



Financial Consumer
Agency of Canada

Agence de la consommation
en matière financière du Canada



*The Cost of
Payday Loans*

Protecting Consumers



Informing Canadians

Canada 

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The Cost of Payday Loans

What is a payday loan?

A payday loan is a short-term loan that you promise to pay back from your next pay cheque. A payday loan is sometimes also called a payday advance.

Normally, you have to pay back a payday loan on or before your next payday (usually in two weeks or less). The amount you can borrow is usually limited to 30 percent of the net amount of your pay cheque. The net amount of your pay cheque is your total pay, after any deductions such as income taxes. For example, if your pay cheque is \$1,000 net every two weeks, your payday loan could be for a maximum of \$300 ($\$1,000 \times 30\%$).

A payday loan is a very expensive way to borrow money.

Payday loans are offered by privately owned payday loan companies and by most cheque-cashing outlets. The government does not regulate these companies.

Internet lenders

Payday lenders also operate on the Internet. Because Internet lenders are not able to actually see your identification and income documents, they will often ask for more personal information than is normally needed to process a loan, such as your social insurance number, your driver's licence number, your mother's maiden name and what the loan will be used for. By applying for payday loans on the Internet, you run the risk of having your personal information stolen from low-security Web sites. It can also be more difficult to detect and avoid fraudulent payday loan sites that exist only to gather and sell your personal information. Where possible, avoid using Internet payday lenders.

How does a payday loan work?

Before giving you a payday loan, lenders will ask for proof that you have a regular income, a permanent address and an active bank account. Some payday lenders also require that you be over the age of 18.

To make sure you pay back the loan, all payday lenders will ask you to provide a postdated cheque or to authorize a direct withdrawal from your bank account for the amount of the loan, plus all the different fees and interest charges that will



be added to the original amount of the loan. The combination of multiple fees and interest charges are what make payday loans so expensive (see page 6 for an explanation of the various fees associated with these types of loans).

The lender should also ask you to sign a loan agreement. If the lender does not offer to give you a copy of the loan agreement, ask for one. **Read this document carefully before signing it, and keep a copy for your records.**

By signing the loan agreement, you are confirming that you have read, understood and agreed to all of the terms and conditions of the loan. These terms and conditions usually include:

- the amount of the loan and the date you must pay it back;
- any upfront or first-time fees and charges added to the amount of the loan;
- various service fees and charges;
- the different repayment options;
- any fees and interest charges added to the amount of the loan when the loan is paid back on time; and
- the consequences and any fees charged when the loan is *not* paid back on time.

Before you decide to get a payday loan, make sure you know and understand what happens if you cannot pay the loan back on time, and what the costs are if you make a late payment.

How and when do I pay back the loan?

A payday loan agreement usually says that you must pay the total amount you owe for the loan on or before the date stated in your loan agreement. This includes the amount you borrowed, plus interest and any additional fees and charges.

Some lenders will cash your postdated cheque or process your direct withdrawal on the day the loan is due. However, some lenders may require that you pay the loan in cash, on or before the due date.

If you have not paid the loan in cash by the due date, some lenders may cash your cheque or process the direct withdrawal you signed on the day after your loan's due date, and charge you another fee. **Ask the lender what the most inexpensive way is for you to repay your loan.**

How does a payday loan affect my credit report?

Credit-reporting agencies collect information on whether or not you make your payments on time. This information, also called your "credit history," is part of your credit report and is used to calculate your credit score.

