

Alternative Financial Services in Canada: Findings from Focus Groups

Discussion Paper

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1.0 Introduction

The so-called Alternative Financial Services (AFS) sector has experienced considerable growth in North America in the last decade. This sector includes a wide variety of cheque cashing facilities and sub-prime lenders, including payday lending and pawnbrokers. Some commentators also include tax discounting companies, finance companies and rent-to-own companies. Although this broader definition of the industry is considered in this report, the main focus of the report is cheque cashing and payday lending organizations, the most recognizable in Canada being Money Marts.¹

There is a concern among consumer advocates that cheque cashing and payday lending operations use ethically dubious practices to take advantage of consumers who have no reasonable alternative sources for credit. These practices are thought to violate federal usury legislation and provincial consumer protection statutes. Yet enforcement has been spotty. This is partly because the Crown has been reluctant to pursue these cases, but also because the industry has been successful in riding the fine line between blatant violation of laws and merely ethically questionable business practices.

Most of the literature in this field has been generated out of the United States with particular reference to inter-state differences in regulatory environments. In addition, legal and economic treatises that attempt to establish the issues surrounding the industry are commonplace. By their nature, these reports tend to be somewhat conceptual and deductive in their reasoning. However, in many ways, the industry violates many precepts of logical, well-functioning markets. Moreover, these studies occasionally lack balance; they are either clearly against the industry to begin with or they take an industry perspective that inevitably glosses over ethical rough spots.

This discussion paper endeavours to make a unique contribution to the literature on cheque cashing and payday lending as it applies to Canada. It is based entirely on the views of Canadian users of the AFS sector, as well as an interview with someone who had worked within the industry. Although the report does not claim to be statistically representative of the sector, it has the virtue of being focused on the Canadian experience and of relating directly the experience of those who have actually used the services. These discussions exposed nuances that are difficult to reveal with either theoretical research or household surveys.

There remains, however, a need for a larger scale household survey to validate the themes discussed in this paper. Therefore this paper will form the basis for a large-

¹ From this point forward the AFS will refer primarily to cheque cashing and payday lending organizations. Money Mart is the brand name for the National Money Mart Cheque Cashing Company, which is a wholly owned subsidiary of Pennsylvania-based Dollar Financial Group Inc.

scale, statistically valid household survey that will be conducted during the Fall of 2001. This discussion paper is merely one of four contributions into the Public Interest Advocacy Centre's (PIAC's) final report on the AFS. In addition to this paper and the findings of the household survey, an extensive literature review and consultations with concerned organizations will be reflected in the final report that is slated for release in Spring 2002.

1.1 Overview of the Paper

The paper begins with a review of the methodology. This is followed by a brief description of the participants in 6 focus groups held across Canada in August 2001.

Before considering the findings of the focus groups, the paper reviews some insights offered by a former employee of a Money Mart on its business practices and customers. This industry view is juxtaposed with the experience of the focus group participants. Special attention is paid to the participants' use of various types of financial services. Then the report considers participants' attitudes toward different types of credit, which plays an important role in their usage of these services and in their attitudes toward government regulation. The report then goes into some detail on usage patterns and how these establish pathways to the AFS. It concludes with participants' views on the role of government regulation and some summary comments.

2.0 Methodology

This report is based on a qualitative interview methodology. This involves a number of group interviews (or focus groups) that bring together small (7 to 9) numbers of people to discuss their attitudes to and experience with various sorts of financial services, with particular emphasis on the AFS. Two focus groups were held in each of Toronto, Calgary and Vancouver (a total of 6) during August 2001. These focus groups were augmented by an interview with a former employee of Money Mart.

There are two structural parameters for the focus group: the recruitment screener that determines eligibility for participation and the discussion guide that provides a framework for the focus group conversation. These are provided in Appendices A and B.

Although our interest was primarily in cheque cashing and payday lending, two types of groups were recruited. One group consisted of people who satisfied the *weak* condition of having had used a finance company. The second group consisted of those who satisfied the *strong* condition of having used a cheque cashing or payday lending facility. This type of recruiting was done because the pathways that lead to the cheque cashing and payday lending organizations are of interest. More importantly, it was felt that a social stigma may be attached to cheque cashing and payday lending that may make some participants reluctant to come forward. This was indeed the case as a number of those who were recruited based on the weak

condition also had direct experience of cheque cashing and, in a few instances, payday lending.

The discussion guide merely acts as a framework for the focus group. In practice, the discussion can be quite wide ranging and there is considerable interaction between the moderator (the present author) and the participants, and among the participants themselves. Group discussion can be very effective because people are gathered with those who have common experiences and participants can empathize with other participants' financial challenges.

The discussion guide (Appendix B) logically begins with usage and attitudes (U&A) towards various forms of financial services. The discussion at this point is supplemented through the use of a tally sheet that summarizes each participants experience with different types of financial services. The discussion then delves further into the course of events that led to the use of the AFS, how people use it, how often they use it and their general impressions and experiences with the sector. The discussion then briefly explores other options for financing outside of the AFS and then considers the participants' views on roles for government regulation.

Exhibit 1 **Characteristics of the Focus Group Attendees**

Total Attendees: 47

Gender

Male 26
Female 21

Education

Some High School	2
Completed High School	16
Some College	16
Some University	4
Completed College	5
Completed University	4

Annual Income Level

<\$10k	1
\$10-19k	4
\$20-29k	11
\$30-39k	17
\$40-49k	6
\$50-59k	6
\$70-79k	1
\$80-89k	1

Source: Grant Insights

3.0 Focus Group Participants

Exhibit 1 reviews some demographic information on the focus group attendees. Most of the participants had at least a high school education and lower to middle levels of income. There was rough gender balance in the groups.

