REPORT ON 2016 PAYDAY LOANS REVIEW

June 17, 2016

BEFORE: Karen Botting, B.A., B. Ed., M. Ed., Acting Chair
Régis Gosselin, B ès Arts, MBA, CPA, CGA, Chair
The Hon. Anita Neville, P.C., B.A. (Hons.), Member
Allan Morin, B.A., ICD.D, Member

Room 400 – 330 Portage Avenue
Winnipeg, MB R3C 0C4
www.pub.gov.mb.ca

330, avenue Portage, pièce 400
Winnipeg (Manitoba) Canada R3C 0C4
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1.0 EXECUTIVE SUMMARY

Pursuant to jurisdiction under *The Consumer Protection Act (Manitoba)* and *The Public Utilities Board Act (Manitoba)*, the Public Utilities Board of Manitoba (the "Board") conducted a public review and consultation of Manitoba's payday loan regulations and the payday loan industry. In this Review, the Board was specifically asked by the Minister of Tourism, Culture, Heritage, Sport and Consumer Protection to analyze the impacts of reducing the maximum allowable rate that may be charged for a payday loan, from $17 per $100 borrowed to $15 per $100 borrowed, and the impacts of reducing the proportion of a borrower's net pay, which is used to determine the maximum loan amount, from 30% to 25%.

Based on the evidence before it and the submissions made by Interveners and Presenters, the Board has made certain findings and recommendations which represent the results of the consultation as contained in this Report.

The Board recommends to the Minister that:

- The cost of credit for a payday loan remain unchanged at 17% of principal loaned.
    - o Limited information was made available to the Board by the payday lenders. While the Coalition's expert witness, using the very limited data available in the public domain, made a prima facie case that excess profits were being generated, the Board was unable to determine conclusively that profits were excessive. However, other

recommendations contained in this report may impact lender profitability. The Board has concluded that maintaining the 17% rate is justified.

- The borrowing limit remain at 30% of net pay.
- The 5% "cooling-off period" rate cap imposed in the regulations (where a payday loans borrower takes out another loan within seven days after the borrower has repaid in full another payday loan previously arranged by that payday lender) only apply for a one day period. After that one day period, the client would be able to take out another loan at the regular rate of 17%. The one day cooling off period would delineate the issuance of a replacement loan which is used to repay the initial loan and a completely new loan. The Board finds that the seven day "cooling-off period" is not preventing borrowers from getting into a debt trap spiral as consumers with access to another lender are simply going "across the street" to the other lender.
- At the request of a borrower, a lender be required to extend the loan for at least another pay period or to convert the loan to an installment loan, provided that the borrower has successfully paid off three previous payday loans during the preceding 12 month period. If an installment loan is issued the cap on the rate for the loan should be set at 7%. The installment loan repayment terms should allow repayment over at least the next four pay periods, where no payment exceeds 35% of the sum of the principal and cost of borrowing.
  - The Canadian Payday Loan Association has offered to develop an installment loan option for a borrower who has successfully paid off three or more previous loans. The Board believes that a mandatory installment

loan option or a loan extension option should be made available to payday loan consumers to assist them in paying back their loans in a manner which is manageable, potentially avoiding the start of a “debt spiral”.

- The Board recommends that the 5% rate cap on extension renewal and replacement loans, other than those included in the "cooling-off" regulation, remain unchanged.
- The Board recommends that lenders be prohibited from making more than 10 payday loans to a customer in a consecutive 12 month period. The Board has concluded that some lenders are making an excessive number of payday loans to individual customers such that these customers are stuck in a debt trap.

The Board believes that a balance must be struck between the financial viability of the payday loans industry and the need to protect consumers from falling into a debt trap or a debt spiral. The Board concludes that the payday loan industry remains financially viable in Manitoba for lenders at the 17% rate cap, provided that loan losses are minimized by a judicious loan approval process. A reduction in the rate cap may have an unduly negative effect on the viability of the industry. Keeping the borrowing limit of 30% of net pay also acts to reduce the risk of consumers overextending their credit. Providing the option of loan extensions and installment loans to consumers will assist them to overcome temporary problems in meeting their payment obligations. The Board recommends that payday lenders be allowed to recover the full cost charged by a financial institution for a dishonoured cheque or debit charge. The current cost limit of $20.00 should be removed.

The Board is very concerned about the risk of financial harm to Manitoba consumers from credit products offered by unlicensed and unregulated lenders. It is pleased that amendments to *The Consumer Protection Act* will take effect in September, 2016, which will serve, in some respects, to regulate high-cost credit products other than payday loans. The Board makes further recommendations in respect of measures to regulate high-cost credit products.

The Board also makes recommendations respecting online payday loans, possible new borrowing disclosure obligations, financial literacy, use of plain language in the preparation of information and documents, and suggested data collection provisions for receipt of more detailed information from lenders.

The Board acknowledges the contributions made by all participants in the review process. They assisted the Board in preparing its findings and its recommendations.

2.0 OVERVIEW

Pursuant to Sections 164(2) and 164.1(2) of *The Consumer Protection Act*, the Board was required to conduct this Review of specific aspects of amounts charged to consumers to obtain payday loans, and to make a report to the Minister responsible, within six months of commencing the review.

Man. Reg. 50/2010, the regulation setting the maximum cost of credit for a payday loan under the Act, came into force on October 18, 2010. Pursuant to section 164(2) of the Act, the Board was required to conduct a review on the issues as above, within three years after Man. Reg. 50/2010 came into force. The Board submitted that report to the Government on September 23, 2013. This Review is conducted further to the report of September 23, 2013, as contemplated by section 164.1(2) of the Act, whereby every third year, the Minister must review the effectiveness of Part XVIII of the Act, which addresses payday loans, and the regulations under the same Part and decide:

a) Whether to require a further review by the Board in accordance with section 164 of the Act; and

b) Whether to recommend changes to the payday loans provisions of the Act or the regulations under Part XVIII.

By his letter received June 30, 2015, the Minister responsible asked the Board to review, no later than 2016, the maximum payday loan limits. The Board was also specifically asked to analyze the impacts of reducing the maximum allowable rate that may be charged for a payday loan, from $17 per $100 borrowed to $15 per $100 borrowed and the impacts of reducing the proportion of a borrower's net pay, which is used to determine the maximum loan amount, from 30% to 25%.

In the review process, there was no applicant, and therefore, no onus of proof on any of the participants. The Board is required to make recommendations to the Minister and is not hereby fixing the cost of credit or any of the related aspects of fees chargeable for payday loans. The Board may make recommendations about the regulation of payday lenders or payday loans in addition to the mandatory requirements to be addressed in its report.

A Notice of Public Hearing was issued with respect to this review both in Winnipeg publications and in a variety of provincial publications on January 9, 2016. Under Board Order 30/16, Intervener status was granted to three Interveners: a joint intervention of The Consumers' Association of Canada (Manitoba) Inc., Winnipeg Harvest and Community Financial Counseling Services (CAC), The Canadian Payday Loan Association (CPLA), and C11 A1 Financing & Loans (C11).

In accordance with the procedural timetable, pre-filed written evidence was received from all Interveners. Information Requests, which are questions to obtain further information, were posed to all of Interveners by the Board. Some Interveners posed questions to each other. All responses of the Interveners were filed with the Board and were and included in the record of proceedings. The Board also sourced certain statistical, consumer and industry information and distributed the information to all Interveners.

The public hearings took place over five days, which included presentations from members of the public and the payday lending industry and oral evidence called by CAC, and closing submissions given by two of the three Interveners.

CAC and CPLA, at the conclusion of the hearings, provided the Board with a number of recommendations, many of which have been accepted by the Board. A summary of those recommendations made by CAC and CPLA are found at Schedule "A" to this Report.

At the public hearings, the Board received presentations from certain presenters who appeared in person. They were: Ron Shemley, a member of the public; industry members Janet Davis, Manager of The Money Tree, and Melissa Soper, the Senior Vice President of Public Affairs for Cash Money; and from Anna Ellison, Research Director with Policis, a think tank based in London, England, whose presence was funded by CPLA.

In addition to the presentations at the hearing, the Board received written presentations and correspondence, all of which were provided to the Interveners and which were entered into the record at the public hearings. The Board received a written presentation from Supporting Employment & Economic Development (SEED) Winnipeg Inc., and letters from staff and customers of payday lenders. The Board also received a letter from National Money Mart Company (Money Mart), which enclosed a report from Deloitte LLP entitled "Summary of the 2015 Survey on the Cost of Providing Payday Loans in Alberta." That same report was included in CPLA's pre-filed written evidence.

During the public hearings, Cash Money offered to provide the Board with financial information regarding its Manitoba operations, on a confidential basis. No objections were made by the Interveners to the Board's receipt of this information. The Board accepted the offer made by Cash Money, and Cash Money provided the information to the Board following the conclusion of the public hearings.

The Board has posted all of the hearing exhibits on its website. The transcripts of the public hearing are also available on the website. This Report has been provided to all Interveners and has been posted to the Board's website.

2.1 INTERVENER EVIDENCE AND SUBMISSIONS

2.1.0 THE CONSUMERS' COALITION (CAC)

The Consumers' Coalition ("CAC") is a coalition of three organizations including the Consumers' Association of Canada (Manitoba Branch), Community Financial Counselling Services and Winnipeg Harvest.

The Consumers' Association of Canada (Manitoba Branch) has over 400 members and donors. It is a non-profit, community-based organization which interacts with approximately 14,000 customers annually. It provides information sessions and workshops which serve approximately 6000 Manitoba consumers annually.

Community Financial Counselling Services (CFCS) is a non-profit agency that provides credit counselling to individuals free of charge. CFCS also delivers education and financial literacy programs, seminars and workshops to community groups, the general public and other organizations. CFCS advocates on behalf of Manitobans for fair practices in lending, debt repayment and financial services.

Winnipeg Harvest is a non-profit, community-based organization committed to providing food to people who struggle to feed themselves and their families. It partners with more than 340 agencies to distribute food to Manitoba families.

CAC explained that it approached this hearing from what it described as three "central realities." First, access to credit is a critically important product in today's society. Second, the population taking out payday loans is disproportionately comprised of vulnerable consumers, tending to be of lower income and wealth. Third, the issues of consumer access, consumer protection and industry sustainability need to be balanced.

CAC filed pre-filed written evidence, which was comprised of original research in the form of expert reports and research studies, including:

1. A literature review prepared by Jerry Buckland, PhD, entitled *Payday Lending: a Mature Industry with Chronic Challenges*, which examined the literature on and related to payday lending, including the dynamics of the industry and the impact of payday loans and payday loan regulation on consumers;

2. An economic analysis prepared by Chris Robinson, PhD, CFP, CPA, CA, entitled *An Economic Analysis of the Payday Loan Industry and Recommendation for Regulation in Manitoba*, in which Dr. Robinson conducted an examination of the profitability of payday lenders;

3. Two papers prepared by Wayne Simpson, PhD, and Khan Islam, PhD candidate, examining the profile of payday loan borrowers in Canada: *A Profile of Payday Loans Consumers Based on the 2014 Canadian Financial Capability Survey*; and *Payday Loans Consumer Profile Based on the Survey of Financial Security*;

4. A research study prepared by Zoe St. Aubin, MA, DBA, *Manitoba Consumers' Experiences with Payday Loans Research Study*, which reviewed the findings of

research conducted into payday loans consumers via surveys, semi-structured interviews, and a focus group;

5. A report on a focus group prepared by Dr. Buckland, Evan Sinclair, and Jessica Piec*, Comparing Payday Loans and Two Alternative Small Loan Products*, which reported on the results from a focus group in which the payday loan product currently available in Manitoba was compared with two other small loan products found elsewhere;

6. A report on research conducted by Evan Sinclair under the supervision of Dr. Buckland, *Manitoba Consumers' Experiences with Payday Loans: Pricing and Practices of Licensed Payday Lenders in Manitoba*, which reported on information obtained regarding practices of payday lenders in Manitoba, gathered via in-person interviews, structured telephone interviews and online data analysis;

7. Historical data and maps of payday lending outlets in Winnipeg, gathered by the experts retained by CAC; and

8. A report on a workshop, prepared by Dr. Buckland, Evan Sinclair and Kate Martin, entitled *Small Loan Workshop: Summary of Proceedings and Recommendations*, which contained a summary of a discussion that took place with mainstream financial institution representatives and experts involved in studying the financial sector, regarding small loans;

CAC also provided the *curriculum vitae* of the experts. Dr. Buckland, Dr. Robinson, Dr. Simpson, and Ms. St. Aubin appeared before the Board. There were no objections raised by the other Interveners regarding their qualifications and areas of expertise. They were qualified by the Board as requested by CAC.