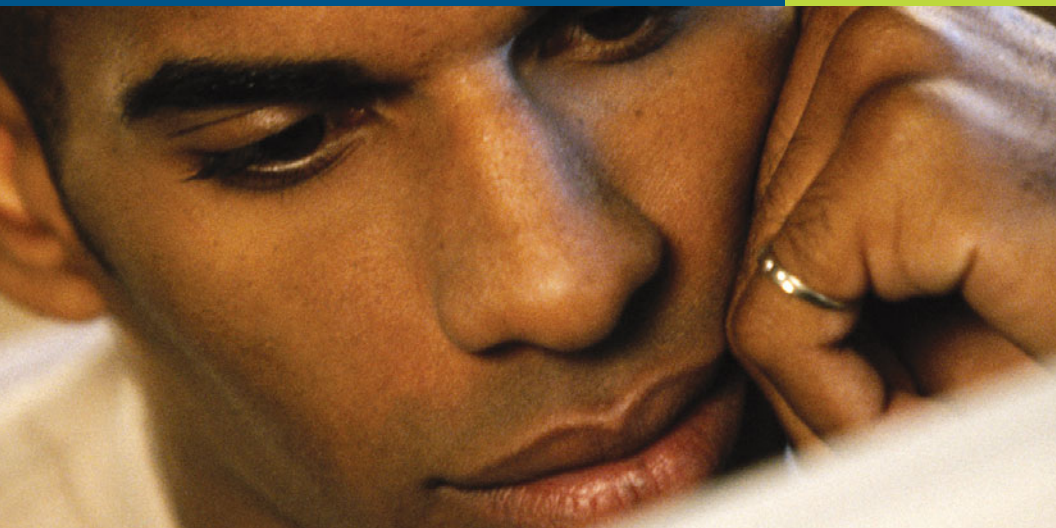
Making payments on time can help improve your credit score by demonstrating that you are able to manage your debt. Even if you have poor credit, you can rebuild it by using a credit card or other type of credit and paying back the money you owe on time.

This is not the case with payday loans. Since payday lenders are not currently members of the main credit-reporting agencies, getting a payday loan and paying it off on time will *not* improve your credit score. However, if you do not pay your loan back on time and it is sent to a collection agency,

this will likely be reported to a credit-reporting agency and could have a negative impact on your credit report.

There is a new service that is being offered to payday lenders — which is similar to a credit-reporting agency — called Teletrack Canada. If you have a history of using payday lenders, rent-to-buy services or certain consumer finance companies, your payment history and personal information will likely be kept in a database held by Teletrack Canada. Payday lenders can get access to this information before deciding to offer you a payday loan. They may also report on your dealings with them to this company. It is possible that in future, this kind of service may be linked with the main credit-reporting agencies.

Tip: You should get — and carefully review — a copy of your credit report from all three major credit-reporting agencies at least once a year to check for errors and to help prevent identity fraud. If you make your request in writing, the credit-reporting agencies will provide you, by mail, with a free copy of your report. For more information on how to obtain and understand your credit report see FCAC's guide entitled *Understanding Your Credit Report and Credit Score*. This free guide is available on FCAC's Web site (www.fcac.gc.ca) or by calling toll-free: 1-866-461-3222.



How much will a payday loan cost?

A payday loan is much more expensive than most other types of loans offered by financial institutions such as banks or credit unions. Before you apply for a payday loan, find out about all the fees and charges you will have to pay — including the fees you will be charged if you cannot repay the loan on time. The fees may not be easy to see right away, so read the agreement *carefully* before signing it. **If you do not receive an explanation of all of the fees, charges and interest that will apply to the loan, or if you are not satisfied with the explanation you receive, do not sign the loan agreement.**

The following is a list of some of the most common types of fees and charges associated with payday loans.

Interest

Interest is charged from the day you take the loan out until the day the loan, including all the fees, is paid back in full.

Payday lenders are not allowed to charge more than 60 percent interest on a loan, according to the *Criminal Code of Canada*. There are cases where payday lenders have taken customers to court for not paying back a payday loan, and the courts have determined that most of the fees and charges connected with payday loans are actually interest costs. This means that, in many cases, when the fees, charges and interest on payday loans are added together, they amount to a lot more than the 60 percent interest allowed.

According to the *Criminal Code*, all of the fees and charges described on the next three pages (except for NSF charges) may be considered “interest”. Several provincial governments have taken payday lenders to court over the amount of interest and fees they charge.

Administration fee/Processing fee/Convenience charges/Verification fee

These are all names for the same type of service charge that may be attached to payday loans. Sometimes service charges include the interest charged on the loan.

Service fees usually cost \$10 to \$35 for every \$100 borrowed — or 10 to 35 percent of the amount of the loan. A \$300 payday loan, due in two weeks, may cost you between \$30 and \$105, depending on the fees that apply.

Broker's fee

Sometimes a payday lender acts as a *loan broker* or intermediary between you the customer and an unidentified lender. Loan brokers charge a “brokerage fee”, in addition to any interest on the loan.

Collection fees

If you are not able to pay back your loan, the payday lender may place your account in collection. This means that a collection agency will contact you about the debt you owe in order to make sure you pay it.

