 2008, S.O. 2008, c. 9, states the following:

> ## Location of offices
>
> (3) In acting as a licensee, a licensee shall not operate an office at a location if a by-law passed under section 154.1 of the *Municipal Act, 2001* or section 92.1 of the *City of Toronto Act, 2006* prohibits the operation of the office at the location. 2017, c. 5, Sched. 2, s. 21 (2).

And section 154.1 of the Municipal Act, 2001, describes the new powers given to municipalities:

> ## Restrictions re payday loan establishments
>
> 154.1 (1) Despite section 153 and without limiting sections 9, 10 and 11, *a local municipality, in a by-law under section 151 with respect to payday loan establishments, may define the area of the municipality in which a payday loan establishment may or may not operate and limit the number of payday loan establishments in any defined area in which they are permitted*. 2017, c. 5, Sched. 2, s. 27 (emphasis added).
>
> ## Exception
>
> (2) Despite subsection (1), a by-law described in that subsection shall not prohibit the operation of all payday loan establishments in the municipality. 2017, c. 5, Sched. 2, s. 27.

The language is identical for the city of Toronto. Effectively these laws have empowered municipal councils to use zoning bylaws to regulate the geographical placement and presence of payday lenders, a power that they did not previously have. The government devolved authority to regulate locations to municipalities after councillors from various municipalities in Ontario noted the challenge these stores were presenting to their cities.

The Effects of Payday Lending on Municipalities and Citizens

We explored the impact of payday lending on communities in our research paper on the small-dollar credit market titled *Banking on the Margins: Finding Ways to Build an Enabling Small-Dollar Credit Market.* As we note in our paper,

> Data suggests that dependency on payday loans extends costs beyond the borrowing household. The financial strain, health effects, and hindrance to the upward economic mobility of the household increase the burden on our whole society due to costs associated with health care, policing, low-income support, and other social services.

In particular, payday lending is correlated with violence, property crime, increased need of social assistance, and increased premature mortality. It stands to reason that municipal costs related to addressing these social ills will also be affected.

However, it is important to note that while the data do show a clear relationship between payday lending and negative household and community outcomes, the causal relationship (i.e., payday loans *cause* increased violence and higher policing costs) is *not* clear. *It is likely more accurate to see payday lending as one part of wider social challenges for your municipality.* This is particularly important as your municipality considers how to use its new powers to achieve the best outcomes for your municipality.