- Dr. Buckland was qualified as an expert in economics, including qualitative and quantitative research methodology with a particular specialization in microfinance, micro community development, economic development, and interdisciplinary development theory;
- Dr. Robinson was qualified as an expert in financial statement analysis and personal finance, corporate finance, and survey research;
- Dr. Simpson was qualified as an expert in applied microeconomics, quantitative methods as applied to social policy; and
- Ms. St. Aubin was qualified as an expert in mixed methods research, including surveys, interviews, focus groups and data analysis.

CAC's expert team provided expertise in econometrics, sociology and qualitative research methods. As stated in the pre-filed evidence provided by CAC, the purpose of the research conducted was to attempt to better understand the payday lending industry, the payday loan product, and its impact on consumers. The research focused on the question of whether the current rate caps and maximum loan amounts are working for the public good.

The CAC experts' research findings were summarized in the pre-filed evidence. There is a limit on the data available regarding both payday loans consumers and lenders, and there is a need for further research on the payday loan industry and the experiences of consumers. The CAC experts concluded that:

- A fee of $15 per $100 borrowed is appropriate;
- Repeat borrowing is harming vulnerable consumers; and regulation is needed to address this issue.

One of the main recommendations made by CAC was that payday lenders should offer repayment by installment, in order to address the problem of repeat borrowing.

CAC did not recommend reducing the maximum loan amount to 25% of the borrower's net pay as it would not alleviate the borrower's "debt trap" problem. Dr. Robinson recommended that an installment option be provided to borrowers, and submitted information about the models that have been used in the States of Colorado and Washington

Based on their research conducted, CAC experts concluded that payday loans consumers are likely to use payday loans to cover necessary expenses. Upon repayment of the payday loan, they are required to take out further loans to cover their basic expenses.

The consumers understand that payday loans are high-fee loans but may not understand the cost of the loans on an annualized percentage rate (APR) basis.

Ms. St. Aubin discussed her research study regarding Manitoba consumers and their experiences with payday loans. The research study aimed to provide an understanding of the factors that influence or play a role in payday loan consumers borrowing practices.

In addition to the evidence provided by the CAC expert panel, the Board heard from consumers of payday loans, called on behalf of CAC. Three consumer witnesses testified in a panel format and provided evidence to the Board regarding their personal experiences with payday loans. A summary of their evidence is provided later in this Report.

2.1.1 THE CANADIAN PAYDAY LOAN ASSOCIATION

The Canadian Payday Loan Association ("CPLA") was formed in 2004, and has 19 member companies holding lending licenses for approximately 940 storefront and online payday lenders, representing approximately 67% of the industry in Canada. In Manitoba, there are six CPLA members holding 30 licenses in total through storefronts or online. The CPLA describes its goal as advocating for the right balance between adequate consumer protection and an economically viable industry for its members.

The CPLA provided the Board with pre-filed written evidence, in which CPLA set out its position on the matters to be considered by the Board, and included the following reports:

1. A research study conducted by Environics: *Payday Loan Users Study, Manitoba*, which was previously filed with the Board and considered by the Board in the 2013 payday loans review;

2. A report prepared by the Consumers Council of Canada, *Consumer Experiences in Online Payday Loans*, regarding a study that was conducted regarding the online payday loans environment for Canadian consumers, and particularly, how compliant the online lenders were with the relevant provincial regulations;

3. A report prepared by Deloitte LLP, entitled *Summary of the 2015 Survey on the Cost of Providing Payday Loans in Alberta*, which was based on data collected regarding financial and other relevant information about Alberta payday lenders via a detailed survey, and in which Deloitte LLP provided information regarding the costs of providing payday loans on the basis of those data;

4. Results of a three-member survey prepared by Grant Thornton LLP, in which Grant Thornton LLP collected payday loan data from three CPLA members and determined: the weighted average proportion of loans that were advanced for less than 100% of the amount for which the consumer was eligible to borrow; and the weighted average percentage of the eligible amount borrowed by those customers who chose to borrow less than the eligible amount.

CPLA did not call any witnesses in the public hearings and conducted limited cross-examination of the CAC expert witness panel.

It was CPLA's submission that Manitobans need small, short-term credit products, which are not provided by mainstream financial institutions. If Manitoba consumers do not have access to payday loans from licensed lenders, they will seek out credit from unregulated lenders that is of higher cost and will be subjected to abusive collection practices. CPLA was of the view that reducing the maximum allowable rate, or reducing the maximum amount that a consumer may borrow would directly impact the profitability of lenders, and would lead to store closures, driving borrowers to unlicensed lenders.

According to the CPLA, it is important to correctly regulate and set maximum rates. If regulations are too harsh, licensed lenders leave the market.

As part of its pre-filed evidence, CPLA provided a sample of the web pages of unlicensed lenders offering payday loans in Manitoba that were identified in a March 2016 website scan. CPLA periodically conducts such scans. It has found that the web pages are constantly changing.

The report on online payday lending prepared by the Consumers Council of Canada in 2015 (the "CCC Report"), which was included as part of CPLA's pre-filed evidence, found that licensed online payday lenders in Canada showed a high level of compliance with regulation, but unlicensed lenders showed virtually no compliance.

CPLA indicated that, due to limited resources, it did not undertake any new research for the Board's Review, but based on its filings and the evidence from the CAC witnesses; there is a need for payday loans.

CPLA's position was that the maximum allowable rate should not be reduced to below $17 per $100 borrowed. If that were to occur, CPLA suggested that would result in store closures, job losses, and restricted access to credit for certain consumers who rely on the product.

With respect to a reduction of the proportion of a borrower's net pay used to calculate the maximum loan amount, CPLA took the position that any reduction would be of no benefit to consumers. Further reducing the maximum loan amount, in CPLA's submission, would force consumers to seek credit from more than one lender at a given period of time.

CPLA also provided the Board with information as to the payday lender data collection measures employed in British Columbia, Ontario, and Nova Scotia.

Finally, CPLA made various other recommendations to the Board, including the lender’s optional offering of an extension loan to certain qualified clients.

2.1.2 C11 A1 FINANCING & LOANS

C11 A1 Financing & Loans ("C11") is a payday lending business operating in Thompson, Manitoba. C11 filed written, pre-filed evidence with the Board but did not call any witnesses in the public hearings.

As part of its pre-filed evidence, C11 made the observation that, in recent years, there has been an increase in services offered by online and unlicensed lenders. Given that the maximum loan amount is set at 30% of a borrower's net pay, consumers will seek out an online lender to borrow an amount that will meet their financial needs.

According to C11, the cap set on replacement or extension loans in the regulations at 5% of the principal amount on a new loan made within the 7 day cooling off period, is financially impossible from a lender's perspective because of the risk of such loans; as a result, borrowers must use unlicensed on-line lenders. Its position was that reducing the maximum amount of a loan at 25% of the borrower's net pay would serve to push more consumers to unlicensed and online lenders and that reducing the amount to be charged to $15 per $100 borrowed would have little effect for the consumer but would further erode the financial stability of licensed lenders. C11 recommended that, if the maximum rate were to be reduced from $17 per $100 borrowed to $15 per $100 borrowed, then the Board ought to consider recommending an increase on the rate for replacement and extension loans, above 5%.

2.1.3 CONSUMER PANEL EVIDENCE

The CAC Consumer Panel provided evidence regarding their personal experiences with payday loans.

The first panel member, Milagros Daraman, has been retired for approximately seven years, and her source of income is old age pension benefits. She stated that she uses payday loans on occasion, when she needs extra funds for pleasure or entertainment. She also sends money to family in the Philippines. She has only ever had one open payday loan at a time, and borrows approximately $160 per loan. She has never used internet payday loans. She estimates that she takes out four to five payday loans in a one-year period.

The second panel member, Deena Wichert, testified that she uses payday loans for personal expenses. She has been using payday loans for approximately five years, and uses them approximately once per month, with the exception of a period where she was on maternity leave and reduced her use of payday loans somewhat. She has had more than one open payday loan at a time. Ms. Wichert stated: "…once you're in it's hard to get out."

With respect to internet lenders, Ms. Wichert described one occasion where she had two loans in one period, and needed a further loan to assist with repaying one of the loans. She attended a storefront payday lender who suggested that she use a computer located in the storefront office. Ms. Wichert recalled that the loan she obtained using the computer was from a lender in Alberta. While Ms. Wichert said that she does not have difficulty repaying the loans, she finds that, upon repayment, she needs to take out a further payday loan to meet her obligations.

Lastly, the Board heard from Brandy Getty. Ms. Getty testified that she had obtained four payday loans in total, from two lenders. The last time that she took out a payday loan was approximately one and one half years ago. She used payday loans both during a period when she was employed, and when she was on social assistance. Ms. Getty was experiencing issues with substance abuse at the time. The loans were taken out to support her habit. Ms. Getty was not in a position to repay all of the loans that she took out, which has had implications for her credit report and for which she is being contacted for collection. Ms. Getty said that she would never use payday loans again, and that, if she found herself in a situation where she required funds, she would exhaust other options such as accessing savings or borrowing from a friend. Ms. Getty has since taken financial training with a social agency and is now saving money.

2.1.4 PRESENTATIONS

Four Presenters made oral presentations to the Board on April 12, 2016. Presenters are not sworn witnesses and were not cross-examined, although they can provide answers to questions posed by the Board.

2.1.4.0 ANNA ELLISON, POLICIS

Anna Ellison presented on behalf of Policis, which she described as a London-based think tank, focused on evidence-based policy-making. Ms. Ellison advised that her presence at the public hearings had been funded by CPLA. Policis conducted some research into the provision of financial services to those on low incomes and disadvantaged consumers. Her presentation outlined Policis' examination of consumer outcomes from different approaches for small-dollar lending regulation. Policis' research was based on information from the largest credit reference database for "non-prime" lending in the United States, looking at all of the installment and payday loans between 2010 and 2014. Policis also conducted interviews of over 20 of the U.S. State regulators.

Ms. Ellison stated that the Policis research indicated that demand for payday loans does not go away when regulations drive licensed lenders out of the market. The experience in the U.S. indicates that an unlicensed credit market can emerge and reach a large scale over a relatively short period when regulations are too restrictive. Where restrictions cause suppliers to withdraw from the market because lending becomes unprofitable, the research indicates that some of the demand for the payday loan product falls away. This is the demand stimulated by the advertising and marketing activity of lenders and brokers. However, the underlying consumer demand for the product remains. In U.S. States where the legitimate supply is more restricted, the demand shifted to the online market, where a high proportion of unlicensed lenders operate. The Policis research showed that by 2016, 59% of all online small sum high-cost loans were made by unlicensed lenders, and of the small sum high cost loans, 41% were made by offshore lenders, located outside of the U.S.

According to Policis, a U.S. concern involves the proliferation of unlicensed lenders. Unlicensed lenders tend not to comply with the regulations of the jurisdictions in which they offer loans, whereas licensed lenders are much more likely to be compliant.

U.S. States with what were described as permissive regulatory approaches tend to have a higher proportion of licensed lenders. In more restrictive U.S. states or states where payday loans are effectively banned, few loans are complying with the regulatory provisions on costs, due to the penetration of unlicensed lenders into the market.

Ms. Ellison's presentation highlighted some key research conclusions. Demand for payday loans does not go away when the supply is restricted, but rather appears to be displaced from the storefront to online, and the online market creates an opportunity for unlicensed and unregulated lenders. The most positive outcomes for consumers are achieved with a simple, focused regulatory framework that allows lenders to operate profitably. According to Ms. Ellison, Manitoba consumers would appear to better protect not by further borrowing restrictions but instead by creating an environment that allows compliant lenders an opportunity to be viable.

2.1.4.1 JANET DAVIS, THE MONEY TREE PAYDAY LOANS

Janet Davis is the manager of The Money Tree. She provided her perspective on the potential effect of decreasing the maximum allowable rate and the maximum loan amount. In her view, reducing the rates would have the effect of closing doors for many payday lenders. If that were the case, this would be unfair to consumers because they would be pushed to use the services of online and unlicensed lenders. While she does not view the maximum allowable rate of $17 per $100 borrowed necessarily fair from the lender's perspective, she did concede that it would be fair from the borrower's perspective.