Payday lenders may charge a fee if your debt to them is placed in collection. This will also likely have a negative effect on your credit report, and the lender could take you to court.

Early repayment fee

This is a fee that may be applied if you pay your loan back early, before the due date.

Initial or one-time set-up fee

Some lenders will charge you a one-time set-up fee of \$10 to \$15 if you are a first-time customer.



Loan repayment fee/First-party cheque-cashing fee

This is a fee that applies when you don't pay the loan in cash on or before the due date. Some lenders may charge you for depositing your postdated personal cheque or processing your direct withdrawal.

Locate fee

This is a fee that applies if mail sent to the address you give the payday lender is returned or if the phone number you give is disconnected when the payday lender tries to contact you.

Return fee/Non-sufficient funds (NSF) fee

If you don't have enough money in your bank account to cover the cheque you gave the lender, or the direct withdrawal you authorized to repay the loan on its due date, you may have to pay the lender a return fee or NSF fee. This fee can range from \$25 to \$75.

Your bank or credit union may also charge you an additional NSF fee if you don't have enough money in your account to cover the cheque or direct withdrawal.

Roll-over fee/Renewal fee/Finance charge/Additional charge/Extension fee

This fee is applied when you don't pay the loan in cash on or before the due date and the original loan is rolled over or extended for another period of time. If you roll your loan over, you will have to pay this extra fee.

Wage assignments or liens on personal property

Some lenders may try to get you to sign an agreement that says that you agree to have your employer sign over all of your wages to the payday lender if you are unable to repay what you owe. In many provinces, this is *illegal*.

If you think that a payday lender may be trying to do this, call the Financial Consumer Agency of Canada toll-free at 1-866-461-3222, to find the appropriate government body in your area that deals with these types of issues.

Some lenders may also try to get you to agree to use your personal property, such as your car, as security for a small loan in case you are unable to pay back what you owe them. Think carefully about this before signing any agreement. The value of the property you are signing over to the lender may be greater than the amount of the loan you are receiving. Also, once your property has been given to a lender, it may be very difficult to get it back, or the lender may already have sold it.

Some payday lenders also offer services or products to accompany payday loans, such as the following.

Insurance coverage

Some lenders may offer you death or disability insurance on your loan. This type of protection is usually expensive. Before you take this protection, make sure you need it and that you know exactly how much it costs, what the insurance covers and how to make a claim.

Make sure your lender has the right to sell you insurance. Ask the lender to show you proof that he/she is a licensed insurance agent. If you are not sure, call the Financial Consumer Agency of Canada toll-free at 1-866-461-3222, to find the appropriate government body in your area that deals with these types of issues.

Electronic loan cards

Some payday lenders offer electronic cards that can be loaded with your personal information, which allow you access to different branches of the same payday lender. The card can also be loaded with the amount of your payday loan and used like a debit card. You should know that these cards come with additional fees including issuing fees, reloading fees and fees for each electronic transaction you make with the card. These cards are also non-replaceable. They are like carrying cash. If you lose the card, you lose the money that is left on it, and the payday lender will not reimburse you.



How does the cost of a payday loan compare with other credit products?

Payday loans are much more expensive than other types of loans, including credit cards. But how much are you really paying? How does the cost of a payday loan compare with taking a cash advance on a credit card, using overdraft protection on your bank account or borrowing on a line of credit?

Let's compare the cost of using different types of loans. We'll assume that you borrow \$300, for 14 days. Note the considerable difference in the cost of each type of loan.

Comparing the cost of a \$300 loan, taken for 14 days¹

| | Payday loan | Cash advance on a credit card | Overdraft protection on a bank account | Borrowing from a line of credit |
|--|----------------|-------------------------------|--|---------------------------------|
| Interest | – | \$2.13 | \$2.42 | \$1.15 |
| | + | + | + | + |
| Applicable fees | \$50.00 | \$2.00 | – ² | – |
| | = | = | = | = |
| Total cost of loan | \$50.00 | \$4.13 | \$2.42 | \$1.15 |
| Cost of the loan expressed as a percentage of the amount borrowed ³ | 435% per year | 36% per year | 21% per year | 10% per year |

¹ The costs and fees shown in these examples are for illustration purposes only.