4.0 Prelude to the Focus Group: The Disclosure Interviews

A weakness in the existing literature is that the motivations and practices of the industry are usually the source of speculation and there is rarely an attempt to juxtapose the industry business practices with the behaviours of the consumers.

To address this weakness, a separate interview was conducted with a former manager of Money Mart in Vancouver. This manager had worked in a middle management capacity for two and half years in four stores in the Vancouver area. This main interview was supplemented by a telephone interview with a former teller of Money Mart who had worked in Toronto and Vancouver for 12 months in 2000-01. This secondary interview was used to confirm some of the findings of the main interview and is not reported separately.

Although the main interview cannot be considered the definitive view on Money Mart's business practices, it is considered preferable to no inside view. The interview was designed to focus on the factual operation of the business with limited impressionistic comments on the quality of the business. None the less, it should be noted that the manager was not bitter about his experience with Money Mart. On the contrary, he considered the Money Mart to be a very good, albeit low-paying, employer. He had a number of positive things to say about the company and overall believes that it provides a needed service. Although he left of his own accord to go to another higher paying employer, his overall job satisfaction with Money Mart was not low.

4.1 *How Money Mart Makes Money*

The most interesting thing about the disclosure interview is the light it sheds on the way Money Mart's pricing regime works and how it manages business risk.

Money Mart has two main (very related) lines of business: cheque cashing and payday lending. The cheque cashing business has been under stress in recent years due to the significant expansion in the use of direct deposit. Notwithstanding the apparently high price to cash cheques (2.9 per cent plus an item fee), the business depends on relatively large volumes to be economic. So the reduction in volumes from direct deposit has presented a challenge for Money Mart. Further, the cheque cashing business became constrained in its growth because it was primarily targeting young, lower-to-middle income males for its business.

In order to grow the business, there was a need to move into alternative financial services that would not be reliant on direct deposit and that would appeal to other types of customers, especially “grey collar” women. The best prospect for growth was considered to be payday lending or “payroll advance”. This product was developed in the United States as a natural outgrowth of the cheque-cashing business and involves small loans that are secured through a personal cheque. It was introduced into Money Mart about 5 years ago and, in the words of the interviewee, has been “100-fold more successful” than cheque cashing. This is because its volumes are growing significantly (although still not as large as cheque cashing) but its pricing is much more lucrative than payday lending.

4.1.1 The Pricing and Revenue Generation Model

The reason that payday lending is so lucrative is because of the way it is priced. Many commentators have tended to focus on the relatively high cost of the loan itself, which can amount up to \$25 dollars for a two-week loan of \$100. But according to the interviewee, the main revenue streams are not associated with the loan itself but rather the fees related to the personal cheque that is used to secure the loan.

Money Mart has a graduated scale of item fees that reflect the general quality of different kinds of cheques. In this scheme, personal cheques are the most expensive to cash and attract an item fee of \$12.99. In addition, a cheque that is irredeemable because of insufficient funds (NSF) attracts an NSF fee of 25 dollars. Money Mart’s management system focuses on maximizing these additional fees.

In this regard, there are direct links between the cheque cashing pricing regime and the payday loan product. Theoretically, a customer can avoid fees by redeeming their cheque before the end of the term. Money Mart, however, encourages customers to allow it to simply cash the cheque. Although there is complete disclosure of these fees within the loan document, the customer usually “don’t understand a word you’re saying”. In the loan document that deals with cheque cashing fees there is language suggesting that it is preferable for the customer to “choose the convenience” of allowing Money Mart to simply deposit their cheque when the term matures.

In addition, Money Mart tightly manages the window between when the loan matures and when the cheque can be redeemed. The whole premise of the payday loan is that cash is required before the next payday. Yet the cheque is written and deposited on the person’s payday. Either the customer has to find another source of cash to redeem the cheque (unlikely) or he/she has to lie to Money Mart about when he/she is being paid thereby allowing time to redeem the cheque. Money Mart’s information systems are set up to identify customers who consistently redeem their cheques before term which calls forth special efforts to determine whether the customer is being paid before the end of the term of the loan. Not surprisingly, the rate of cheque redemption is “very low”.

NSF fees are another source of revenue. At 25 dollars these are significant and, once again, Money Mart has specific management systems around ensuring that a certain number of cheques “go NSF”. However, the interviewee was unclear as to how Money Mart could manage this directly other than those efforts that were already in place to ensure high item fees. Undoubtedly the practice of discouraging redemption would lead to some NSF fees being charged.

4.2 *Managing Risk*

One might think that Money Mart would want to avoid NSF fees because these would be offset by higher collection costs. Although these costs are incurred, the interviewee suggested that Money Mart is in a good position to manage these costs effectively. To begin, the vast majority of collections are managed at the branch level through simple telephone calling. Teller staff is used to make collections during down periods in business. For the most part, the customers “have nowhere else to go” so are willing to work with Money Mart to clear their name. In the instances where collections do remain a problem, the practice of “scooping” (garnishment) of presented cheques is common.

In general, Money Mart is extremely shrewd in the way it structures its business to minimize risk. On the cheque cashing side, it ensures due diligence around the “three R’s” : right cheque, right person leading to recourse. This means that if Money Mart has taken sufficient steps to ensure the cheque is legitimate, and the right payee is presenting it, then it has legal recourse to ensure collection from the payor. This management system suggests that the costs to Money Mart of managing the risk of bad cheques may not be as high as the industry claims and that its bad debt is actually low, although how low remains unclear.