With respect to the licensing fee and the fee paid by lenders into the Financial Literacy fund, Ms. Davis suggested that some of those funds could be spent on polling the existing payday loans consumers regarding their views on the regulations, and in particular, the "cooling-off" period and the maximum allowable rate. With respect to the "cooling-off" period, she stated that it may be detrimental to consumers because it can result in their not being able to meet their obligations and being subject to costly NSF charges from their banks.

Ms. Davis expressed that payday loans can be of real value to individuals who run into situations where they require funds, but they cannot use the services of traditional financial institutions. Further, many of the consumers using the services of The Money Tree are professionals such as teachers, nurses, and upper management of their own stores.

She also explained that it is difficult for lenders to explain to a borrower that the amount they can borrow is limited, particularly where the borrower has a specific need which is greater than the maximum loan limit. The Money Tree tries to coach its customers to borrow only the amount needed, and not the amount that they want. But in the case where the customer needs more than the maximum amount permitted under the regulations, that customer will simply go to another lender to obtain a second loan.

If the maximum allowable rate were to be further decreased, Ms. Davis estimated that The Money Tree would see a decrease in revenue in the amount of $43,000.00, and decreasing the maximum loan amount would lead to a potential loss of revenue in the amount of $70,000.00.

Lastly, Ms. Davis said that the regulations can be difficult for the lender to understand, it might help if they could be set out in more easily understandable terms.

2.1.4.2 MELISSA SOPER, CASH MONEY

Ms. Soper is the head of Public Affairs for Cash Money, a payday lender operating in Manitoba. It has four locations in Manitoba and 185 across Canada. According to her submission, a payday loans is the only viable small dollar credit option for consumers with credit scores lower than 649.

Ms. Soper explained that, in Manitoba, the $17 per $100 borrowed fee enables the lender to cover rent, payroll, operating expenses, cost of capital, and earn a reasonable profit. In Manitoba, Cash Money's profit represents only one percent of revenues. A reduction in the rate from $17 to $15 per $100 borrowed would represent an almost 12% reduction in revenue, and the Manitoba stores would not generate a profit.

Ms. Soper stated that Cash Money has deliberated about whether to keep its Manitoba operations open. It has decided to keep them open for now as part of its national brand strategy, despite what she described as negligible returns. In 2013, Cash Money operated five stores in Manitoba. Cash Money closed one store when the lease came up for renewal, and of the remaining four stores, leases are being renewed on a month-to-month basis in order to allow Cash Money to re-evaluate its ability to continue operations.

2.1.4.3 RON SHEMLEY

Ron Shemley, member of the public and a payday loans consumer, made a presentation to the Board. He expressed frustration with a particular payday lender. A pensioner, he requires three payday loans in a given month to meet his financial obligations. He takes out payday loans from three lenders because the maximum loan amount that he is able to obtain from one lender is not sufficient for him to meet those obligations. He had learned that Money Mart was beginning to offer an installment loan, which might serve to stop him from needing further payday loans in the future. Mr. Shemley also voiced his support for the regulations on the interest rate on payday loans in Manitoba.

2.1.4.4 WRITTEN PRESENTATIONS

The Board received a number of written presentations, which were entered on the record at the public hearings. Among them were letters from payday loans consumers and staff, from the industry, and from SEED Winnipeg Inc., a community-based organization.

The Board received a number of letters of support from payday loans customers and staff of Cash Money and Money Mart. Customers expressed their support for payday loans and the good service received from payday lenders. Consumers explained that they took out payday loans to meet financial obligations and to purchase food or pay bills, to pay unexpected expenses and for emergencies. Cash Money staff stated that they are providing a necessary service to customers and assisting them in difficult circumstances.

In its written submission, Money Mart provided various criticism of Dr. Robinson's report.

Money Mart stated that a reduction in the maximum allowable rate would force the consolidation of stores in Manitoba. Access to credit would be restricted and consumers would be driven to unlicensed lenders. Money Mart also stated that the maximum amount borrowed ought not to be reduced from the current 30% of a borrower's net pay.

SEED Winnipeg Inc., (SEED) in its written submission, brought its perspective as a non-profit charitable organization working to reduce poverty and supporting community renewal, by assisting low-income individuals, groups, and neighbourhoods. SEED works with partners in Manitoba to deliver programs in areas such as financial literacy and access to financial services.

SEED stated that it has witnessed negative impacts associated with the business practices of payday lenders, including consumers foregoing necessities in order to make loan payments, becoming trapped in a cycle of debt, the negative impacts on credit history, and the repeated NSF or overdraft charges caused by payday loans. SEED recommended that the maximum allowable rate be reduced from $17 to $15 per $100 borrowed, and that the maximum loan amount be reduced from 30% to 25% of net pay. In addition, SEED made a number of other recommendations to the Board which were aimed at allowing alternatives to payday loans, regulating payday loan-like products, investment in financial literacy initiatives and supports through community organizations with a view to assisting individuals with building savings and accessing government entitlements and benefits.

3.0 BOARD FINDINGS

In this Review, the Board was tasked with examining two specific issues:

1. To analyze the impacts of reducing the maximum allowable rate that may be charged for a payday loan from $17 per $100 borrowed, to $15 per $100 borrowed; and

2. To analyze the impacts of reducing a borrower's net pay, which is used to determine the maximum loan amount, from 30% to 25%.

In addition to those specific issues, a number of other issues emerged in this Review, about which the Board received valuable evidence and submissions from Interveners and other stakeholders in the industry. The other issues and areas that were examined by the Board in this Review by way of pre-filed evidence or in the oral hearings were, among others:

1. The current regulatory climate and state of the payday lending industry, including data challenges associated with studying the payday lending industry;

2. The demographics of payday loans consumers and any changes to those demographics or trends since the last review;

3. The rate charged for extension and replacement loans;

4. Repeat borrowing and its impact on consumers and the industry;

5. The development of alternatives to payday loans and their possible effect on the industry and consumers;

6. Internet and unlicensed payday lending and its effect on the industry and consumers; and

7. A number of other issues including financial literacy, licensing fees paid by lenders, areas of research that might benefit the industry and consumers, and regulation of high-cost credit products.

All of these issues are discussed below.

3.1.0 REGULATORY PROVISIONS

Pursuant to definitions under Part XVIII of the Act, a “payday loan” means:

> “An advance of money in exchange for a post-dated cheque, a pre-authorized debit or a future payment of a similar nature, but not for any guarantee, suretyship, overdraft protection or security on property and not through a margin loan, pawn broking, a line of credit or a credit card."

The *Consumer Protection Act* provisions apply to a payday loan if the amount initially advanced under the loan is no more than $1,500.00 and its initial term, ignoring any extension or renewal, is no longer than 62 days; or it is a replacement loan, such that the payday loan is part of a series of transactions that results in the borrowers debt under another payday loan by that payday lender being repaid in whole or in part.

The Payday Loans Regulations apply to loans meeting the definition under Part XVII of the Act. The Regulations set the maximum rate on payday loans, the maximum loan amount, the rates on replacement or extension loans, among many other matters. A chart of the main regulatory provisions reviewed by the Board is included in Schedule “A” to this Report.

In addition to the current regulatory framework, Bill 34, *The Consumer Protection Amendment Act (High-Cost Credit Products)*, which amends *The Consumer Protection Act* to impose regulations on high-cost credit products which are not payday loans, is to come into force on September 1, 2016. Under the amendments, only a licensed high-cost credit grantor may offer, arrange or provide a high-cost credit product. The amendments also require that high-cost credit grantors post signage indicating that the product is high-cost, disclose key information to the consumer prior to entering into the transaction, not charge a fee or penalty for early repayment, and maintain records of high-cost credit products and agreements. High-cost credit grantors are also required to pay into the Financial Literacy Fund. The amendments do not, however, regulate the maximum fees or rates that high-cost credit grantors may charge.

3.1.1 REGULATION ACROSS CANADA

There are currently seven Canadian jurisdictions (British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, Nova Scotia and Prince Edward Island) that regulate payday loans. In addition, in New Brunswick, the *Cost of Credit Disclosure Act*, SNB, c. C-28-3 has been renamed the *Cost of Credit Disclosure Act and Payday Loans Act* by *An Act Respecting Payday Loans*, SNB 2008, c. 3, which is still not in force. The Act is awaiting proclamation and imposes standards of practice and enhanced disclosure requirements for licensed payday lenders.

Of the provinces referred to above, the key provisions are as follows:

Province	Price Cap	APR Disclosure	Borrowing Limit	Cancellation Period	Maximum NSF Fee	Post default interest rate
BC	23	Yes	50% of net pay	Next business day	$20	30%
Alberta	23	Yes	$1500	2 business days	$25	2.5% per month
Sask.	23	No	50% of net pay	Next business day	$50	30%
Manitoba	17	Yes	30% of net pay	48 hours	$20	2.5% per month
Ontario	21	No	$1500	2 business days	"reasonable charges"	N/A
New Brunswick	Pending	N/A	Pending	48 hours	$40	Pending
Nova Scotia	25	Yes	$1500	Next business day	$40	60%
PEI	25	No	$1500	2 business days	"reasonable charges"	Pending

3.1.2 PAYDAY LOAN INDUSTRY

The Manitoba Consumer Protection Office (CPO) reported to the Board that in March 2016, there were 43 licensed payday outlets operating in Manitoba. This was the same number of outlets as was reported to the Board in the 2013 Review. The Board noted in the 2013 Review that as of October 18, 2012, Cash Store Financial Services Inc. had voluntarily given up all of its payday loan licenses in Manitoba. It stopped offering payday loans in this province through its Cash Store and Instaloan outlets. In this Review, the CPO indicated to the Board that on April 14, 2014, The Cash Store Financial Services Inc. (CSF) obtained an initial order under the *Companies' Creditors Arrangement Act* (CCAA). CSF was granted a stay of proceedings and other relief under the CCAA. The stay of proceedings was granted to May 20, 2016.

On February 6, 2015, CSF announced that it had completed the sale of 150 branches across Canada operated by CSF and its subsidiaries, including six locations in Manitoba, to National Money Mart Company.

CPLA provided some data on changes in number of payday outlets in Manitoba between 2007 and 2016. In CPLA's outlet survey of January, 2007, there were 71 outlets offering payday loans in Manitoba. CPLA's information is that there are currently 40 licensed outlets, and three internet payday lenders in Manitoba.

Dr. Robinson provided data on payday lenders in Manitoba for three periods of time: 2008, 2010, and February 28, 2016. His data show that in 2008, there were 73 stores in Manitoba. That number increased to 76 in 2010, and as of February 28, 2016, the total number was 40.

According to Dr. Buckland, payday lending is now a mature industry. Critics claim that payday lenders harm their customers through their location strategies, high fees, and repeat loans. According to Dr. Buckland, the industry has undergone a corporatization; in previous years, smaller, individually-owned outlets held the larger market share. The industry's corporate players are taking advantage of economies of scale and are able to operate across many outlets. In addition, they take advantage of economies of scope; they offer other products in addition to payday loans.

The Board notes that, in the research project prepared for CAC, *Manitoba Consumers' Experiences with Payday Loans: Pricing and Practices of Licensed Payday Lenders in Manitoba*, the conclusion was that payday loans are widely accessible across Manitoba, in urban and suburban neighbourhoods of varying socio-economic backgrounds.

The CPO numbers record 43 licensed outlets in 2016. In the 2013 Review, the Board recognized that the number of licensed outlets had dropped since regulation, and it remained uncertain whether the number of customers remained the same given the reduced number of outlets, or if the volume of loans or the profit margin changed with the reduction.

The Board does not have specific Manitoba financial data from the CPLA membership; however, given the apparent stability of the payday lending industry as evidenced by the static number of payday lending outlets since the 2013 review, the Board concludes that the payday lender outlets remain open in Manitoba because they are profitable in the current regulatory environment.

3.1.2.0 DATA CHALLENGES

The Regulations do not require Manitoba lenders to report to the CPO on matters such as loan volume, number of borrowers, data on repeat borrowers, or average loan amount.

The Board concludes that there is a lack of Manitoba data to assist in analysis and decision making. CPLA provided the Board with a chart outlining the standard regulatory reporting requirements in BC, Nova Scotia and Ontario. BC and Ontario have the most robust reporting requirements and both provinces require reporting on such matters as: the number of loans made; the total cost of credit charged for all loans; the amount of the loans made by amount of principal; and the number and amount of loans defaulted on. Both Nova Scotia and Ontario require reporting on the number of repeat loans issued and number of individual borrowers who obtained repeat loans.

