**Payday Loans**

**How do payday loans work?**

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**Generally people use payday lending to access a few hundred pounds in between pay dates for rainy days when unexpected financial shortfalls need to be addressed.**

**An agreement is reached regarding a proposed repayment date and a post – dated cheque is given to the lender containing the amount of the loan plus interest.**

**BE WARNED!**

**Should you miss the payment date further extortionate fees will be incurred.**

**How many people use them?**



Taking advantage of huge marketing budgets, payday lending firms are buying advertising space across the media to raise their profiles and target consumers. Millions of consumers are turning to payday loans to access fast and easy cash but safer and less costly alternatives are available.

**Payday Loans – The Facts**

* If you like **high cost, short term loans** with extortionate fees then payday loans are for you – or not!

Convenient and all too easy to access it’s the accessibility of these loans that make them dangerous. These loans make it easy to act first, think later.

On the surface the costs can seem decent but often if you dig a little deeper there’ll be some nasty fees and hidden charges.

* Charging **more per month than credit cards** do for a year, payday loans just don’t add up!
* APR’s are often meaningless but do act as perhaps the only obstacle in reminding you of **exorbitant interest fees** charged even when borrowing small amounts (see example table below). If you find yourself unable to pay the loan off in time these APR’s can quickly become a reality especially when hidden fees and charges start adding up.
* Payday loans will only **compound your problem** not ease it. If you continually have to rely on payday loans, there’s a problem. Time to take a look at your finances in detail. Create a budget to assist you in balancing your income and outgoings.
* **If there’s a danger you won’t be able to repay it on time – you can’t afford to get one**

If you don’t know how you will be able to repay the loan, don’t take it out. You may be desperate for that money but borrowing using a payday loan is going to make life far more difficult in the long term. **There are** **better, cheaper alternatives available** such as Credit Unions where you can organise a repayment scheme you **can** afford. (See the example below by way of comparison.)

* Taking the rollover option? **Beware!** Whilst this might seem like a good option, you may be racking up further fees and charges. This only works out for one party and that party isn’t you. You could be doubling the initial fee you paid and then **owing more money** because of the interest on the new balance.
* Phew, you’ve repaid on time but as far as the company are concerned you are now a **walking target** for an even bigger (even higher and nastier interest rate – what they don’t tell you) loan.
* Taking a payday loan can **hurt your credit rating**. Credit reference agencies set apart payday loans from high street ones on credit reports. Underwriters (making lending decisions) are able to identify how much and how often you’ve used them.

The presence of a payday loan on a credit report throws up red flags to lenders. Implying that the applicant has underlying money management and budgeting issues, this **unsettles lenders** throwing doubt on whether the applicant will be able to meet their lending terms and make their monthly payments.



The Money Saving Expert website says,

“Mortgage lenders, including GE Home Lending and Kensington Mortgages, have publicly said **applicants who have used payday loans won't be accepted for a mortgage** with them - even if they were fully repaid on time. Yet even those who haven’t spoken up are likely to behave in a similar way.”



* Someone else paying your debt on your behalf? You could be putting their account at risk. Common tactics of payday lenders include using a recurring payment system called ‘Continuous Payment Authority’ or

CPA. You are asked to give the 16 digit number on the front of the card. In doing this you are giving the **lender the right to take payment whenever they wish.**

What this means:

You (or your payer) may have prioritised your (their) bills to meet the necessities and be about to pay but the payday loans company will prioritise their debt over anyone else’s and simply take the money. This could **leave priority debts unpaid** and not enough in the bank to pay off the debt.

What can you do?

As it is your right to cancel CPA’s, you can speak to the bank running the account regarding cancelling them. It is better for you to have full control over the money leaving your or someone else’s account and pay as and when you owe the money.

Payday lenders keep information on anyone making payments on your behalf and can use their details to pay back any future loans without consultation or agreement.

|  |  |
| --- | --- |
| * If after reading this you think payday lenders are bad – **loan sharks are even more unscrupulous, devious, and immoral** and are not shy to **use threats and acts of violence** to get what they want. | Great white.jpg |

If you know of loan sharks near you, report them on **0300 555 2222** (you can also text LOAN SHARK and lender's details to 60003, or email [reportaloanshark@stoploansharks.gov.uk](mailto:reportaloanshark@stoploansharks.gov.uk)).