4.3 *Potential Competitors*

According to the interviewee, Money Mart “rides the fine line between revenue generation (on one side) and legality and morality (on the other)”. Yet he describes the business as being “relatively unsophisticated” but nonetheless “highly profitable”. All this begs the question as to why others do not enter the market, thereby bidding down the prices for these services. The interviewee speculated that the main reason is that Money Mart was one of the earliest entrants and has established a dominant position in a market that is still a “grey area” from a regulatory point of view. As such, new entrants may be reluctant to enter the market in a later stage for fear that regulations may greatly reduce the profitability of the business. The ambiguity of the regulatory situation and the existing market structure has created the conditions for a quasi-monopolistic structure that benefits Money Mart, both in terms of the prices it charges for its services and in minimizing costs due to bad debts.

5.0 Main Themes of the Focus Group Discussions

5.1 Overall Use of Credit

Participants were asked to fill out tally sheets to describe their use of various forms of financing. Chart 1 (overleaf) reviews usage for various forms of finance based on these tally sheets. Not surprising, given the selection criteria for the focus group, there is a high rate of usage of cheque cashing among the participants. Indeed, about 8 people that were recruited based on their use of finance companies had experience with cheque cashing and one of these people had also taken out a payday loan.

Most participants had interactions with mainline financial institutions but were not using them either because they were disqualified through their credit rating or they were dissatisfied with their services, even though these were widely acknowledged to be the cheapest forms for credit. There was a general distrust of banks. This did not seem to apply to credit unions in the same way although experience with these was not as extensive as with banks and other deposit-taking institutions.

Some forms of credit definitely had stigmas attached to them, but once this stigma had been overcome participants merely considered the source to be a normal part of their financial service use. For instance, non-users of cheque cashing and payday lending facilities were much more likely to consider these morally repugnant, (“they’re just legalized loan sharks”, “they are preying on the poor”) than those that had actually used the service. This also applied to sources of cash like pawnshops, which many users considered to be a reasonable service to help them through cash emergencies. This was especially true in Calgary where participants could point to “hundreds” of pawnshops as an indication of the demand for their services. In the words of one: “no problem, if you have to pawn something it can’t be that important to you”.

5.2 Credit Cards: Paving the Way to the AFS

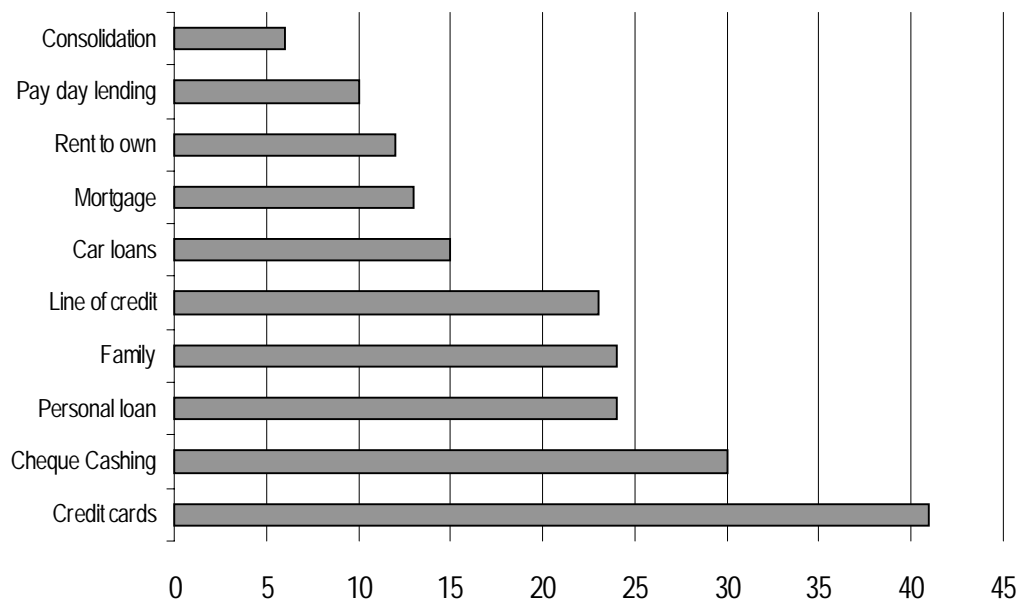
People were most familiar with credit cards and many times this was the product that ultimately led them to the AFS market. Participants were initially attracted to credit cards by their availability, incentive programs (like Air Miles or limited free credit) and the fact that they offer an easy way to establish a credit rating. It was also noted that credit cards are necessary for securing certain types of lending arrangements, like video and equipment rentals.

However, the idea of using a credit card to establish a credit rating was seen as a double-edged sword. Although participants recognized that credit cards are a cheap form of credit for those who exercise discipline in paying the monthly balance, for those who do not have this discipline, credit cards are trouble. “They are only good if you pay them off” was a typical sentiment expressed. So while credit cards are convenient, they are “a bit too convenient” for many people.

Many participants had started their initial cycle of debt through overuse of credit cards and this ultimately undermined their credit rating and limited their access to cheaper forms of credit. For these participants, credit cards were something to be feared with the credit card debt considerations overriding any cost effectiveness considerations (discussed further below).

In addition to aggressively marketing these cards, participants complained that credit card companies initiate increases in card limits without being requested by the cardholder. Not only did this create problems for those lacking the discipline to use the cards effectively, but it also created security concerns should the cards be lost or stolen. In general, these participants were not confident in their ability to take action to get incorrect charges to their credit cards reversed and this creates a source of anxiety when the credit card companies engineer unsolicited increases in credit limits.

Chart 1
Use of Various Financing Options By Focus Group Participants (Number of Participants)



Source: Grant Insights. Data collected from focus group tally sheets.

5.3 Retailer Extended Credit

Of course, retailer credit cards presented many of the same problems as bank credit cards, but there are also some unique issues. For example, retailer finance is often made available at the end of a purchasing decision. As such, some participants were overly focused on the goods at hand as opposed to the cost of financing the goods. For consumers that may lack a disciplined approach to credit, the enticement of the goods may cloud their judgment on financing.