While the Interveners and Presenters provided useful evidence and information to the Board in this Review, many Review participants commented on the lack of data. Further research and data are required regarding payday lenders and consumers for future reviews by the Board or Government. The Board and Government would be well-served by further, and more extensive, industry-wide, and consumer-based research. The CPLA is supportive of an initiative that would enable data collection in Manitoba but suggested that, in determining the information to collect, the payday lending industry should be consulted.

The Board therefore recommends that research be undertaken by Government to assess the economic and social consequences of payday loans on individuals and communities, in order to inform future payday loan reviews. Such research should focus on issues such as repeat borrowing, internet borrowing, and the potential of new communications technologies for mainstream financial institutions to provide alternatives to payday loans. A review of best practices in other jurisdictions, related to payday loans, should also be undertaken.

The Board recommends that the Manitoba Government consult and negotiate future reporting requirements with payday lenders and industry leaders. This would determine the most meaningful and cost efficient data for confidential filing by lenders so as to allow for more effective future regulation. The Board recommends that the data reported in BC, Nova Scotia and Ontario, as listed above, be reported in Manitoba.

3.1.3 NATURE OF PAYDAY LOANS

The Board was provided with considerable information regarding the needs of customers who borrow from payday lenders. This information came from the CAC Research Study conducted by Ms. St. Aubin, from the CAC consumer panel, and from 2013 Environics Research Study which was filed by CPLA.

In Ms. St. Aubin's Research Study, a sample of 104 survey respondents stated that payday loans were used to:

- Pay for living costs (rent, food, utilities, or clothing): 48.1%
- Only for emergencies: 44.2%
- Pay other loans (credit card, line of credit, car payment): 4.8%
- Pay outstanding payday loans: 2.9%

As the Board noted in the 2013 review, CPLA's 2013 Environics Survey identified reasons why payday loans customers borrowed cash from lenders. The category options were scripted by the survey firm and results reported by Environics. The majority of respondents (58%) stated that they used payday loans for emergency cash to pay for necessities. 30% stated that they used payday loans to assist with an unexpected expense. Others stated that they used payday loans to avoid late charges on routine bills, to assist with a temporary reduction in income, to buy something they wanted, and to avoid bouncing cheques.

In its 2013 review, the Board noted that 58% of Environics Survey respondents were accessing cash to pay for necessities. The only clear category of need not in the control of the customer was "to help get through a temporary reduction in income" at a reported 17%. The Environics Survey cited "quick and easy" as the number one reason for choosing a payday loan; the Board found this research finding difficult to reconcile with the fact that, in the Board's estimation, it is usually easier and quicker to access funds via a line of credit or a credit card advance, assuming the credit limit is not breached by the borrowing need.

The anecdotal evidence from the CAC consumer panel showed that one of the three consumers was using payday loans for living costs. It seems that a significant proportion of payday loans consumers are using those loans to cover basic living expenses, rather than using them occasionally for emergencies, as the product appears to be marketed.

The Board accepts, as it has previously, that market and consumer factors have created and continue to create a need for small sum unsecured short term loans. The Board accepts that payday lenders are currently satisfying a need in the absence of other small short term loan options. It also appears that, in many cases, payday loan consumers want the product and like the service.

3.1.4 CONSUMER DEMOGRAPHICS

According to CAC's experts, certain identifiable variables are statistically significant when comparing payday loan borrowers to non-borrowers.

Dr. Simpson and Khan Islam analyzed the 2014 Canadian Survey of Financial Capability ("CFCS") and the 2012 Survey of Financial Security ("SFS"). Their quantitative analysis compared the more recent survey data against previous survey data to observe any trends and new developments in the area of payday lending. However, the CFCS and the SFS did not probe into payday lending in the fashion that other studies have in the U.S.

According to their analysis research, the typical consumer of payday loans is likely to be low-income and low wealth, although there are increasing numbers of middle-income consumers. The number of consumers borrowing against non-employment sources of income such as pensions has also increased. Nationally, and in Manitoba, Aboriginal people are over-represented among borrowers.

The 2014 CFCS asked respondents whether they, and other household members, had taken out a payday loan in the previous 12 months. The reported use rate of payday loans in response to this question was 4.2%. With respect to the 2012 SFS, the question asked was whether in the past three years, anyone in the family had borrowed money through a payday loan. In the 2012 SFS, the report showed a use rate of 2.8%. The limitation of the SFS results is that the Manitoba sample is small, involving only 33 payday borrowers.

A regression analysis allowed Dr. Simpson to assess various factors that might influence payday loan borrowing and the extent of borrowing, as well as the frequency of borrowing. The survey data from the CFCS, which is from across Canada indicates that the group with a household income of $32,000.00 to $54,000.00 and $55,000.00 to $80,000.00 are the groups that predominantly use payday lending. This indicates that payday borrowing tends to come from lower income households, not necessarily the poorest households.

The results of the SFS analysis show that the income gap between users of payday loans and non-users is only 12% in Manitoba, and is 42% in the rest of Canada. Dr. Simpson explained that that would be primarily due to the lower mean incomes of the non-borrower sample in Manitoba.

The results also show that most people in the payday loan sample do not own a home. Approximately 30% of borrowers have a home or a mortgage as against 70% of the non-borrower sample. This is a consistent result throughout Canada, not just Manitoba. Most of the non-borrower sample, approximately 88%, of borrowers use credit cards. Approximately 61% of the Canadian borrower sample has access to credit cards; the Manitoba result is slightly lower at 51.5% suggesting that Manitoba borrowers may have more restricted access to credit cards which could impact the level of pay day borrowing.

Payday loan borrowers are less likely to have post-secondary education. They tend to be older, married, from larger families, and have responsibility for children. They are more likely to be Aboriginal and immigrant, although the proportion of Aboriginal borrowers has declined from 2009 to 2014 across Canada.

Dr. Simpson noted that the major sources of income of payday loan borrowers are different in the 2014 CFCS as compared to the 2009 CFCS. In particular, the proportion of borrowers relying on non-employment sources of income such as CPP, and social assistance are increasing. In addition, the number of repeat borrowers in those categories has increased.

According to Dr. Robinson, non-employment sources of income are more likely to be fixed and cannot be increased, as they could in the case of employment income, by having the borrower work more.

The Board is concerned with the levels of repeat borrowing in the non-employment group as evidenced by the results of the analysis conducted by Dr. Simpson and Mr. Islam, and the tendency of the non-employment borrowers to engage in repetitive borrowing practices.

CPLA and Presenters from the payday lending industry commented that borrowers come from many different fields of occupation, including professional backgrounds.

The Board finds that overall; payday loan borrowers are financially vulnerable. Borrowers tend to have insufficient savings, insufficient cash flow and, in many cases do not have access to other, lower-cost consumer credit options. They are less likely to own their homes, and less likely to have access to credit cards. Assets and wealth, rather than income, are associated with lower payday loan usage.

Dr. Simpson and Mr. Islam found that, accounting for all other factors, Manitobans tend to payday loans at a higher rate than other Canadians. Dr. Simpson was not able to provide any explanation for this phenomenon, and the Board makes no finding as to its cause.

The Board was pleased in this hearing to receive evidence from the consumer panel. This was a first for the Board, and allowed the Board to receive first-hand evidence from actual payday loans consumers. Although their evidence is anecdotal, it offered the Board valuable insight into real-life experiences with payday loans and the benefits and drawbacks of payday loans from consumers' perspectives. The Board is appreciative of the willingness of the consumers to come forward and assist the Board with this Review.

3.1.5 MAXIMUM ALLOWABLE RATE

Payday Loans Regulation 13.1 provides that "the total cost of credit for a payday loan must not be greater than 17% of the principal amount of the payday loan." Included within the "cost of credit" are all of the component costs for a payday loan.

In this Review, the Board was required to examine the potential impacts of reducing the maximum rate from 17% to 15%, and received evidence from all Interveners on this issue.

Dr. Robinson's evidence was that a rate cap of $15.00 per $100.00 borrowed would be a just and fair rate that would allow an efficient payday lender to continue to operate in Manitoba without earning excess profit. Dr. Robinson evidence was based on the analysis he completed using the financial model he developed, which allowed him to estimate the cost structure for an efficient payday lending outlet, including the cost of capital, for a single store that could be either a single operation or one outlet in a chain of stores. Dr. Robinson confirmed that he had used a similar model in his testimony for the 2007/2008 payday loan hearings before the Board. The current model has now been adapted to allow for a fixed fee structure rather than multiple rate caps based on the regulations, which have come into force since the 2007/2008 payday loan hearings.

Dr. Robinson opined that, due to the nature of the payday lending industry, competition has not served to reduce prices to a level that might reduce excess profit, or economic rents. The reason that competition does not seem to work in the payday lending industry, in Dr. Robinson's estimation, is because of what he refers to as the disadvantaged nature of the majority of borrowers, including that:

- Borrowers often do not understand the nature of the charges;
- Borrowers are typically unable to obtain credit from mainstream financial institutions which charge lower rates;

- Borrowers tend to belong to marginalized groups in society and may view mainstream financial institutions as discriminating against them; and

- Borrowers get into a payday borrowing cycle or a debt trap that they have difficulty escaping.

The inputs having the most significant impact on the results from Dr. Robinson's model are loan volume, the loan fee, operating costs and bad debt expenses. Costs of capital and capital expenditures are less influential on the outcome.

The figures used in Dr. Robinson's financial model were based on 2013/2014 numbers from the Form 10-K filing in the U.S. of Dollar Financial Group (DFG), the parent company of Money Mart, which Dr. Robinson described as the dominant firm in Canada. The DFG 10-K includes segmented financial information of Money Mart's Canadian operations. Dr. Robinson was of the view that DFG appears to be relying on a contribution margin from its Canadian operations that is double what its other segments earn, and is using the excessive profits in Canada to subsidize the rest of its operations.

Dr. Robinson used DFG 10-K information because no current data exist for Manitoba, or Canada as a whole, with respect to loan volume on a per store basis. The best available provincial data is from 2013/2014 with respect to store counts for each province and some additional data from the Provinces of British Columbia and Nova Scotia.

3.1.5.0 LOAN VOLUME

Per the DFG 10-K for the year ended June 30, 2013, DFG's loan volume in Canada was $922.9 Million and the count of company-operated stores was 479, for a loan volume per store of $1.927 Million.

Dr. Robinson also commented that in order to evaluate the performance in the industry of payday lenders at this time, the values from 2013 to 2014 must be adjusted to take into account the exit of Cash Store Financial from the Canadian market. Dr. Robinson estimated that Money Mart would have captured a substantial portion, if not all, of the volume of Cash Store Financial's loans following its exit from the market. Taking into account the figures from the DFG 10-K and the information regarding the exit of Cash Store Financial, Dr. Robinson utilized a store volume of $2.34 million which incorporates an estimation of how much added volume should be added as a result of the CSF closure. Dr. Robinson's calculation of the loan volume for Money Mart assumes a 2016 total of 574 stores for Money Mart instead of the 479 stores as at June 30, 2013. Assuming a volume estimate for Cash Store Financial of $600 million, and assuming that Money Mart captured 70% of that volume, this would translate into $1,342,900 of loan volume captured by Money Mart, for a total per store loan volume of $2.34 Million.

3.1.5.1 OPERATING COSTS

Dr. Robinson derived data from the DFG 10-K to calculate operating costs.

Dr. Robinson remarked on what he characterized as a "red flag" in the DFG 10-K, referring to corporate expenses of $109.4 Million, and other depreciation and amortization of $24.7M. Dr. Robinson commented, that based on his experience, he would not be able to find any reason for those large head office expenses. Therefore, he concluded that those expenses should not be used to calculate a just and fair rate. Dr. Robinson was of the view that operating costs of $12.01 per $100.00, which includes the allocation of head office cost, were likely too high; without any allocation of head office cost, the operating cost would be $9.53 per $100. Therefore he incorporated a value of $11.00 per $100.00 in his financial model. In addition, Dr. Robinson calculated the operating cost as $11.12 per $100.00, using the Cash Money financial information provided by Ms. Soper in the course of her presentation.