² The monthly service fee you pay for your banking service package often covers any processing fees for overdraft protection. To be sure, check your account agreement or talk to your financial institution.

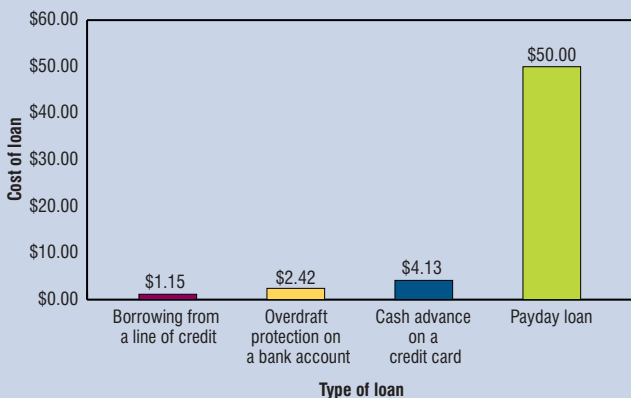
³ This is an estimate of the annual cost of the loan. This is calculated by adding together all of the fees, charges and interest charged after 14 days, and projecting this cost over a one-year period. Although the cost is expressed as a percentage of the amount borrowed, it does not represent the annual interest rate.



The following chart shows just how expensive payday loans are compared to other types of short-term loans.

Comparing the cost of a payday loan with other types of short-term loans

Based on a \$300 loan taken for 14 days



As you can see, borrowing from a line of credit is the cheapest option, followed by using overdraft protection on a bank account and taking a cash advance on a credit card. **Payday loans are by far the most expensive option.**

For a step-by-step guide on how to calculate the cost of these short-term loan options yourself, see the section on how to calculate the cost of different short-term loans at the back of this booklet (pages 17 to 22).

Here is some additional information about the various short-term loan options mentioned in the preceding tables.

Overdraft protection

Overdraft protection allows you to withdraw more money than you have in your bank account. The amount you owe for an overdraft is the difference between the money you have in your account and the amount you withdraw from your account. For example, if you have \$100 in your chequing account and you withdraw \$400 at an automated banking machine (ABM), the amount of your overdraft will be \$300.

The bank charges you interest on the amount you are overdrawn until you make a deposit that equals the overdraft, plus any interest and fees you have to pay. An overdraft is much cheaper than a payday loan.

Not all financial institutions offer overdraft protection. Contact your bank or credit union to see if it offers overdraft protection on its accounts and, if so, find out how much the overdraft costs and how it works.

Cash advances

Cash advances on your credit card are cash withdrawals, usually made with your credit card at an ABM or a bank. They can be as high as your credit limit. There is no interest-free period.

Interest is charged from the day you withdraw money from your credit card account until the day you pay back the cash advance in full. This is also a much cheaper option than a payday loan.

Lines of credit

This type of loan, offered by financial institutions, allows you to withdraw money, as needed, up to a maximum credit limit. You are charged interest from the day you withdraw money from your line of credit until you pay the loan back in full. A line of credit offers several payment options that you can choose from. The interest rate on a line of credit is usually lower than the interest rate on a credit card or overdraft.