This can be further exacerbated by the fact that the conversation about finance is usually held with a retail sales person whose main expertise lies in the goods being purchased. Usually a third party (a finance company) provides the finance in these transactions. These situations were ripe for miscommunication about financing terms. Several participants found that there were unforeseen charges and that the loan documents tended to be confusing. Indeed, this was more likely to occur with retailer-extended credit than with payday lending.

The same dynamic was at work with rent-to-own. The main consideration of the person was the need for a particular product. The conversation with the rent-to-own sales person is usually about the product itself and the 'easy' financing terms. It is only after the fact that people realized that this easy financing comes at a large cost. "I just fell in love with the sofa and I wanted to have it...I didn't realize how much it cost until months later" was how one Toronto participant described the process.

Yet most participants seemed to be aware that rent-to-own was not the best way to finance ownership and should be considered only for leasing. In Calgary, participants pointed to a recent promotion by IBM for "a computer for a dollar a day" as being an especially egregious example of rent-to-own. Other participants in Calgary and Vancouver compared rent-to-own to "leasing a car", which should only be done for short term needs or in cases where goods become quickly obsolete.

5.4 Attitudes Toward AFS Services

Participants were asked to compare the costs of the various forms of credit detailed in their tally sheets (Exhibit 1). Participants in all three cities had difficulty distinguishing between the specific cost of various forms of credit. To the extent that differentiation did take place, it was done so in a dichotomous fashion: banks and credit unions are "cheap" (yet unavailable) and everything else is "expensive" (and "easy to get"). As an example, some participants confused the bi-weekly rate of a payday loan with the annual percentage rates (APR's) charged by credit cards and finance companies. These were both seen as being "expensive" but the extent of the expense did not seem to matter.

5.4.1 Volume of Credit Major Consideration in Total Cost

Views on the cost of credit were often coloured by attitudes toward other credit parameters, most notably the *volume* of credit, which for many people is of far greater concern than the *per dollar* (or unit) cost of credit. Many people at the focus groups had significant credit card debt that occasionally resulted in personal bankruptcy. To these people, the volume of credit is the source of great anxiety. In a perverse way, many of these people consider the payday lending companies to be less repugnant than the credit card companies. Although the cost of credit is "high", you "don't have this debt hanging over your head and just snowballing". So the real cost of credit is the volume of credit times the per dollar cost. Even if AFS credit is expensive, it is usually highly structured as opposed to open-ended. This constrains

the volume of credit and, in the minds of some participants, leads to a lower total dollar cost of credit.

5.4.2 Strict Terms of AFS Loans Viewed as a Virtue

Given their views on the importance of the volume of credit, some participants had come to see the strict terms of the AFS as “necessary medicine”. Indeed this was considered to be a major benefit of payday loans: they are relatively small loans that add little to the volume of credit. When the volume of credit is a main consideration, the low volume/strict terms of the typical payday loan is actually seen as being a virtue.

5.4.3 Bank Holds Drive Cheque Cashing Business

Of importance to the participants was the fact that they could get their money right away from a cheque cashing institution. These are people who have both a very high need for cash and who are most likely to face holds on cheques by mainline financial institutions. These circumstances are tailor-made for the cheque cashing sector that specializes in satisfying the demand for cash while organizing their management systems around managing the risk of bad cheques.

5.4.4 Mainstream Movement to Fee-For-Service and AFS Prices

The holds issue combined with the movement of mainstream financial services to fee-for-service pricing makes cost comparisons more problematic. For example, a participant in Calgary noted that his bank would put constraints on his access to a recently-deposited pay cheque, limiting this to \$200. But the participants required “every dime” of his pay cheque. Although he could withdraw this over time, he would incur fees every time he made a withdrawal. Even though the bank service fees would definitely amount to less than the cheque cashing fees, to him cheque cashing was “about the same as the banks service fees”, especially when you consider the extra time involved to get all of the money from his cheque. Similarly, the time cost of cashing a first cheque at Money Mart was seen as being “basically the same as opening a bank account”.

5.4.5 The AFS as a “Value for Money” Service

In another vein, opinions on the cost of credit was heavily influenced by attitudes toward the level and convenience of service. As with most consumers, the participants recognized that a higher price was merely the cost of greater convenience. One Vancouver participant put it this way: “...when I go into the 7-Eleven I pay 6 bucks for box of cereal. But the place is open when I get out of work, so I pay it. Money Mart is just like that...you are paying for the convenience”.

5.4.6 Views on Customer Service

Although bank hold periods are the main driver of the cheque cashing side of the business, users of cheque cashing also pointed out that the advantage of Money Mart’s opening hours, with at least 1 branch in major municipal areas opened 24 hours. Many people worked in night shift jobs and were in the habit of stopping into Money Mart after work when other cheque cashing options were unavailable.

Beyond this, users of Money Mart pointed to the general friendliness of the staff and the welcoming atmosphere compared to banks.

The interview with the former Money Mart manager revealed that a great deal of effort had been made by the company to “spruce-up” the stores and to make them more inviting to females. Those that had used payday lending pointed to the fact that Money Marts were “welcoming” and that “they want to give you the money”. This was contrasted with the banks who were considered to be more judgmental and questioning. Vancouver participants also felt that Money Marts had greater privacy than the banks and were suspicious that banks were using their information systems to target customers for increases in credit card limits. Overall, customer satisfaction among users of Money Mart in all the groups among users was high.