3.1.5.2 COST OF CAPITAL

Dr. Robinson calculated a weighted average cost of capital (WACC) of 7.9% as cost of capital; this was rounded up to 8% in this model. He assumed 10% interest rate to be a reasonable rate. He also used a 25% tax rate, adopted a 60/40 debt to equity ratio and a 2% inflation rate. The following table sets out the values he used to generate the model's financial results:

Component	**Estimate**	**Weight**	**Weighted Value**
Debt	[(1+.1(1-25))/1.02] = 5.4%	0.6	3.2%
Equity	(1.12/1.02) - 1 = 11.8%	.4	4.7
Weighted Average Cost of Capital			7.9%

Dr. Robinson testified that he took into consideration Manitoba's large and small corporate tax rates and different capital structure, to provide different WACC scenarios. By using 27% for the large corporation tax rate, and 11% for the small business tax rate, and changing the 60/40 capital structure to 15/85, the sensitivity range of WACC was from 6.2% to 11%. Dr. Robinson concluded that 14% of WACC used by the CPLA-filed Deloitte LLP Report was unreasonably high, possibly attributed to an over-evaluation of industry costs during the industry's expansion period.

3.1.5.3 BAD DEBT EXPENSE

Using the DFG 10-K figures, Dr. Robinson calculated the bad debt ratio by using the loss rate for a payday lender divided by total loan volume. Therefore, Dr. Robinson used 2.2% as Money Mart's bad debt ratio. Dr. Robinson ran different scenarios to test the sensitivity range for bad debt expenses, and concluded that a 2.8% bad debt rate at a $15 rate cap, while other factors remained the same, would generate a zero excess profit for a lender.

The Deloitte LLP Report which was included in the CPLA's pre-filed evidence used a bad debt expense of $6.35. Dr. Robinson was critical of that expense because, in his estimation, lenders who responded to the survey might have had a selection bias. Further, he was of the view, the bad debt cost included opportunity cost. This means that the lender was counting the loss of the loan fee instead of just the principal amount of the loan. He disagreed with Deloitte LLP's bad debt ratio assumptions, defining the bad debt expenses as only the value of the loan not ultimately collected.

Dr. Robinson testified that he had calculated a 4.4% bad debt ratio based on the Cash Money information provided by Ms. Soper during her presentation. According to Dr. Robinson, if the bad debt ratio was 4.4% per $100, the corporation would only generate excess profit at a $17 rate cap, and would lead to a loss at a rate lower than $17. However, if Cash Money did some underwriting of its loans, then in Dr. Robinson's view, operations could be viable with a rate cap of $15 per $100.

3.1.5.4 CONCLUSIONS IN FINANCIAL MODEL

Assuming a per store loan volume of $2.34 Million, operating costs of $11.00 per store, a cost of capital of 8.00%, and a bad debt rate of 2.20%, according to Dr. Robinson's model, a payday lender would be financially viable at a rate cap of $15 per $100 borrowed.

Dr. Robinson was of the view that there is strong evidence a rate of $17 per $100 borrowed is too high, and recommended a reduction in the rate cap to 15%. He also noted that a rate of 14% would generate a significant economic loss at the assumed loan volume of $2.34 Million and operating costs of $11.00.

3.1.5.5 CPLA POSITION

CPLA provided the Deloitte LLP Report on Payday Loans in Alberta as evidence of the cost of lenders to offer a payday loan in Alberta. The study was based on data provided by four companies, operating 185 payday loan outlets and two internet licenses. CPLA was of the view that the study provided relevant information on costs to provide a payday loan.

Based on the responses received to the survey, Deloitte LLP summarized the loan statistics in its Report, as follows:

Description	Total	Per Store (simple average)
Total dollar volume of loans issued in most recent fiscal year	$443,830,902	$2,008,285
Total number of loans issued in most recent fiscal year	814.891	3,687
Average loan size	528.20	528.20
Dollar value of loans that went into default[1]	80,113,422	362,504
Defaulted loans as a percentage of total loans	18.05%	18.05%
Defaulted loans ultimately collected	51,600,229	233,485
Collected loans as a percentage of defaulted loans	56.73%	56.73%
Defaulted loans ultimately not collected	28,513,193	129,019
Bad debts as a percentage of loans issued	6.89%	6.89%

Defaulted loans represent loans not collected on the due date. Many loans that go into default are ultimately collected.

Deloitte LLP's methodology involved segregating costs into four components: operating costs; cost of capital; cost of supplementary capital; and bad debt cost. The report estimated the cost of providing a $100.00 payday loan in Alberta to be $20.74, attributed as follows: $12.84 to operating costs; $0.56 to cost of capital; $0.99 to cost of supplementary capital; and $6.35 to bad debt costs.

Deloitte LLP also calculated the average WACC of 14% in calculating the cost of loan capital. Deloitte LLP commented that this was likely a conservative estimate.

To calculate bad debt costs, Deloitte LLP used:

- the uncollected principal amount loaned out ; and
- a portion of operating and supplementary costs allocated to the default loans, which represented the share of costs that would otherwise be borne by the loan if it had been repaid

CPLA does not have access to its members' data. CPLA's position is that the evidence appears to indicate lenders are not making excess profits at a rate of $17. CPLA stressed that the fees for payday loans are those which lenders must necessarily charge in order to stay viable.

CPLA commented that Dr. Robinson's evidence was based on assumptions, estimates and projections. CPLA pointed to Dr. Robinson testimony in cross-examination in which he conceded that, because of the many estimates used in his financial model calculations, 17% might be the correct rate cap. CPLA noted that when Dr. Robinson used figures given by Cash Money in his presentation~~,~~ there were indications that the lender would not be profitable at a rate of 15%. CPLA also noted that if, as was stated by Dr. Robinson, lenders were making excess profits, then one would expect to see more lenders opening up storefronts in Manitoba. Instead, the information from Cash Money was that one Manitoba location had been closed and one storefront operation is operating on a month-to-month lease.

3.1.5.6 CAC POSITION

CAC argued that CPLA's filings had shortcomings. With respect to the Deloitte LLP Report, CAC argued that and the Board should draw an adverse inference against CPLA respecting its failure to call a witness to speak to the findings in that report.

Such a finding is more suited to an adversarial framework where a party in a proceeding bears an onus of proof. The Board is of the view that it is not required to make such a finding as it relates to the Deloitte LLP Report.

The Board finds that Dr. Robinson's analysis, based on the data from the DFG 10-K, and the assumptions in his report, appears to suggest that Money Mart's Canadian operations would still be profitable if the rate were reduced to $15.00 per $100.00 loaned in Canada. However, it is difficult to assess the profitability of the Manitoba segment of the Money Mart operation, or the payday lending industry as a whole, with the limited data available to the Board. A rate reduction might benefit consumers in the short term, but the Board is concerned about the possibility of store closures if the rate is reduced to $15 per $100 borrowed. The Board also notes that Dr. Robinson, in cross-examination, commented that 17% may, in fact, be the equilibrium rate.

Regulations imposing the 17% rate cap, along with the other cost of credit and related limits have been in force since October 2010. The Board recognizes that licensed payday lenders are offering a loan product that is desired by its customer group and fills a need not met by mainstream banking institutions. It appears that more likely that profitability and thus viability for an efficiently run payday lending operation is being achieved in Manitoba at the current 17% rate and in accordance with loan amount restrictions existing under Manitoba regulations.

The Board is of the view that equilibrium is more likely to be achieved between the needs of consumers and the viability of payday lenders at the existing rate cap. Some consumers need and want this product. It was the Board's opinion in 2013, and continues to be so, that the credit predicament of borrowers continues to compel consumer protection, which the existing regulation brings to this industry. A reduction of the cap to 15% may reduce the number of lenders in Manitoba, and may cause licensed providers to leave the Manitoba market. In addition, the Board is recommending other changes to legislation most of which are for the benefit of borrowers that will impact the financial results of lenders.

The Board, therefore, recommends that the rate cap remain at 17% of the principal amount loaned. In so doing, the Board relies not on the findings in the Deloitte LLP Report, but on the industry stability since the 2013 review, the evidence from Dr. Robinson that 17% may in fact be the equilibrium rate, and that the financial model provided by Dr. Robinson tends to show that there is risk of financial loss for a lender at the 15% rate, if bad debt levels surpass 2.8%.

C11, in its pre-filed evidence, suggested that the cost of cash cards be removed from definition of "cost of credit" because, due to C11's particular circumstances it is not feasible to provide payday loans in cash. The Board is not satisfied, however, that there is sufficient evidence that this is a cost that should be borne by the consumer rather than the lender. To allow the lender to pass on the cost of the cash card to the borrower could lead to inequality among borrowers as to the cost of credit charged to them, depending on their location and whether or not they are given the option of receiving their funds in cash, or whether they are required by the lender to use cash cards.

3.1.6 MAXIMUM LOAN AMOUNT

Payday Loans Regulation 15.2 provides that the maximum amount of a payday loan must not be more than 30% of a borrower's net pay. The Board was tasked in this Review of examining the impacts of further reducing the maximum, to 25%.

In the 2013 review, the Board found that the 30% maximum was serving to reduce the risk of consumers over-extending their credit. The rationale for the maximum loan amount has been to reduce the risk of over-extension and prevent a debt trap situation for the borrower.

Dr. Robinson provided evidence as to the effect of the payday loan limit on the total fees per year and fees as a percentage of take-home pay, if the borrower was to borrow the maximum amount one to eight times in a given year. In his opinion, a single loan would be reasonably regarded as having an immaterial effect. In his view, a reduction to the permitted borrowing level would not significantly improve the experience of borrowers. Reducing the maximum fee would reduce the total share of the budget going to loan fees, but it would not assist with the borrower’s challenge of making the large balloon repayment due on the next payday.

In Manitoba, according to Dr. Robinson's analysis, the effect on a borrower's income with a maximum loan amount of 30% versus 25% on a rate cap of $17.00 per $100.00 borrowed (assuming the borrower takes out eight loans per year) would be as follows:

- Maximum loan amount of 25%: loan fees as 1.3% of the borrower's income
- Maximum loan amount of 30%: loan fees as 1.6% of the borrower's income

Dr. Robinson opined that reducing the maximum loan size from the 30% would not provide substantial relief to borrowers. The problem for borrowers caught in a debt trap is the fact that they are required to make a balloon payment of a single lump sum on the next payday. Dr. Robinson recommended installment plans as a more suitable way to respond to the debt trap problem, rather than a further reduction in the maximum allowable rate.

CPLA's submission was that the maximum loan amount should not be reduced. CPLA provided information in its pre-filed evidence that reducing the amount of the borrower's net pay to determine the maximum loan amount, from 30% to 25%, would reduce revenue for lenders by 16.7%. This was premised on the assumption that all borrowers are always taking out the maximum permissible amount.

The report prepared by Grant Thornton LLP and filed by CPLA in this Review indicated that 62% of borrowers did not borrow the full amount for which they were eligible, and on average, they borrowed 68.1% of the eligible amount. According to the CPLA, this showed that borrowers are aware of their financial circumstances and seek only to borrow the specific amount needed. Given the foregoing, the Board finds that it is more likely that the reduction in overall revenue would be somewhere below the 16.7% referred to by CPLA.

Essentially, CPLA's position was that further regulation would not reduce demand for the payday loan product, but could limit consumers' access to licensed lenders since poorer financial results would likely cause a reduction in the number of licensed operators.

CAC, CPLA, and C11 took the position that the maximum loan amount should not be further reduced as it would not serve to alleviate the debt trap many borrowers find themselves in.

Based on the evidence and information received, the Board has concluded that some consumers who cannot have their needs met with a single loan at the existing maximum amount simply get another loan from another payday lender during the same period. Further reducing the maximum loan amount will not serve to alleviate this situation. On the other hand, increasing the maximum loan amount, which was discussed as a possibility in the cross-examination of Dr. Robinson, could lead to further debt repayment challenges for consumers.

The Board therefore recommends that the limit on borrowing remain at 30% of net pay based on the existing regulation.

3.1.7 RATE CAP AND "COOLING-OFF" PERIOD

The Payday Loan Regulations impose a rate cap of 5% in three circumstances: where the loan is a replacement loan, where the loan is an extension or renewal of a payday loan previously arranged or provided, and where the payday loan is arranged or provided by a payday lender within seven days after the borrower repaid in full another payday loan previously arranged or provided by that payday lender.

The Board received information regarding the effect of the latter, commonly referred to as the "cooling-off" period.

The Board explained in its 2013 Report that "cooling-off" period intended to slow the growth of consumer debt and minimize the risk of borrowers falling into a debt trap.