**WARNING**

**DO NOT USE YOUR OVERDRAFT** to pay your payday loan off – you’ll be sinking yourself far deeper in debt. Please refer to the **Bank Overdrafts** section of the document.

**Cheaper borrowing alternatives to payday loans**

The table below details the interest incurred when borrowing just £100 at an APR interest rate of 4215% (lending rate for a leading payday loan company).

|  |  |
| --- | --- |
| Duration | Cost (£) |
| 1 Month | 36.85 |
| 2 Months | 87.28 |
| 3 Months | 156 |
| 4 Months | 251 |
| 5 Months | 380 |
| 6 Months | 557 |
| 7 Months | 799 |
| 8 Months | 1130 |
| 9 Months | 1584 |
| 10 Months | 2204 |
| 11 Months | 3053 |
| 12 Months | 4215 |

So that’s £4215 in one year! Imagine the interest charge if you borrowed for 2, 3, 4 or even five years?

Even if you only intend on paying it back within a month you are still paying 36.85% per month interest! It all begins to add up...if you pay an initial fee to receive the loan and then add the interest incurred over the course of that month that’s now:

|  |  |  |
| --- | --- | --- |
| Loan amount |  | £100.00 |
| Initial payday loan fee (example) | + | £ 30.00 |
| Interest @ 36.85% | + | £ 36.85 |
| **Total** | = | **£166.85** |

Compare this with an indicative interest rate of a Credit Union loan of £100 at an APR of 27%

|  |  |
| --- | --- |
| Duration | Cost (£) |
| 1 Month | 2.01 |
| 2 Months | 4.06 |
| 3 Months | 6.16 |
| 4 Months | 8.29 |
| 5 Months | 10.47 |
| 6 Months | 12.69 |
| 7 Months | 14.96 |
| 8 Months | 17.27 |
| 9 Months | 19.63 |
| 10 Months | 22.04 |
| 11 Months | 24.50 |
| 12 Months | 27 |

So by comparison when you add the interest over a month period the total of a payday loan doesn’t even compare!

|  |  |  |
| --- | --- | --- |
| Loan amount |  | £100.00 |
| Initial payday loan fee (example) | + | £ 0 |
| Interest @ 2.01% | + | £ 2.01 |
| **Total** | = | **£102.01** |

If you are borrowing money for a short period of time, the interest rate could be reduced or if you are already saving with a credit union the rate could potentially be dramatically reduced.

To help you calculate exactly how much a loan could cost you here’s a [link](http://www.bbc.co.uk/consumer/24746198) to a monthly interest calculator.

Or to compare loan rates use this useful [Loan Comparison Tool](http://www.moneymadeclearwales.org/loan-comparison-tool)

**The following information has been sourced from** [The Guardian](http://www.theguardian.com/money/2013/dec/15/credit-unions-payday-lenders)

**What is a credit union?**

They are not-for-profit financial organisations offering an increasingly wide range of savings and loan products. They serve groups of people with a common interest and are often most appreciated by members on low incomes who would otherwise struggle to access financial services.

The sector isn't only for the poorest members of society – many members are attracted by its ethical approach to finance – and it is doing its best to modernise so it can compete with mainstream financial services companies. It is also moving into products such as bank accounts and mortgages. The largest credit unions, such as Glasgow Credit Union, London Mutual Credit Union and the NHS Credit Union, have tens of thousands of members. The smallest have just a few hundred.

**Who can join?**

Each credit union serves a particular section of the community. However, members must, by law, be linked by a "common bond" – they might all live in the same part of the country, say, or work for the same employer. Credit unions also exist to serve members of trades unions, religious groups and other organisations. You may be eligible to join several – you could even set up your own.

Credit unions are owned and run by their members and you will have to buy shares in the organisation to join. Typically, one share is enough and you'll be able to pay as little as £1.