5.4.7 Finance Companies As Source of Business Finance

In some instances, finance companies had acted as a key source of capital to finance small businesses that ultimately led participants away from the AFS sector. In Calgary, three participants had successfully used finance companies in this way. So when posed the question of expense, one participant turned the question on its head: “...expensive in relationship to what? I don’t think it costs a lot if I can pay \$2000 in interest but then make \$3000 with the money I have borrowed”. Although this situation was not commonplace, it does point out that the sub-prime market may serve the function of extending credit to those who would otherwise not qualify for credit and that it rations it such a way to make the borrowers focus on the cost of credit. As another Calgary participant put it: “ I got into debt through credit cards while partying in university...those bastards at the finance company charged me an arm and a leg for that money but if I didn’t have it, I wouldn’t have started my business.”

5.5 Pathways to the AFS

All customers of the AFS share the characteristic of having a poor (or no) credit rating that limited their access to mainline credit. Most often this credit rating resulted through credit card use. But within this, there are two customer types: disciplined credit users and ill-disciplined credit users. Disciplined credit users tend to be older, have learned from their bad credit experiences and are much more wary about credit in general. Many have cut up their credit cards and will only use the AFS in genuine emergencies. They are aware that credit cards are best when they are paid off monthly and are more inclined to comparison shop for credit.

Ill-discipline credit users may have a poor credit rating or no credit rating. Some are not the least bit interested in establishing a credit rating and see their use of the AFS as being a manifestation of their desire not to conform. Others are merely coping with debt through a variety of means. They tend to cope by revolving credit between various facilities but do not really have a plan for putting their high credit needs behind them. These people tend to be younger and may be on the path to personal bankruptcy but have yet to experience that trauma. They recognize that

they pay a lot for credit but are much more likely to focus on the volume of credit as opposed to the dollar cost or annual percentage rate (APR) of interest.

Exhibit 2 and 3 outline the characteristics of cheque cashing and pay day lending use of the participants. These users come to cheque cashing and payday lending through two main pathways: straight to the AFS based on its perceived merits or through a poor credit rating.

5.5.1 *Straight to the AFS*

Some participants have come to cheque cashing and payday lending without having significant experience of other forms of retail financial services. These people tend to be younger people who have started using cheque cashing services. They may have a bank account, but this is either dormant or rarely used. Many may not have established a credit rating or their credit rating is not an issue because they are not looking to borrow significant sums of money. In some cases, they value the “alternative” of the AFS because they see themselves living an alternative lifestyle. For instance, one Toronto participant proudly declared that he was using cheque cashing and payday lending for “recreation”.

Exhibit 2 **Cheque Cashing Use**

Numbers Using Cheque Cashing	30
Average Amount of Cheque Cashed	\$ 450.00
Minimum Amount	\$ 50.00
Maximum Amount	\$1000.00
Cost of cashing cheque (n=26)	
Those expressing cost as a percent	15
Those expressing as a dollar amount	10
Those expressing as both a per cent and dollar amt.	1
Average cost for those expressing as a per cent	3 per cent
Average cost for those expressing as a per cent	\$ 31.65

Source: Grant Insights. Data collected from tally sheets.

Like any financial services company, Money Mart endeavours to establish a loyalty relationship with its customers and, by all accounts, has had some success in doing this. These users tend to value the aforementioned convenience and service aspects of their relationship with Money Mart. Although they acknowledge that the initial steps of establishing this relationship can be very similar to a bank, in terms of filling in forms and the like, they do not really see any difference between this and a bank. They are far less likely to be aware of the cost of credit.

Within this group are people that could be best described as rational or quasi-rational users of cheque cashing and payday lending. These people operate in cash and have a

high demand for converting cheques into cash immediately. Although the cost of credit may be high, the bank does not offer them an opportunity to get all their cash without both incurring transaction fees and wasting time. They are inclined to see their relationship with the cheque cashing and payday lending organizations in a positive light. This is because they are not entirely cognizant of the relative cost of the service and in fact see these strict, closed-ended arrangements as preferable to the relatively open-ended credit card arrangements that have resulted in many of their peers' carrying high debt. So within the context of their financial discipline and needs, and the current market structure, they are simply making a rational decision to use cheque cashing because of its features.

Exhibit 3
Payday Lending Use

Numbers Using Payday Lending	10
Average Amount of Payday Loan (n=3)	\$ 335.50
Maximum Payday Loan	\$ 700.00
Minimum Payday Loan	\$ 120.00
Cost of Payday Loan	
Those expressing cost as a percent	3
Those expressing as a dollar amount	7
Average cost for those expressing as a per cent	25 per cent
Average cost for those expressing as a dollar amt.	\$ 85.00
Number that had rolled over a payday loan	2

Source: Grant Insights. Data collected from tally sheets.

5.5.2 Route R-9

Another major group of people will have had initial exposure to the AFS because of problems with mainstream credit, most likely via credit cards. Some of these people are using the AFS as a temporary measure to get through a difficult time. Others are in a situation of long term coping with no access to other sources of credit. They have incorporated the AFS into their financial coping but do not see anyway out in the foreseeable future.

This group is very aware of the dreaded “R-9” credit rating. They fully understand that the credit rating limits their financing options and leads to them paying more for finance. The “Straight to the AFS” group was more likely to express negative and dismissive sentiments toward the mainline financial institutions whereas this group was more likely to express dissatisfaction with the credit rating system. This manifested itself in two ways. First, they believe that the credit rating system is impenetrable meaning that extenuating circumstances or errors cannot be accounted for or corrected. This leads to the second concern; unsolicited increases in credit

card limits expose them to credit card fraud that will affect their rating, which they believe they have very little power to correct.

All this can lead them to using the AFS. Although they may very well develop relationships with AFS institutions, they clearly understand that this costs them dearly and they would prefer to repair their credit rating and deal with mainstream financial institutions. Some of these people have a plan to make this happen but others see no way out and incorporate the AFS into their coping strategies.