However, the Board acknowledged that a borrower could still go to another lender to source another loan within that seven day period if the original lender did not issue another loan during the cooling off period.

The lender can choose to make another loan before the expiry of the cooling off period. However, it appears that none do so. C11, in its pre-filed evidence, stated that the rate cap of 5% is not viable in any circumstances.

The Board recommends that the seven-day "cooling-off" period be reduced to a one day period. This period is also used in some U.S. jurisdictions. The Board concludes that this seven day period is not preventing consumers from proceeding to take out payday loans from other lenders during the seven-day period. Removing this requirement in the regulations will allow consumers to remain with their lender of choice than seek another loan from an alternative source. The one day waiting period will allow continued enforcement of the replacement loan provisions currently set out in legislation.

There may be cases where the borrower is unable to repay a loan by the due date because of the balloon repayment of an amount owing or because of a temporary drop in income. In such cases, the lender has the option of granting an extension or can allow repayment by installments. There was no evidence heard by the Board that disclosed how often this option is utilized or granted by lenders.

CPLA indicated that it was prepared to work with government to offer repayment by installments provided a borrower had successfully repaid three or more previous loans.

The Board is of the view that allowing borrowers to make installment payments or get a loan extension when suitably qualified makes sense. Borrowers experiencing unexpected difficulties would then be allowed to repay over a longer period. While the CPLA advocated for installment loans as an option, the Board is of the view that this be made mandatory because the clientele is predominantly composed of low income, vulnerable consumers. However, this right should be limited so as to provide temporary relief only. The Board is of the view that lenders who allow repayment by installments should be compensated incrementally for the duration of the installment period because of the longer repayment period.

The Board recommends however that a rate cap of 5% apply when loans are extended by a lender. The 5% rate cap should apply when extending the loan until the next pay period. The duration of the installment period should be four pay periods beyond the initial due date and the rate cap for the installment period be set at 7%. Borrowers would be able to get an extension or an installment loan provided that they have successfully repaid three loans during the previous 12 month period.

The borrower could only opt to get a loan extension or an installment loan twice during a successive 12 month period.

3.1.8 REPEAT BORROWING

The Board received significant evidence on the issue of repeat borrowing:

Dr. Buckland stated that, based on the literature, it appears, there is no evidence that payday loans do not benefit any consumers. However, there is a particular concern that some consumers are not benefiting from payday lending, specifically those consumers who are described as vulnerable. He described repeat borrowing as a chronic challenge with the payday loan industry. Dr. Buckland cited research from Pew Charitable Trusts in the U.S., which found that borrowers take out eight, 18-day, on average, $375.00 loans in one year, and owe $520.00 in fees. Dr. Buckland concluded that U.S. research provides considerable evidence repeat borrowing is quite common. Data in Canada is more limited, which makes it difficult to assess with any precision how often Canadian borrowers are taking out payday loans on an annual basis.

The CFCS survey asked respondents how many payday loans had they taken out over the past 12 months: none, one, two, or three or more. The 2014 results showed that 19.63% of respondents had taken three or more payday loans out in a 12-month period.

The majority of respondents, 57.01%, had taken out payday loans twice in the previous 12 months.

Dr. Simpson noted that the CFCS information provides no further information about repeat borrowing beyond what is contained within the category of three or more payday loans. Dr. Simpson indicated that within the category of three or more borrowers, there might be borrowers with a very high number of loans per year, both simultaneous loans and sequential loans. The survey data did not, however, allow Dr. Simpson to draw any further conclusions.

The presence of repetitive borrowing amongst payday loans consumers is also evidenced by the findings in the Research Study conducted by Ms. St. Aubin. In the study, a sample of 120 survey respondents were asked to report how many payday loans they had taken out in the past 12 months. The results were as follows:

- 1 to 3: 45%
- 4 to 6: 24%
- 7 to 9: 6%
- 10 to 12: 20%
- 13 to 15: 2%
- More than 15: 3%

While the sample from the Research Study is non-representative because of small sample size, a majority of respondents had taken out four or more payday loans in a 12-month period. The survey also showed that 31% of respondents had taken out seven or more payday loans over a 12-month period. Those respondents who had taken out seven or more payday loans gave, the main reasons for using payday loans as: not being able to pay the first loan and meet current expenses; unexpected expenses; and due to emergencies.

Dr. Robinson discussed the frequency of repeat borrowing in the payday lending industry. In his opinion, the business model of the payday loan industry requires repeat borrowers and not one-time customers. In his view, the data seems to indicate the proportion of payday loan borrowers taking out a substantial enough number of loans per year is such that it can be concluded they are caught in a debt trap.

The only Canadian data in Canada made available to the Board with respect to the proportion of payday loans borrowers engaged in repetitive borrowing practices is from BC and Nova Scotia. Consumer Protection BC data show that the average annual number of loans per borrower in BC was 5.9 in 2012, 5.4 in 2013, and 4.3 in 2014. In Nova Scotia, data gathered by the regulator indicated that for 2013-2014, 52% of all payday loans were repeat loans of some type, and of those, 30% of borrowers received eight or more loans.

The Board is concerned about repetitive borrowing of payday loans. Although the data regarding loan frequency in Canada is somewhat limited, the Board accepts that a significant proportion of borrowers are repeat borrowers. The proportion noted in the

CFCS survey is consistent with the Board's previous findings in the 2007-08 and 2013 reviews, and the research provided by CAC in this Review. It appears that approximately 75% of loans are being made to repeat borrowers; that is, borrowers who have taken out two or more loans in a 12-month period.

The Board concludes there is a pattern of frequent use of payday loans by individuals with ongoing cash flow problems. Such individuals may be trapped in a repetitive borrowing cycle because they have insufficient funds to meet their financial needs after they have repaid their payday loans in full. The Board is of the view that repeat borrowing is a significant concern, and recommends that alternatives to payday loans be made available to alleviate this problem.

Repetitive loans to a single borrower are tantamount to a line of credit except that the cumulative effective loan rate is well beyond the rate applicable for personal lines of credit issued by financial institutions. In addition, the cumulative cost represents a significant burden for repeat borrowers who are predominantly low income individuals.

Therefore, the Board considered the option of either limiting the number of loans that can be issued to a single borrower or set a rate cap limiting the amount of money that can be generated by lenders who make repetitive loans beyond a regulatory threshold.

The Board concluded that a limit on the number of loans is the better option because the repeat borrower would be blocked from making additional loans, something that a rate cap might not do. The Board recommends that a lender be barred from making more than 10 loans to an individual in a successive 12 month period. The Board believes that this will address those borrowers who are clearly engaged in a debt cycle of repetitive borrowing.

3.1.9 ALTERNATIVES TO PAYDAY LOANS

The Board was presented with evidence from CAC regarding some current alternatives to payday loans, which are being offered in other jurisdictions. Alternatives most frequently discussed were the VanCity Credit Union Fast & Fair Loan, the Colorado State model, and the Washington State Model.

The VanCity model, offered by the VanCity Credit Union in British Columbia, provides loans in the range of $100 to $2500, with flexible repayment terms. The APR for the VanCity loan is 19%, for a term of up to 24 months. To access the loan, borrowers must become members of the VanCity Credit Union.

Colorado has a mandatory six month installment plan, rather than a two-week payday loan. The borrower may choose to repay earlier and there is no mandated schedule of how the repayments work. The loan limit is $500. Dr. Robinson explained that the fee is complicated, as follows:

- A fee of 20% on loans from $0 to $300, + 7.5 on amounts from $300 to $500.
- Once the borrower enters into the contract, the fees above are earned and the borrower must pay for it.
- In addition, the borrower pays a 45% APR + a 7.5% maintenance fee per month, to a maximum of $30 per month, starting after the first month.

The Washington State model allows a borrower to convert a payday loan into an installment loan on or before the due date. The installment period is no more than 90 days for a loan of $400 or less, and no more than 180 days for a larger loan. The specific installment plan is not prescribed. The borrower may not take out more than eight loans per year and may not take out another loan while on an installment plan. There is a state-wide database, which allows enforcement of the eight loan limit.

Dr. Buckland provided evidence with respect to the focus group report, *Comparing Payday Loans to Alternative Small Loan Products.* The purpose of the focus group of nine participants was to hear thoughts from borrowers regarding the strengths and weaknesses of the payday loan product available in Manitoba as compared with the VanCity loan and the State of Colorado installment loan. Participants were aged from 25 to 67 years old, half of whom were between the ages of 25 and 45, and the remaining four in their sixties. Annual household incomes of the participants ranged from $11,600.00 to $45,000.00.

Many of the focus group participants stated that they had few alternatives to the payday loan product. Some were not able to obtain credit from mainstream financial institutions due to bankruptcy or poor credit ratings. Some commented that because of the high cost of repaying a payday loan, they had fallen into a dependence on payday loans.

Some participants did express preference for a short-term one-time repayment because this was less worrisome or they could pay it off and be "okay" for a while. Others felt that they would not trust themselves with a larger or longer-term loan. For those participants, the small-sum and short-term loan appeared to offer them the discipline required to limit their borrowing.

Dr. Buckland stated that the focus group involved two types of payday users:

- Borrowers able to strategically use small loans from time-to-time and are able to repay them in a timely fashion; and
- More vulnerable and repeat borrowers who would eventually become dependent on payday loans.

The focus group participants were largely in favour of the VanCity model because of its lower interest rates. When presented with the information that the payday loan rate in Manitoba was approximately 517% APR, they concluded that it was too high. Some of the participants identified installment repayments and possibility of early repayment without penalty as the main strengths of the Colorado State model product. With respect to the VanCity product, the focus group was split between those who felt the long-term installment payments were strengths, and those who felt they were weaknesses. Those who viewed this as a weakness, preferred to pay off their payday loan within Manitoba's typical two week period. The larger loan size available through the VanCity model was appealing to some participants because it allowed them to access a larger sum of money compared to Manitoba payday loans. One focus group participant noted that a larger loan could potentially provide assistance to those who are stuck in a cycle of repeat borrowing because the borrower would be able to pay off more money at a reduced rate. Others saw this as a temptation to borrow too much leading to a risk of being unable to repay. Most participants agreed that the $500.00 maximum offered by the Colorado State model was not adequate.

The focus group which was a part of Ms. St. Aubin's study, discussed possible alternatives to payday loans. The State of Colorado required payday lenders to offer a six month loan product with installment repayments. Only one of the seven focus group participants was in favour of this model. The United States Consumer Financial Protection Bureau proposed that payday lenders either underwrite their loans or limit the number of rollover loans customers are allowed, followed by 60 day "cooling off period". Five of the seven participants did not see this regulation as fair. The installment loan offered by VanCity Credit Union was viewed favourably by half of the focus group participants. Most of the focus group participants did not view other alternatives such as financial education or savings plans as options that would meet their needs. The majority did not support using secured credit cards. Overall, when asked to comment on other alternatives they might like to see regarding payday loans, the focus group participants discussed the issue of interest rates applied to payday loans which in their view ought to be lower. The Board is of the view that borrowers should be assisted to get out of the debt trap cycle by offering them the option of converting a payday loan into an installment loan. It is important that regulations be put in place requiring payday lenders to offer borrowers the option to convert a payday loan into an installment loan.

The Board notes that both CAC and CPLA recommended that an installment loan option be made available to borrowers. However, they did not agree on the terms of such loans.

The Board accepts the recommendations made by both CAC and CPLA, that such a product be offered. The Board recognizes the evidence from C11 that their previous attempts to offer small installment loans to customers was not successful. There are many examples of such installment loans in other jurisdictions, such as the U.S. States of Colorado or Washington. The Board notes that the CAC evidence from the Small Loans Workshop was that some traditional financial institutions have begun to explore the feasibility of small loans and alternatives to payday loans. The Board notes that a theme in the Research Study prepared by Ms. St. Aubin was the participants' limited access to products offered by mainstream financial institutions and their feeling of marginalization. The Board is pleased to see some engagement of a few mainstream Manitoba financial institutions in this area and recommends that the Manitoba Government explore ways to engage other institutions to improve financial inclusion of low-income and vulnerable consumers.

The incoming regulations on high-cost credit products will provide Manitoba consumers with further protection regarding payday loan-like products and other high-cost credit products, but these regulations do not address rates. The Board notes that further regulation might be explored regarding the fees and charges for these high-cost credit products, and the Board therefore recommends that the Manitoba Government consult with the Government of Canada and seek the ability to regulate those fees and charges at the provincial level.