**How much do they cost?**

Terms vary on the cost of loans, how much you may borrow and over what period. Rates typically start at around 1% a month – the equivalent of an annual interest rate of 12.7%.

By law, credit unions may not charge an annual rate of more than 26.8% (around 2% a month), which is a fraction of what borrowers pay to companies such as Wonga. There is also a ban on hidden charges and early repayment fees. All the same, borrowers with the best credit ratings should be able to find cheaper deals with mainstream loan providers and credit card lenders.

Search for your local credit union [here](http://www.findyourcreditunion.co.uk/home).

**Bank Overdrafts**

**Payday loan interest rates may be extortionate but high street banks have a product where the charges are simply downright shocking!**

Bank charges incurred for going over a pre-agreed overdraft limit are beyond belief. Money Saving Expert has this to say about how expensive bank charges are in comparison:

**“**Clydesdale Bank charges £25 per day for going beyond your limit. I tried to calculate this in Excel as an APR, based on someone getting a £25 charge a day for being £1 over. The resultant interest rate was TOO LARGE FOR EXCEL TO CALCUATE % APR – which means it’s a ‘figure with way more than 300 zeros after it’ percent.

So I had to take more standard charges like Nationwide’s £15 per item or Lloyds £5-10 per day depending on how overdrawn you are (see the [Bank charges comparison guide](http://www.moneysavingexpert.com/banking/bank-charges-compared) for more).

But even here, if you got a charge for being £1 over, it was too large to calculate so I went for the following scenario…

Go £5 over your overdraft at Lloyds and get charged £5. Based on payday loan calculation rules this would be roughly: 7,500,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000,000% APR.

Or, to put it another way – compare the above costs to borrowing a range of amounts at an APR of 5,000%:

|  |  |
| --- | --- |
| **Amount** | **Day’s cost at 5,000% APR** |
| £1 | 1p |
| £10 | 11p |
| £50 | 54p |
| £100 | £1.08 |

As you can see, in comparison 5,000% APR is cheap.

Banks have three limits within overdrafts:

* The authorised overdraft *– ie, no bank charges.*
* The unauthorised, paid overdraft *– ie, there will be bank charges, but your cheques/DDs don’t bounce.*
* The unauthorised, unpaid overdraft *– ie, there will be bank charges and your cheques/DDs do bounce.*

These are just functions of a bank account – the banks don’t have to have a ‘paid’ overdraft, it was introduced to increase profitability and added over £3 billion a year to their coffers. Of course during the [bank charges reclaiming](http://www.moneysavingexpert.com/reclaim/bank-charges) height over a billion was paid back – and still now a few whose charges cause hardship can get some cash back. Yet overall it’s still immensely profitable.

|  |  |  |
| --- | --- | --- |
| **Fee** | **Amount** | **Description** |
| **Monthly Fee** | £15.00 | You will pay this fee if you have an Unplanned Overdraft at any time during your monthly billing period (even if your next monthly billing period is only a few days away).  **You will be charged a maximum of one monthly fee in a monthly billing period** |
| **Daily Fee** | **Unplanned Overdraft balance is:**  Less than £25.00 = £ 6.00 per day  £25.00 - £100 = £15.00 per day  More than £100 = £20.00 per day | You will pay a daily fee for using an Unplanned Overdraft. The amount of the fee will be worked out at the end of each day (including weekends and bank holidays) on the balance of your Unplanned Overdraft.  **You will be charged a maximum of 10 daily fees in a monthly billing period.** |

**Useful links:**

[Money Saving Expert Payday-Loans Information](http://www.moneysavingexpert.com/loans/payday-loans)

[Find Your Credit Union](http://www.findyourcreditunion.co.uk/home)

[The Guardian](http://www.theguardian.com/money/2013/dec/15/credit-unions-payday-lenders)

[Monthly Interest Calculator](http://www.bbc.co.uk/consumer/24746198)

[Debt Free Wannabe Forum](http://forums.moneysavingexpert.com/forumdisplay.php?f=76)

[Citizens Advice](http://www.swanseaneathporttalbotcab.org.uk/)