5.6 AFS Usage Behaviours: “Crisis, What Crisis?”

One area of interest during the focus groups (and the forthcoming household survey) were the usage patterns of the participants. Some participants indicated that they would use payday loans to deal with crises, the main one being the possibility that a utility would be cut off because of non-payment of a bill. No one at the focus groups indicated that they were using payday loans to avoid NSF fees on outstanding cheques.

A more likely scenario was that a person had incorporated payday loans into a cycle of high cost credit that may include credit cards, finance companies and pawnshops. The manager of Money Mart indicated that he saw many of the same customers come in for payday loans during the course of a year and a number of participants indicated that they had drawn on payday loans more than once during the course of a year.

At this juncture, an important distinction should be made between rollovers (or consecutive use) of payday loans and periodic use of payday loans. Some commentators in the United States have expressed concern with payday loans being rolled over, thereby generating astronomical APR's. A more likely scenario, based on the focus groups, is that payday loans are drawn on occasionally and incorporated into a cycle of payments. Although some participants had used payday loans several times during the year, there was no reporting of consecutive use of payday loans.

A common scenario is that a person may be short money for a minimum payment on a credit card and they may use the payday loan to make this payment and free up space on their credit card for other payments. They may also consider pawning items or use them to secure a small loan at a pawnshop. In fact, focus group participants were more likely to roll over a pawnshop loan than a payday loan because they may be emotionally attached to the collateral in some way. This is not really crisis use per se unless one considers the whole situation a crisis.

Any multiple use of payday loans during the course of the year will undoubtedly result in a very high annual cost of credit, especially given the prevalence of item fees and the possibility of NSF charges. However, this behaviour is somewhat different in kind from rolling over a payday loan. As such, advocates might be wise to consider the total usage during the year as opposed to merely rollover behaviour.

5.7 Disclosure and Information Issues

Most of the concern about disclosure and information issues related to retailer-extended credit, rent-to-own and the credit rating system. These issues have already been discussed in previous sections. The main relevant point here is that many people who use the AFS are insufficiently focused on the cost for disclosure rules to have a significant effect on their behaviour. With reference to a payday loan, one participant in Calgary noted: “its two or three pages of gobblygook...you don’t read it because you just want to get the money”.

In general, participants were not wildly impressed with the idea of improving disclosure. To the extent to which they thought it would make a difference was in terms of ensuring that no “extra fees” were added to leasing, retailer finance or rent-to-own contracts. But participants did not seem to have any issue with disclosure as it applied to cheque cashing and payday lending. They either knew that this was “expensive” or they didn’t seem to care because they wanted the money.

5.8 Enforcement Issues

Another concern expressed in the US literature is about aggressive enforcement methods to collect debts in the AFS sector. One tactic is to threaten to deposit a cheque that the payday lending company thinks will likely “go NSF”. But as seen earlier, there is no need for Money Mart to make any threats in this regard, they just go ahead and do it!

The interview with the former Money Mart manager indicated that there was little reason for Money Mart to become aggressive in their collection practices. To begin, the loan amounts were usually fairly small and not secured by personal property. It was more effective to have a teller telephone the person and work out an arrangement or have a discussion with the person the next time they came in, which more often than not they did. Money Mart’s internal information system was effective at identifying repeat customers with outstanding debts. Notwithstanding this, and the fact that no one at the focus group had experienced poor treatment directly, some participants in Calgary indicated that they had overheard clerks being aggressive with customers over the telephone. Aggressive collection was more likely to be reported in relationship to finance companies who “can get quite nasty.... they’ll harass you at work” in the words of a Calgary participant.

To the extent that there were threats leveled at the participants, these were more likely to be by utilities for unpaid bills in the form of removal of service. As mentioned, such threats may very well be an impetus to someone using a payday loan.

5.9 Alternatives to the AFS

Most people considered the payday lenders as the “end of the line” primarily because of their reputation for doling out very small and expensive loans. The only other alternatives to payday lending were family and friends and loan sharking.

The use of family as a source of money depended very much on a person’s existing relationship with family members. For instance, one Toronto participant indicated that he always went to his mother for financing and this was a long-standing relationship. More commonly, people were concerned that using family and friends as a source of money would compromise their relationship and violate their privacy. This was especially true for people who were using payday loans “recreationally” as they realized that they could not go to their family for this purpose. Also, some participants indicated that their family was in similar financial straits, so the idea of going to them to get money to pay the utility bill was a non-starter.

In general, people preferred arms-length relationships in borrowing, even if this cost them much more money. The exception would be young people who would occasionally use a parent to co-sign a loan with a bank or finance company.

No one had direct experience of loan sharking and no one suggested that they would be tempted to use a loan shark in the absence of payday lending. A more likely scenario would be that they would simply have to do without this source of funds, as people undoubtedly did before the introduction of payday loans. Loan sharking was seen as being something that was used by gamblers or drug addicts, people who were, apparently, unrepresented at the focus groups.

5.10 Role for Government

Participants were generally skeptical about the ability of government to improve the situation through increased regulation. As mentioned, non-users were more likely to see cheque cashing and payday lending organizations in a negative light but only a few thought that they should be regulated. For example one participant in Calgary, who was especially vociferous in her disgust for the payday lenders, suggested that she did not want to see them outlawed but rather regulated so that they could not lend to young people who were going to use the funds for recreational purposes.

People generally thought that more variety in financing options, even high-priced options, would work in their favour. To the extent that they wanted more government involvement, it was more likely to be in general regulation of the financial services sector as opposed to specifically the AFS sector. In this way the participants felt, for example, that all finance service charges should be regulated and that “hidden charges” should be banned.