THE HARMFUL RIPPLE OF PAYDAY LOAN DEPENDENCY

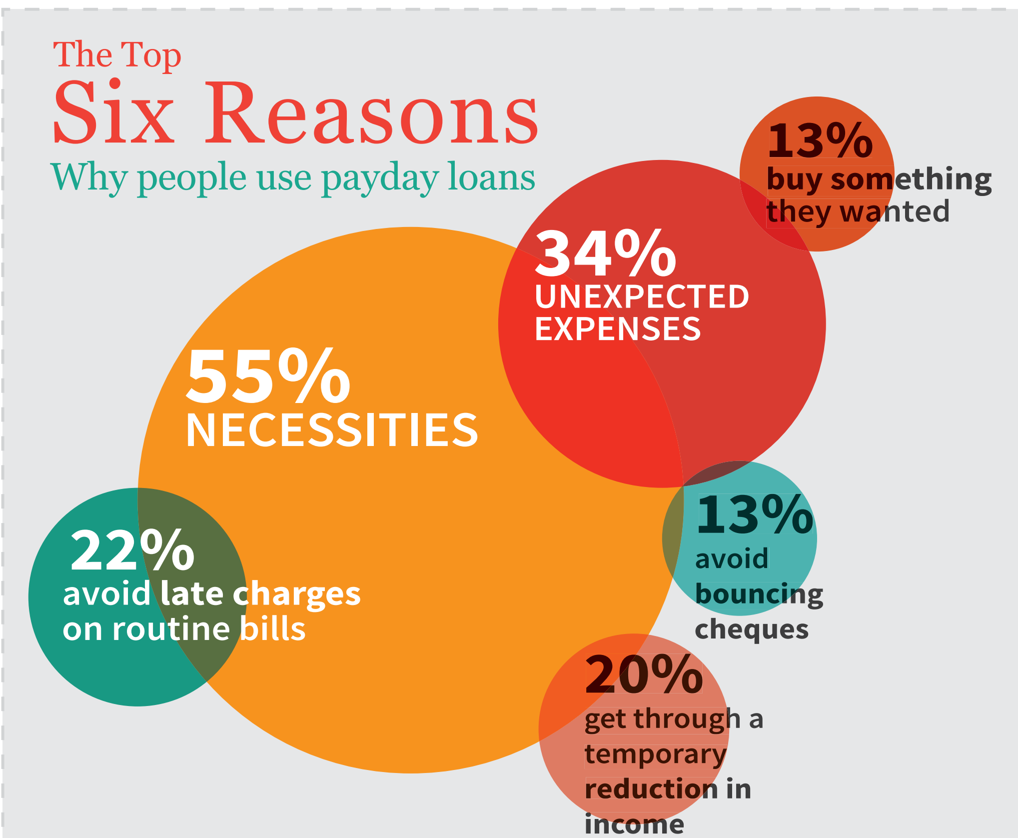
It is also important to note that payday lending, as much as it seems a poor choice, is often cheaper for consumers than alternative forms of small-dollar finance. As an economic choice "the desperate user is still making the best decision on the margin. It is, in effect, a case of substituting a very bad outcome with a slightly less bad outcome." As we show in our paper (see pp. 37–38), there are times when a payday loan costs less than alternatives, including NSF fees, fees levied by companies for missed bills or disconnection/reconnection costs for certain utilities. It is also important to note that the majority of payday loan users report using them to meet basic necessities, and other standard living expenses. This too should be considered as your municipality considers its use of its new powers.

COST OF BANKING FEES FOR NON-SUFFICIENT FUNDS

BANK	NSF CHARGE
Scotia Bank	$42.50
RBC	$45
CIBC	$45
TD Canada Trust	$48
BMO	$48

Data sourced from advertised rates of each bank

WHAT ARE PAYDAY LOANS BEING USED FOR?



Data Sourced: "Payday Loan Users Study British Columbia"; "Payday Loan Users Study Manitoba"; "Payday Loan Users Study Ontario"; "Payday Loan Users Study Alberta." Environics/Canada Payday Loan Association, 2013

Guidelines for Using New Powers

Given what research suggests about the role that payday loans play in the households of your community, and the lives of citizens within it, how might your city use its new powers in ways that serve the public good? Below we present a number of guidelines for addressing the challenges that accompany payday lending in your city.

First do no harm

Keep your focus on the people who use the loans

Municipal councillors care a great deal about their communities and their citizens. Most municipal officials, when they hear of individual stories of costs associated with payday lending, have a proper moral reaction—one of distaste—and will want to immediately spring into action and dive in to help those who are floundering economically. But the danger of the desire to "do something" is that the impetus to act leads to an exacerbation of problems. And often, this desire to do something takes the form of focusing on the lenders rather than the consumers. Data suggests that, regardless of the availability of small-dollar credit, the need for small-dollar credit is fairly steady, and when payday loan stores are legislated out of business, unsavory alternatives (like loan sharking, black-market loans, or higher-cost alternatives) fill the gap. Keep your focus on the people who use the loans, and attempt to avoid a simplistic focus on "punishing" lenders, even though punishing lenders leads to positive headlines. Look deeper to find the root of the problem. Develop a plan to address that.

Know where they are, who uses them, and why

Cardus's study compiled aggregate data on payday lending in Canada, as well as evidence from provincial jurisdictions, but due to the varied nature of payday loan usage and payday store prevalence, it is important for your municipality to **understand the way payday loan stores and their customers work *within your own jurisdiction.*** Prior to enacting any bylaw, it would be prudent for policy-makers to study the small-dollar loan market within their own jurisdictions. Get to know the users and providers and listen to their stories and, as much as possible, attempt to collect unbiased data that will assist you in making decisions that will help, rather than hinder, citizens.