3.1.10 ONLINE PAYDAY LENDING / UNREGULATED LENDERS

The Board received significant evidence and information about online payday lending and unregulated online lenders.

Dr. Buckland identified a series of challenges unique to the online platform. One is the asymmetry of information in the online context. For example, depending on the information provided by the consumer in order to obtain a payday loan, the relationship between the payday lender and the consumer could be asymmetrical because the lender then has significant information about the borrower and the reverse is not true. Much of the reporting and research on online lending is based on reviewing websites, and in some cases, follow-up phone calls but there is limited data regarding what happens when consumers actually take out a payday loan. In addition to the asymmetry problem, according to Dr. Buckland, there is an issue with what is referred to as "lead generators". A lead generator is a company with a strong internet presence that can attract customers to its website, collect information from the customer, and then direct that person to a payday lender. There is a cost to lead generation which can then in turn be a cost that must be paid by the customer.

Dr. Buckland was a research consultant on the CCC study filed by CPLA, which found that online unlicensed payday lenders typically do not follow regulations in the jurisdictions where the loans are offered. Unlicensed online payday loans are being made available to Manitoba consumers. According to Dr. Buckland, currently, online lending tends to be used by younger people who are more comfortable with online platforms. It also appears that online borrowers tend to be borrowers who have a slightly higher income. However in many cases the online customers are also storefront customers.

Dr. Buckland said that to date he has not found any evidence that vulnerable people are more likely to use online lending; however, it doesn't mean it is not the case. There is simply no evidence available.

Dr. Buckland reviewed the research done by the Pew Charitable Trusts in the U.S., which looked at the impact of different regulatory regimes, classified as "permissive", "hybrid", and "restrictive". In permissive regulatory schemes, the regulations essentially allow the payday lender to operate using the lender's own business model, with high rate caps. The hybrid model contains some limitations in business practices; for example, rate caps could be set at the level required for an efficient lender. Restrictive regulatory regimes are those where payday lenders are essentially prevented from operating, and the interest rate cap could be approximately 36% APR.

Dr. Buckland testified that U.S. research indicates there is limited evidence that restrictive rate caps lead consumers to rely on underground payday lending. However, there is convincing evidence that there has not been a major move to internet payday lending in restrictive U.S. states. He added that more data are required regarding internet payday lending. The research to date indicates that there is a need for continued regulation of payday lenders and that governments should more carefully examine other fringe financial institutions. In his view, both storefront and online platforms ought to be regulated.

The sample of online payday loan borrowers for Ms. St. Aubin's study was relatively small. 6% of respondents had used online payday loans. Respondents used online payday loans primarily because they were convenient, secondly because service was quick.

C11 provided some anecdotal evidence that use of online payday loans is increasing among its clientele. C11 reviews consumers' bank account statements in order to determine their eligibility for loans; consumers are taking out loans from what appear to be online lenders.

According to the CPLA, there is limited data regarding online lending but the information from the CCC Report shows that this is a growing area. The CCC Report also shows that online, unlicensed lenders show little compliance with regulation.

CPLA's representative expressed the view that if online payday loans can easily be accessed and a borrower is restricted from obtaining a storefront payday loan, that person will seek a loan from an online, and possibly offshore and unlicensed lender.

CPLA argued that if regulations become overly restrictive, licensed lenders will leave the market and borrowers will move to online, predatory unlicensed lenders. CPLA was critical of the studies upon which Dr. Buckland based his opinion of online lending because they were older and therefore out of date. CPLA stated that consumers are more sophisticated and e-commerce is becoming widespread.

During the course of the hearing, Ms. Ellison of Policis made a presentation to the panel. The Policis conclusion was that if storefront payday lenders are unduly restricted, internet lenders will take over the business and charge higher rates invade privacy and expose borrowers to the risk of identity theft.

CAC responded that the Board ought to draw an adverse inferences about the information provided in the Policis presentation. First, Policis did not disclose prior to appearing as a Presenter that its appearance was funded by CPLA. In addition, no expert report was filed. Ms. Ellison was not called as a witness on behalf of CPLA, and she was not subject to cross-examination.

Dr. Buckland contended that Policis did not demonstrate a shift to internet lending in restrictive regimes. Furthermore, Dr. Buckland stated that the Policis presentation failed to take into account the United Kingdom experience. The United Kingdom only imposed regulation at the beginning of 2015 and the Policis and Dollar Financial Group evidence was that the growth in internet lending happened before payday lending became seriously regulated. Dr. Buckland outlined various issues with the source of the Policis data. Dr. Robinson stated that the Policis information did not seem to be consistent with the balance of the data in the research in this area.

The Board recognizes that the information provided by Policis was not subject to cross-examination, nor was it given under oath. Therefore, the findings in the Policis presentation were not rigorously tested. Moreover, the response from the Coalition experts outlined what appeared to represent some serious shortcomings with Policis' conclusions. As a result, the Board concluded that the presentation or its findings cannot be relied upon in arriving at its decisions.

Nonetheless, the Board remains concerned about the possibility that overly restrictive rates might drive licensed lenders out of the market, leaving a vacuum for unlicensed and unscrupulous lenders to fill. The Board is of the view the evidence has established that a group of consumers need and use the payday loan product.

The Board is concerned about the presence of unregulated lenders and the potential growth of unregulated lending in Manitoba. The Board acknowledges there is some indication in the literature reviewed by Dr. Buckland that U.S. jurisdictions with stringent regulations, have not experienced an increase in use of online or unregulated payday lenders. However, Canadian data are limited on this question. Moreover, it is clear that online and unregulated payday lenders are active in the Manitoba market. The Board accepts as a common sense inference that overly onerous regulations and rate caps might ultimately lead to the departure of regulated lenders and give unregulated lenders free rein to serve an underserved consumer. The Board has therefore taken this into account in recommending that the existing rate cap of 17% remain in place, so as to ensure industry viability and prevent the potential that more unlicensed or unregulated lenders permeate the market.

Given the evidence received by the Board through Dr. Buckland's reports and testimony and the CCC Report regarding the risks to consumers associated with online lending, the Board also makes a number of recommendations regarding online payday loans. The Board notes that online lending is an area in which unlicensed lenders show little to no compliance with regulation, and the Board is concerned with issues such as the asymmetry of information between the consumer and lender in online platforms, along with the increased risk to consumers who borrow online. As such, the Board accepts the recommendations made by CAC on this issue, and recommends that:

- The Manitoba Government and the payday lending industry take steps to: inform the public about privacy safeguards and requirements when using online payday lending sites; inform the public about their privacy rights, and what information they do not have to provide to online lenders; and inform the public about the risks of providing personal information to lead generators and unlicensed lenders;

- That the Manitoba Government and industry leaders require online lenders to implement discernible measures to ensure that privacy policies are read and understood by consumers;

- That licensed lenders be encouraged to report unlicensed lenders and lead generators to the regulator;

- That cooperation among jurisdictions be encouraged, to enable prosecution of non-compliant lead generators and online lenders;

- That the Manitoba Government and industry leaders recommend to the Government of Canada that regulations to the *Personal Information Protection and Electronic Documents Act* (PIPEDA) should be put in place, prohibiting online lenders from requiring borrowers to provide their Social Insurance Number (SIN) for identification purposes, and if a SIN is required that the borrower be provided with an explanation as to why it is needed and how it is to be used;

- That regulations be put in place that prohibit online lenders from obtaining consent to disclose the borrower's personal information to unidentified third parties, except in keeping with PIPEDA exceptions; and

- That regulations be put in place requiring online lenders to inform borrowers of their right to access their personal information, challenge its accuracy and have inaccurate information amended

3.1.11 FINANCIAL LITERACY

The Board received some evidence on the financial literacy of borrowers.

In the Research Study conducted by Ms. St. Aubin, 41% of survey respondents were somewhat satisfied or very satisfied with the lending rate that they received, but the majority of participants did not have an understanding of the annualized percentage rate or APR. 65% of survey respondents did not know the APR that they had paid on their last payday loan. Payday loan borrowers may not be fully aware of the true cost, on an APR basis, of payday loans. The Board noted in the 2013 review, and wishes to highlight again, the underlying need of consumers of payday loans to be better informed regarding personal credit and basic financial matters and to have a better understanding of how to manage their personal financial affairs.

The Board accepts that disclosure of information to payday loan consumers can be improved. The Board notes that both CAC and CPLA made recommendations to the Board regarding the use of a standard form contract, directed at providing consumers with plain-language, clear and understandable explanations of the terms and conditions of payday loan contracts. The Board supports making changes to disclosure requirements which would have the effect of making the terms of payday loans transactions as understandable as possible for consumers. The Board therefore recommends that the requirements for printed materials provided to payday loan consumers be revisited, including the establishment of a standard form contract such as that recommended by CPLA. The Board further recommends that in developing the standard form contract, a plain language consultant, user testing, and a stakeholder working group should be used.

The Board also recommends that the regulations be amended such that payday lenders be required to provide an oral explanation of the information contained in the standard form contract. The Board also recommends that the regulations be amended so as to require Manitoba payday lenders to provide consumers, at the time of borrowing, with a document that demonstrates the cost of a payday loan to the consumer as compared to borrowing with a credit card.

The Board accepts that there is evidence from both the CAC experts, and the CPLA via the CCC Report, showing that some storefront and online payday lenders require that borrowers provide their Social Insurance Number (SIN) for identification purposes. In the study, *Manitoba Consumers' Experiences with Payday Loans: Pricing and Practices of Licensed Payday Lenders in Manitoba*, the majority of lenders interviewed requested a SIN from borrowers. Dr. Buckland’s literature review showed that some online lenders require the customer's SIN. While loan applicants could decline to provide personal information, the lender could then decline the applicant's loan request. This puts borrowers in a position where they have no choice but to provide a SIN in order to obtain a payday loan. There is also an indication that online payday lending may carry with it a particular risk given the issue of asymmetry of information where the lender has knowledge and access to information while the borrower has limited knowledge and minimal access to information.

The Board is concerned about the potential privacy risks to consumers using both storefront and online payday loans who do not have other forms of identification than the SIN. The Board therefore accepts the recommendation made by CAC, and recommends that the Manitoba Government establish a low or no cost universal identification option, that would eliminate the need for the SIN as identification.

3.1.12 OTHER FINDINGS AND RECOMMENDATIONS

Dr. Robinson also commented on the licensing fee that lenders are required to pay in Manitoba on an annual basis. The amount in Payday Loan Regulation 7 is $5,500.00. Dr. Robinson was of the view that the licensing fee ought to relate to the loan volume of the lender as opposed to a flat fee. He recommended calculating a fee based on 0.2% of loan volume. In his view, this would be a fair form of licensing to tie it to the business operations.

CPLA did not take a clear position on this issue. In its closing submissions, CPLA commented that Manitoba's licensing fees are among the highest in Canada.

The Board recommends that the licensing fee be changed from the current regulated amount. The Board accepts that a flat fee for all licensed payday lenders may result in a situation where large, corporatized lenders with multiple outlets are better able to afford the significant licensing fees than smaller, individually-owned outlets. The Board therefore recommends that the regulations be amended such that the licensing fee be payable based on a percentage of the lender's per-store loan volume. The Board recommends however that the financial education levy remain in place at the current rate, and not be tied to loan volume, so as to ensure that the Financial Literacy Fund receive a consistent level of funding. The Board suggests that tying licensing fees to loan volume might serve to allow the provision of further information to the Consumer Protection Branch regarding the state of the industry.

With regard to default, the Board did not receive evidence that would indicate that there should be any departure from current default interest rate found in Payday Loan Regulation 15.4(1), and therefore the Board recommends that it remain in place, at 2.5% per month, non-compounding.

The regulation regarding a payday lender’s recovery of the cost of a dishonoured cheque or debit transaction should be changed. Dr. Robinson suggested that the full expense of a lender be recoverable, and the Board agrees with this recommendation. The Board notes that it made this same recommendation in its 2013 review.

In addition to the foregoing, included among the recommendations made by CPLA were the following:

- A job loss extension program: if, following a borrower taking out a payday loan, the borrower experiences an involuntary job loss or loss of income, the borrower may notify the lender before the loan is due, providing reasonable evidence of the income or job loss, following which the lender will be required to extend the payment date of the outstanding loan, to a date that is the next payday after the date three months following the date of notification to the lender; during this period, no further interest or fees will accrue on the loan.