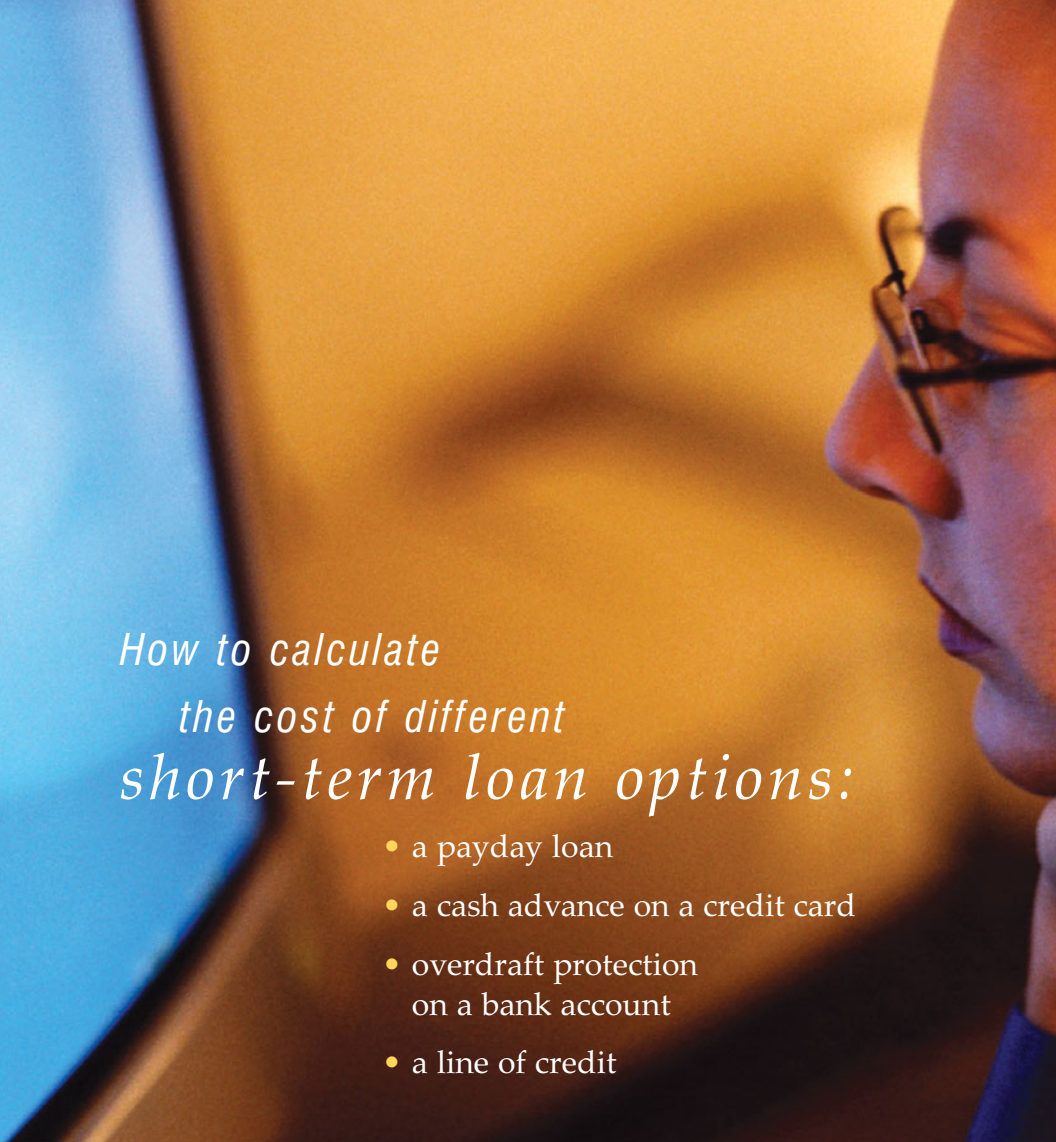


Things to consider before you apply for a payday loan

- Even if you think you may be turned down, ask your bank or credit union for overdraft protection on your bank account, or a line of credit. These are relatively inexpensive ways of obtaining access to extra funds, for short-term use.
- If you are turned down for any of these credit options, ask why. If the reason is that you have a poor credit history, contact the three credit-reporting agencies to get a copy of your credit report. Read the reports carefully to make sure that all of the information in it is correct. If you find any errors, contact the credit-reporting agency to find out how you can have the information corrected. The three major credit-reporting agencies in Canada are Equifax Canada, TransUnion Canada and Northern Credit Bureaus. All three of these agencies will give you a copy of your credit report for free if you request that it be sent to you by regular mail.
- Ask yourself if you really need to take out a loan, or whether you can get by until your next pay cheque. If you need the money immediately, try to make other arrangements. For example, you may be able to cash in vacation days. Or you might consider getting a short-term loan from a family member or a friend.
- If you find that you need to apply for a payday loan because you have no alternative, **only borrow an amount that you are 100 percent sure you can repay on the due date of the loan.**
- **Don't borrow more than you need.**

Things to consider if you take out a payday loan

- Don't be afraid to ask a lot of questions. Read carefully — and take home with you — a copy of the loan agreement that you are being asked to sign. Don't feel pressured to sign the loan agreement right away if you have questions and want more time to read through the agreement on your own. If the lender does not want to give you a copy of the agreement, look for another lender.
- Be sure to ask about all the fees, charges and interest that apply when you first get the loan, and what other charges you will owe if you can't pay the loan back on time.
- If you are taking out a payday loan at another location to pay back the first payday loan, or you are extending or "rolling over" the loan that you had with the same lender, you could find yourself in serious financial difficulty. The fees, charges and interest will add up quickly on these types of loans, which can put you into serious debt.