Opt for a targeted, rather than blanket, approach

The city of Hamilton, one of the proponents for these new powers, has indicated that it will use its zoning power to remove all but one payday loan store per ward (with existing stores grandfathered). This is an example of a blanket approach that is targeted at providers of payday lending. The challenge with this approach is that it underestimates the possible negative consequences of less choice for consumers, and provides a monopoly for the remaining providers. As we note in our paper, evidence suggests that one of the key problems behind the high costs associated with payday lending is the lack of alternatives. **Payday lending has developed the way it has, in large part, due to the lack of competition in this market.** Given this, and given that the vast preponderance of data suggest that monopolies leave consumers with less choice, decreased service, and increased costs, this move is unlikely to benefit those it is intended to help, and indeed may harm consumers and families.

The major need for those who take payday loans is more affordable alternatives

There are, however, ways in which your municipality can use a targeted approach that is more likely to address the needs of those who are most vulnerable. As we note in our paper, most consumers of payday loans are making rational decisions—they know the costs, and enter agreements with eyes wide open. However, there are some segments of the market—particularly those with disabilities—who are particularly susceptible to the advertising of lenders and are unable, for whatever reason, to make informed decisions. In such cases, councillors may wish to consider "buffer zones" for payday loan institutions, akin to those used to place establishments like bars or strip clubs away from vulnerable populations such as children in schools.

Avoid redundancy and concentrate on the most effective use of municipal authority

The city of Hamilton has also used its licensing powers to enact bylaws relating to such things as signage and advertising to ensure that lenders provide borrowers with knowledge of credit counselling prior to giving lenders licenses to operate (see here). However, provincial law already requires these disclosures. And municipal licensing requirements, to maintain the integrity of the city's laws, require inspection and enforcement, which bear significant costs that are already being borne by the province. Redundancy in this case is unlikely to improve the consumer's well-being and will add municipal costs to work already being done by the province.

Don't be satisfied with restrictions: Look for positive, enabling municipal measures

The new laws aimed at providing municipalities with the ability to restrict payday lenders can give the impression that restrictions are the only thing that municipalities can do to address the challenges associated with payday lending. But there are other, positive policy steps that cities can take to achieve their objectives. As we note in our paper, the major need for those who take payday loans is to have more affordable alternatives (pp. 47–50). We note that new alternatives are arising in the financial technology sector (online loans that leverage lower overhead costs into lower prices for consumers), but that the most likely competitors will arise from partnerships between credit unions and civil society organizations who possess the financial and relational infrastructure to assist those with short-term cash needs. Examples of this can be found in Ottawa, with the Causeway Community Finance Fund, a partnership between the Causeway Work Centre, an NGO in Ottawa, and Alterna Savings, Frontline Credit Union, and Your Credit Union, as well as the "Smarter Cash" alternative offered by Windsor Family Credit Union. One major challenge for these initiatives is their ability to properly market their availability to potential customers. According to our research, approximately 75 percent of the costs of providing a payday loan are related to overhead (i.e., space and staff) and marketing. In both cases, municipalities are well placed to lend their assets in ways that can help payday loan alternatives with little marginal increase in their budgets. Two tangible examples here include providing community-based payday loan alternatives with access to underutilized municipal spaces (e.g., in rec centres or boardrooms) and municipal ad space (e.g., on buses).

Conclusion

Ontario's new payday lending laws provide municipalities with both opportunities and responsibilities. The space is a difficult one to navigate, with complexities on economic, social, and governance fronts. If there are any questions, or if your municipality would like to learn more about what research says about how your municipality might address this issue, please do not hesitate to be in touch. We are happy to share our work with you in the hope of providing Ontario's municipalities with the best information to assist them in making their cities the home of enabling credit markets.

MORE RESEARCH:

Introductory Video on Payday Lending

Banking on the Margins: Finding Ways to Build an Enabling Small-Dollar Credit Market