- o Mandatory acceptance of settlement plans proposed by credit counsellors: a regulation should be enacted which requires that any licensed payday lender accept a proposal put forward by a not-for-profit credit counsellor providing for pro-rata settlement of debt with all other creditors.
- o Mandatory referral to credit counselling services: a regulation should be considered which would require a lender to provide any borrower who has taken out three or more payday loans within a three month period with referral information to a credit counselling service at the time of applying for their first loan.

CAC indicated its support for these recommendations. The Board notes that these three recommendations would serve to address the debt trap problem, and as such, agrees with two recommendations but recommends that the offer of loan extensions and installment loans to suitably qualified borrowers be mandatory for the lender.

Lastly, the Board recommends that one year's notice be given by the Manitoba Government into the initiation of further payday loan reviews. This would permit potential Interveners and Presenters to have sufficient notice in order to conduct any research or consultation needed to bring a fulsome perspective to the payday loans hearing.

Schedule “B” to the Report has a chart which discloses the regulatory provisions reviewed and the Board’s recommendations for ease of reference.

4.0 SUMMARY OF BOARD RECOMMENDATIONS

In accordance with Section 164 of *The Consumer Protection Act of Manitoba,* the Public Utilities Board hereby recommends:

1. That the maximum fee on a payday loan remain at the rate of $17.00 per $100.00 borrowed.

2. That the maximum percentage of a borrower's net pay used to calculate the maximum loan amount remain at 30%, and not be reduced to 25%.

3. That the cost of credit remain as calculated in the regulations. The single rate should continue to include all of the component costs for a payday loan.

4. The limit of 5% on the rate for a replacement, extension or renewal loan remain at 5% of the principal.

5. With respect to the "cooling-off" period set out in Regulation 13.1(3), the Board recommends that it be changed to one day, permitting lenders to issue a new loan with a rate of up to 17% of the principal amount of the payday loan, provided the preceding loan was paid off at least one day prior.

6. At the request of a borrower who has successfully repaid three prior pay day loans from a lender over the preceding 12 month period, the lender be required to either grant a pay day loan extension at a rate of 5% or convert the pay day loan to an installment loan to be repaid over the next four pay periods and that

the applicable rate for the installment loan be 7% of the principal outstanding amount of the principal owing when the installment loan was requested.

7. Pay day lenders be prohibited from issuing more than 10 pay day loans to a borrower over a successive 12 month period.

8. Upon default, the current interest rate remain at 2.5% per month, non-compounding.

9. That the full expense of a dishonoured cheque or debit transaction incurred by a lender be recoverable, subject to proof of the actual cost incurred being provided by the lender to the borrower.

10. That the licensing fee for payday lenders should be calculated on a percentage of loan volume per store. The appropriate percentage rate should be calculated after consultation with industry consumer stakeholders. The financial education levy should remain in place and at the rate currently set by regulation.

11. That payday lenders and industry leaders consult and negotiate with the Manitoba Government to discuss further reporting requirements that might be put in place to determine data that should be available for confidential filing by lenders to serve the interests of regulators. The mandatory reporting items on a per store basis should include: the number of loans made; total cost of credit for all loans; the dollar value of loans (principal) made and; the number and value of defaulted loans; and the number of repeat loans issued and number of individual borrowers obtaining repeat loans.

12. That the Manitoba Government consult with the Government of Canada and seek the ability to regulate the fees and charges of high-cost credit products other than payday loans sold in Manitoba.

13. That the requirements in the regulations for printed materials provided to payday loan consumers be revisited, including the establishment of a standard form contract. In developing the standard form contract, a plain language consultant, user testing, and the stakeholder working route should be used.

14. That payday loans regulations be amended such that payday lenders be required to provide an oral explanation of the information contained in the standard form contract where the consumer has limited literacy skills.

15. That the payday loans regulations be amended so as to require Manitoba payday lenders to provide consumers, at the time of borrowing, with a document that demonstrates to the consumer the cost of a payday loan as contrasted with the fees associated with borrowing on credit cards.

16. That the Manitoba Government establish a low or no cost universal identification option that would eliminate the need for the Social Insurance Number as identification for payday lenders.

17. That research be undertaken by the Government of Manitoba to assess the economic and social consequences of payday loans on individuals and communities, in order to inform future payday loan reviews. Such research should focus on issues such as repeat borrowing, internet borrowing, and the

potential for new communications technologies to be used by mainstream financial institutions in providing alternatives to payday loans. A review of the best pay day loans practices from other jurisdictions should also be undertaken.

18. That the Manitoba Government explore ways to engage mainstream or traditional financial institutions in improving the financial inclusion of low-income and vulnerable consumers.

19. That the Manitoba Government and the payday lending industry take steps to: inform the public about privacy safeguards and requirements when using online payday lending sites; inform the public about their privacy rights, and what information they do not have to provide to online lenders; and inform the public about the risks of providing personal information to lead generators and unlicensed lenders.

20. That the Manitoba Government and industry leaders require online lenders to implement discernible measures to ensure the privacy policies are read and understood by consumers.

21. That licensed payday lenders be encouraged to report unlicensed payday lenders and lead generators to the regulator.

22. That the Manitoba Government encourage cooperation among jurisdictions to enable prosecution of non-compliant lead generators and online lenders.

23. That the Manitoba Government and industry leaders recommend to the Government of Canada that regulations to the *Personal Information Protection and Electronic Documents Act* (PIPEDA) be put in place, prohibiting online lenders from requiring borrowers to provide their Social Insurance Number for identification purposes, and if a Social Insurance Number is required that the borrower be provided with an explanation as to why it is needed and how it is to be used.

24. That the payday lending regulations be amended so as to prohibit online lenders from obtaining consent to disclose the borrowers personal information to unidentified third parties, except in keeping with PIPEDA exceptions.

25. That the payday lending regulations be amended so as to require online lenders to inform borrowers of their right to access their personal information, challenge its accuracy, and have inaccurate information amended.

26. The payday lending regulations should be amended so as to require that any licensed payday lender accept a proposal put forward by a not-for-profit credit counsellor providing for pro-rata settlement of debt with all other creditors.

27. The Manitoba Government should consider an amendment to the payday lending regulations which would require a lender to provide any borrower who has taken out three or more payday loans within a three month period with referral information to a credit counselling service at the time of applying for their first loan.

28. That one year's notice be given by the Manitoba Government to the initiation of further payday loan reviews, thereby permitting potential interveners and presenters to have sufficient notice of the hearings in order to conduct any research consultation as necessary so as to bring a fulsome perspective to the payday loans review.

Upon review by the Panel Members herein below, The Public Utilities Board respectfully submits this Report.

"Original Signed By:"

Régis Gosselin, B ès Arts, MBA, CPA, CGA,
Chair

SCHEDULE "A"

SUMMARY OF RECOMMENDATIONS MADE BY CAC AND CPLA

CAC Recommendations

- The rate cap be reduced to $15 per $100 borrowed.
- Manitoba should amend the payday loan regulations to require lenders to offer borrowers the option of converting a payday loan into an installment loan, on the first due date.
- The maximum percentage of net pay that can be borrowed should remain at 30% of the borrower's net pay.
- Data collection on payday lenders in Manitoba should be improved.
- The licensing fee for payday lenders should be changed to a percentage of their total loan value, maintaining the current volume for the Financial Literacy Fund, and adjusting for inflation.
- Disclosure of information by payday lenders to borrowers should be improved.
- Payday lenders should not be permitted to pass on the charge for debit or cash cards to consumers.
- Research should be undertaken into the economic and social consequences of payday loans, the use and potential for new communications technologies to be used by mainstream financial institutions in providing alternatives to payday loans, and into best practices relating to payday loans in other jurisdictions, to inform future payday loans reviews.

- Ways to engage mainstream financial institutions in the small loans market and in financial inclusion should be identified.
- A low or no cost universal identification option should be established that would eliminate the need for a Social Insurance Number as identification.
- Efforts should be continued to investigate and regulate the payday loans industry, including the issues of licensing and lead generators.
- A number of recommendations should be made regarding online lending, including recommendations on information to consumers, privacy measures and disclosure obligations respecting online lenders, and encouraging cooperation among jurisdictions.
- Consideration should be given to one year's notice for payday loan review hearings, so as to allow sufficient time for research to be conducted.
- Consumers should be protected from other high-cost credit products that are not currently regulated.

In addition to the recommendations made by CAC, the CAC also provided commentary on recommendations that were made by CPLA in its submissions to the Board. CAC was supportive of the CPLA's recommendations, adapted as necessary to the Manitoba context.

<u>CPLA Recommendations</u>

CPLA provided the Board with what it described as a seven-point plan, previously prepared for the Payday Lending and Financial Inclusion Task Force in Alberta, and referred to it in providing the Board with recommendations for Manitoba. The recommendations provided by CPLA which are applicable to the Manitoba context were as follows:

- An optional extended payment plan: where a borrower takes out three or more successive loans, then for that and each subsequent loan, the lender must offer and the borrower has the option to accept repayment terms for the loan over at least three pay periods, where no payment exceeds 35% of the sum of the principal and cost of borrowing.
- A standard form of contract should be prescribed for use across the payday lending industry, in plain wording and in a consistent font, providing a clear, understandable and succinct contract, avoiding any wording that may be confusing to borrowers.
- A job loss extension program: if, following a borrower taking out a payday loan, the borrower experiences an involuntary job loss or loss of income, the borrower may notify the lender before the loan is due, providing reasonable evidence of the income or job loss, following which the lender will be required to extend the payment date of the outstanding loan, to a date that is the next payday after the date three months following the date of notification to the lender; during this period, no further interest or fees will accrue on the loan.
- Mandatory acceptance of settlement plans proposed by credit counsellors: a regulation should be enacted which requires that any licensed payday lender accept a proposal put forward by a not-for-profit credit counsellor providing for pro-rata settlement of debt with all other creditors.

- Mandatory referral to credit counselling services: a regulation should be considered which would require a lender to provide any borrower who has taken out three or more payday loans within a three month period with referral information to a credit counselling service at the time of applying for their first loan.

SCHEDULE "B"

REGULATIONS CHART

Reg. 50/2010 Section Number	**Summary of Existing Provisions**
Section 7	Fee for payday lender license - the fee payable for a payday lender license or a renewal of a license for one year or part of a year is $5,500.
Section 13.1(1)	Maximum cost of credit - the total cost of credit for a payday loan must not be greater than 17% of the principal amount of the payday loan.
Section 13.1(2)	Replacement loan - the total cost of credit for a replacement loan must not be greater than 5% of the principal amount of the replacement loan.
Section 13.1(3)	Extensions, renewals and consecutive payment loans - the total cost of credit for a payday loan must not be greater than 5% of the principal amount of the payday loan, if: (a) the payday loan is an extension or renewal of a payday loan previously arranged or provided; or (b) the payday loan is arranged or provided by a payday lender within seven days after the borrower repaid in full another payday loan previously arranged or provided by that payday lender.
Section 15.2(1)	Maximum amount of a loan - payday lender shall enter into a payday loan agreement with a borrower for a loan that exceeds 30% of the borrower's net pay, as calculated in accordance with Section 2.2(1) of the Regulation.

Section 15.4(1)	Maximum amount payable for default - the penalty that may be charged, required or accepted in relation to any default by a borrower under payday loan is a penalty of 2.5% of the amount in default, calculated monthly and not to be compounded. This penalty may be charged, requirement or accepted only once in the thirty day period.
Section 15.5	Fee for a dishonoured cheque or a stop payment - in addition to any penalty that may be charged under 15.4(1), if a payday lender is charged a fee for a cheque, pre-authorized debit or other negotiable instrument that is dishonoured or upon which a stop payment order is placed, the payday lender may charge a fee to the borrower in the same amount, by way of reimbursement, but in no case shall the fee charged by the payday lender to the borrower exceed $20.00.
Section 15.7(1) and Section 15.7(2)	No repeated attempts to process repayment - the payday lender may present a cheque, pre-authorized debit or other negotiable instrument that the borrower provided in exchange for the advance of money to a financial institution only once. Exception - despite subsection (1), a payday lender may present a cheque, pre-authorized debit or other negotiable instrument to a financial institution more than once, but only if (a) the borrower is not charged a fee, penalty or other amount by the financial institution to process it; and (b) in circumstances where they payday lender is charged a fee, penalty or other amount by the financial institution to process it, the lender does not in turn charge a fee to the borrower under Section 15.5.