*How to calculate
the cost of different
short-term loan options:*

- a payday loan
- a cash advance on a credit card
- overdraft protection on a bank account
- a line of credit

How can I figure out the cost of each type of loan?

To estimate the total cost of a loan, including the annual cost of the loan expressed as a percentage of the amount borrowed, follow the steps below.

Step 1: Determine how much interest you will pay. First, find out the annual interest rate that applies to the loan (if there is one). Figure out the daily interest rate by dividing the annual interest rate of the loan by 365 days. Then, multiply that rate by the length of time you are taking the loan. Finally, multiply the result by the amount you will borrow, in dollars:

$$\begin{aligned} &\text{Amount of interest} \\ &= \frac{\text{Annual interest rate}}{365 \text{ days}} \times \text{Length of the loan (number of days)} \times \text{Amount of the loan} \end{aligned}$$

Step 2: Determine the total cost of the loan by adding any fees that may apply to the interest you will have to pay. Find out what fees apply to the loan and add them to the cost of the interest, found in Step 1:

$$\text{Total cost of the loan} = \text{Amount of interest} + \text{Total fees}$$

Step 3: Estimate the annual cost of the loan, expressed as a percentage of the amount borrowed. First, divide the total cost of the loan, found in Step 2, by the amount of the loan. Then, divide this rate by the length of time you are taking the loan (in days) and multiply it by 365 (the number of days in the year):

$$\begin{aligned} &\text{Annual cost of the loan (\%)} \\ &= \frac{\text{Cost of the loan}}{\text{Amount of the loan}} \div \text{Length of the loan (number of days)} \times 365 \text{ days} \end{aligned}$$

Here are some specific examples to help you with the calculations.

Example: Cost of a payday loan

Let's find out the cost of a \$300 payday loan, taken for 14 days.

We'll assume that the lender charges you a one-time set-up fee of \$10 and a service fee of \$40, which includes interest on the loan.

Step 1: Determine how much interest you will pay. In this case, there is no interest fee. The interest is therefore \$0.

Step 2: Figure out the cost of the loan by adding together any fees that apply and the interest you will have to pay. In this case, you would add the \$10 set-up fee and the \$40 service fee together:

$$\$10 + \$40 = \$50$$

Step 3: Estimate the total annual cost of the loan, expressed as a percentage of the amount borrowed:

$$\begin{aligned} & \text{Annual cost of the loan (\%)} \\ &= \frac{\text{Cost of the loan}}{\text{Amount of the loan}} \div \frac{\text{Length of the loan}}{\text{(number of days)}} \times 365 \text{ days} \\ &= \frac{\$50}{\$300} \div 14 \text{ days} \times 365 \text{ days} \\ &= 4.35 \text{ or approximately } 435\% \end{aligned}$$

The total cost of the payday loan would be \$50 with an annual cost of 435 percent of the amount borrowed.

Example: Cost of a cash advance on a credit card

Let's find out the cost of a \$300, 14-day loan, obtained by a cash advance on your credit card.

We'll assume your credit card has an annual interest rate of 18.5 percent and a \$2 processing fee for each cash advance. There is no annual fee.

Step 1: Determine how much interest you will pay, for 14 days:

$$\begin{aligned} & \text{Interest you will have to pay} \\ &= \frac{\text{Annual interest rate}}{365 \text{ days}} \times \text{Length of the loan (number of days)} \times \text{Amount of the loan} \\ &= \frac{18.5\%}{365 \text{ days}} \times 14 \text{ days} \times \$300 \\ &= \$2.13 \end{aligned}$$

Step 2: Add any fees that apply to the interest you will pay:

$$\$2.13 + \$2.00 = \$4.13$$

Step 3: Estimate the total annual cost of the loan, expressed as a percentage of the amount borrowed:

$$\begin{aligned} & \text{Annual cost of the loan (\%)} \\ &= \frac{\text{Cost of the loan}}{\text{Amount of the loan}} \div \frac{\text{Length of the loan (number of days)}}{365 \text{ days}} \\ &= \frac{\$4.13}{\$300} \div \frac{14 \text{ days}}{365 \text{ days}} \\ &= 0.36 \text{ or approximately } 36\% \end{aligned}$$

The total cost of a \$300 cash advance on a credit card would be \$4.13 with an annual cost of 36 percent of the amount borrowed.