6.0 Summary Comments

The focus groups revealed a complexity of experience that does not easily lead to straightforward prescriptions for regulating the AFS. On the one hand, cheque cashing and payday lending institutions profit from a group of customers who are in financial straits and others who are lacking in financial literacy. The companies' management systems for maximizing profits from these people are, at best, ethically suspect.

On the other hand, the pre-conditions leading to the use of the AFS very much grow out of other parts of the financial services sector (especially credit cards) and our consumer culture. Moreover, there are genuine needs that these customers have, in terms of convenience and customer service, that are addressed by companies such as Money Mart and that are not addressed by mainline financial institutions. Notwithstanding the moral repugnance of the industry to some, the customers themselves are actually quite satisfied with the services and do not want to see them outlawed.

These themes need to be explored in greater detail through a larger sample of customers to verify some of the findings reported here. Moreover, a larger sample will allow for more statistically representative findings for quantitative data such as usage volumes and costs. Addressing these information needs will be a key role of the large-scale household survey that is planned for the Fall 2001.

Appendix A: Recruiting Screener for Focus Groups

Grant Insights

31 Fairfield Road
Toronto, Ontario
M4P 1S9

Recruiting Screener
June 22, 2001

RESPONDENT _____

TELEPHONE # _____ DATE: _____

POSTAL CODE _____

INTERVIEWER _____

SUPERVISOR _____

CITY:	Toronto	1	GROUP:	5:30PM	1
	Calgary	2		7:30PM	2
	Vancouver	3			

Hello, my name is _____ of _____, a market research firm. We are conducting a research study on non-bank consumer credit and financing, and we are looking for people to take part in a focus group.

1. First of all, do you, or does anyone in your household work for any of the following types of companies? **(READ LIST. IF "YES" TO ANY, THANK AND TERMINATE)**

Market research	1	
Banking	2	
Finance company	3	
Cheque cashing company	4	
TERMINATE		
Tax rebating company	5	
The federal government	6	
Advertising or media	7	
NONE OF THE ABOVE	0	→ CONTINUE

2a. Have you ever taken part in a focus group discussion before?

- Yes 1 → **CONTINUE**
- No 2 → **SKIP TO Q.**

3

2b. How long has it been since you last took part in a focus group? (**DO NOT READ LIST**)

- 6 months or less 1 → **TERMINATE**
- More than 6 months ago 2 → **CONTINUE**

3. Would you feel uncomfortable freely expressing your opinions in a group of people?

- Yes 1 → **TERMINATE**
- No 2 → **CONTINUE**

3. The focus groups we are recruiting will take place at 5:30 PM and 7:30 PM on...(READ DATE)...and participants will be paid an honorarium of \$50 for attending. Are you available to take part in a focus group discussion on this date?

Yes

1 → CONTINUE

No

2 → TERMINATE

4. We are recruiting people who have used alternative sources of consumer credit and financing other than banks or trust companies, whether for emergencies, or for short term cash needs. Have you ever borrowed money from or arranged financing through any of the following types of companies? **(READ LIST. CIRCLE ALL THAT APPLY)**

A finance company
(like Household Finance
or Avco Financial Services)

1 →

**RECRUIT
FOR 5:30
GROUP**

A cheque cashing outlet
(like Money Mart or UniCash)

2

A payday advance loan company
(like Money Mart, Stop 'n' Cash
or Financial Stop, where consumers
RECRUIT
are loaned money against their

FOR

7:30

paycheques)
GROUP

3

A tax discounter (ie:, will advance
you money on your tax return in
return for a percentage of the total
amount you are owed)

4

NONE OF THE ABOVE

0 →

TERMINATE

5. Which of the following categories best describes your age group?
(READ LIST. CIRCLE ONE ONLY)

Under 18

1 → TERMINATE

18 to 24	2	
25 to 34	3	RECRUIT A
35 to 54	4	GOOD MIX
55 or more	6	

6. **RECORD GENDER. DO NOT ASK**

Male	1	RECRUIT A
Female	2	GOOD MIX

7a Are you working or not working?

Working	1	
Not working	2	→ SKIP TO

Q 7c

7b What is your occupation, that is, what kind of work do you do?

_____ **NOW SKIP TO Q.**
8

7c Are you ... **(READ LIST. CIRCLE ONE ONLY)**...?

Retired	1
A student	2
A full-time homemaker	3
<u>or</u> not currently employed	4

8 What is the highest level of education you have completed? **(DO NOT READ LIST. CIRCLE ONE ONLY)**

Some/completed primary school	1
Some/completed secondary school	2
Some/completed community college	3

- Some/completed university 4
- Some/completed postgraduate degree 5

9. Which of the following best describes your marital status? **(READ LIST. CIRCLE ONE ONLY)**

- Married or living common-law 1
- Separated or divorced 2
- Single, never married 3
- Widowed/widower 4

10. And finally, which of the following categories best describes your annual household income before taxes? **(READ LIST. CIRCLE ONE ONLY)**

- Under \$10,000 1
- \$10,000 to \$19,000 2
- \$20,000 to \$29,000 3
- \$30,000 to \$39,000 4
- \$40,000 to \$49,000 5
- \$50,000 to \$79,000 6
- \$80,000 to \$99,000 7
- \$100,000 or more 8

CONFIRM DETAILS AND RECRUIT FOR APPROPRIATE GROUP

Appendix B: Focus Group Discussion Guide

Grant Insights

31 Fairfield Road
Toronto, Ontario
M4P 1S9

I. INTRODUCTION

- Role of moderator
- No right or wrong answers
- Please do not self-censor
- What is said in the room stays in the room
- Taping for moderator's reference only (report)
- Confidentiality, don't talk to the next group coming in

II. RESPONDENTS

- Who has been to a group before, who hasn't (SHOW HANDS)
- Introductions around the table
 - First name
 - Household composition/family/kids
 - What do you do (occupation)

III. AWARENESS OF FINANCING OPTIONS

- Third Person *Awareness* of types of financing
 - Credit Card
 - Car loan
 - Mortgage
 - Personal loan
 - Line of credit
 - Loan consolidation
 - Hire purchase/rent to own
 - Car equity loan
 - Payday loan

- OTHER VOLUNTEERED MENTIONS
- Probe for any not mentioned
- ***For each, discuss...***
 - Advantages/disadvantages
 - Perceptions of cost and specific rates
 - Perceived reasons for using each

IV. DESCRIBE YOUR CURRENT FINANCING BEHAVIOUR

- First Person *Currently used* sources of
 - Credit Card
 - Car loan
 - Mortgage
 - Personal loan
 - Line of credit
 - Loan consolidation
 - Hire purchase/rent to own
 - Car equity loan
 - Payday loan (**SEPARATE SHEET**)
 - OTHER VOLUNTEERED MENTIONS
- Probe for any not mentioned
- **HAND OUT TALLY SHEETS TO NOTE MONTHLY PAYMENTS/RATE**
- CREDIT CARDS
 - Is a balance carried?
 - What is/are rates?
 - How do you know? Where do you get information on costs?
 - How much?
 - Payments?
 - Perceptions of credit card rates vs. bank loan rates
 - Perceptions of ease of use of card credit
 - Why card credit vs. other forms of credit?
- CAR LOAN
 - How much
 - How long

- What is rate?
- Payments
- MORTGAGE
 - How much
 - Payments
 - How long
 - What is rate
- PERSONAL LOAN
 - From whom?
 - For what?
 - How much
 - Payments
 - How long
 - What is rate
- LINE OF CREDIT
 - Reasons
 - From who
 - Collateral/guarantee
 - How much
 - How much used
 - Payments
 - What is rate*
- LOAN CONSOLIDATION
 - How many loans consolidated
 - Who with
 - *Was loan/debt consulting used*
 - Reasons
 - New payments vs. old payments
 - What is rate
 - How do you know? Where do you get information on costs?
- HIRE PURCHASE/RENT TO OWN
 - What/how much

- Payments
- How long
- Reasons vs. purchase
- What is rate

- **PAYDAY LOAN**
 - Reasons
 - What did you use it for (emergency or regular payments)
 - Is this considered an alternative to bouncing a cheque and incurring fees for this?
 - With who?
 - How much?
 - Where did you get the information on how much it would cost?
 - Frequency? Is it rolled over? If not rolled over, do you use it regularly?
 - Payments?
 - How long?
 - Have you used more than one lender?
 - What is rate - daily/monthly/annual

- **ASK RESPONDENTS LOOK AT SHEET AND CONSIDER TOTAL COST**
 - How do you feel about the cost of credit..is it high or low?
 - Is better financing rate available.....?
 - Banks/trusts
 - Finance companies
 - Credit unions
 - Neighbours/friends(PROBE GENTLY FOR LOANSHARKING)
 - For each used...
 - Reasons
 - Advantages/disadvantages
 - For each not used...

- Why not
- Advantages/disadvantages
- Credit history with each

V. CHEQUE CASHING (U&A)

- Awareness/usage of cheque cashing
 - Frequency
 - Average amounts
- Outlets used/aware of
 - Cash Stop
 - Money Mart
 - Cash 'n' Go
 - OTHER
- Reasons (WRITE ON FLIPCHART - PROBE EACH MENTIONED)
 - Emergencies
 - Convenience
 - Timely
 - No bank account
 - Just moved/transient
- Advantages/disadvantages
- Awareness of rate
 - Daily
 - Monthly
 - Annual
- Perceptions of fairness/unfairness (IF NOT MENTIONED)
- Are other sources of emergency/short-term cash available
 - Banks/trusts
 - Finance companies
 - Credit unions
 - Neighbours/friends (PROBE GENTLY FOR LOANSHARKING)

- For each not used...
 - Why not
 - Advantages/disadvantages
 - Credit history with each

VI. TAX REBATE DISCOUNTING

- Awareness/usage of payday loans
 - Frequency
 - Average amounts
- Outlets used/aware of
 - H&R Block
 - BenTax
 - Others
- Reasons (WRITE ON FLIPCHART - PROBE EACH MENTIONED)
 - Convenience
 - Get cash fast
 - Timely
- Advantages/disadvantages
- Awareness of cost/rate
 - Daily
 - Monthly
 - Annual

VII. ROLE OF GOVERNMENT

- Which financing sources are regulated (WRITE ON FLIPCHART)
 - Banks
 - Trust companies
 - Credit unions
 - Finance companies (like Avco or Household Finance)
 - Car leasing firms
 - Cheque cashing outlets

- Payday loan companies
- Car equity loan companies
- Pawnshops

- Probe for any not mentioned

- For each mentioned...
 - How much are they regulated
 - Are rates regulated
 - Does regulation benefit company or consumer
 - Is regulation fair for the business
 - Is regulation fair for consumer
 - Is more regulation/oversight needed
 - Do they abuse current regulations

- Does the government have any role in regulating the alternative financing industry such as...?
 - Finance companies
 - Cheque cashing outlets
 - Payday loans companies
 - Car loan equity companies
 - Pawnshops

- Do consumers need protection from this industry?

- What type of information should the government insist that companies provide to help you make good decisions?
 - Where do you look for information that helps you decide which company and financial services to use?
 - Do you feel you have enough information or too much information right now?

IX. "BLUE SKY SESSION" (RESPONDENTS WRITE ON COMMENTS SECTION OF SCORE SHEET)

- In a perfect world, what would the role of the government be in regulating the financing and loans industry and protecting the rights of both consumers and businesses?