Example: Cost of using overdraft protection on a bank account

Let's find out the cost you will pay for a \$300, 14-day loan obtained by withdrawing more money than you have in your bank account (if you have overdraft protection).

We'll assume that your financial institution charges you 21 percent interest annually on every amount overdrawn, and that the processing fee for the use of your overdraft is covered by your banking service package (check your account agreement to see if charges apply in your case). To calculate the cost, follow these steps.

Step 1: Determine how much interest you will pay, for 14 days:

$$\begin{aligned} & \text{Interest you will have to pay} \\ &= \frac{\text{Annual interest rate}}{365 \text{ days}} \times \frac{\text{Length of the loan}}{\text{(number of days)}} \times \text{Amount of the loan} \\ &= \frac{21\%}{365 \text{ days}} \times 14 \text{ days} \times \$300 \\ &= \$2.42 \end{aligned}$$

Step 2: Add any fees that apply. In this case, there are no additional fees:

$$\$2.42 + \$0 = \$2.42$$

Step 3: Estimate the total annual cost of the loan, expressed as percentage of the amount borrowed:

$$\begin{aligned} & \text{Annual cost of the loan (\%)} \\ &= \frac{\text{Cost of the loan}}{\text{Amount of the loan}} \div \frac{\text{Length of the loan}}{\text{(number of days)}} \times 365 \text{ days} \\ &= \frac{\$2.42}{\$300} \div 14 \text{ days} \times 365 \text{ days} \\ &= 0.21 \text{ or approximately } 21\% \end{aligned}$$

The total cost of a \$300 overdraft from a bank account would be \$2.42 with an annual cost of 21 percent of the amount borrowed.

Example: Cost of a loan from a line of credit

Let's find out the cost of the same \$300, 14-day loan, obtained by borrowing on a line of credit.

We'll assume that your financial institution charges you an annual interest rate of 10 percent on the amount borrowed, and that there are no service fees. Follow these steps.

Step 1: Determine how much interest you will pay, for 14 days:

Interest you will have to pay

$$\begin{aligned} &= \frac{\text{Annual interest rate}}{365 \text{ days}} \times \frac{\text{Length of the loan}}{\text{(number of days)}} \times \text{Amount of the loan} \\ &= \frac{10\%}{365 \text{ days}} \times 14 \text{ days} \times \$300 \\ &= \$1.15 \end{aligned}$$

Step 2: Add any fees that apply to the interest you will have to pay:

$$\$1.15 + \$0 = \$1.15$$

Step 3: Estimate the total annual cost of the loan, expressed as percentage of the amount borrowed:

$$\begin{aligned} &\text{Annual cost of the loan (\%)} \\ &= \frac{\text{Cost of the loan}}{\text{Amount of the loan}} \div \frac{\text{Length of the loan}}{\text{(number of days)}} \times 365 \text{ days} \\ &= \frac{\$1.15}{\$300} \div 14 \text{ days} \times 365 \text{ days} \\ &= 0.1 \text{ or approximately } 10\% \end{aligned}$$

The total cost of a \$300 loan on a line of credit would be \$1.15 with an annual cost of 10 percent of the amount borrowed.

The Financial Consumer Agency of Canada (FCAC)

The Financial Consumer Agency of Canada (FCAC) ensures compliance with the consumer protection laws that apply to banks and federally incorporated trust, loan and insurance companies. FCAC also provides consumers with accurate and objective information about financial products and services, and informs Canadians of their rights when dealing with financial institutions.

Information

All of our information, services and publications are available to you free of charge. Our publications help you shop around and choose the best financial product or service for your needs.

Protection

FCAC makes sure that federal financial institutions such as banks, trust, loan and insurance companies respect the laws and agreements that protect you. Call us for more information about your rights.

How to contact FCAC

Telephone (toll-free): 1.866.461.3222

(Monday to Friday, 8:30 a.m. to 6:00 p.m., Eastern Time)

Fax: 1.866.814.2224

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Notes:
