4-7: Protect Yourself While Borrowing

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Cast List
- Darryl
- Terri
- Credit Counselor, 40s, black male, Jay Broderick
- Mother, 40s, black female, Tonya

Synopsis
- Single mother who appeared in 1-5 writes in to ask about nontraditional loans
- Terri and Credit Counselor meet her again in the park as her two young children play nearby
- They advise her how to evaluate some of the nontraditional loans she is considering and how to avoid predatory lending

Location
- Park

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A. Avoid Nontraditional Loans
  a. Pay day loans
    i. To get money right away and plan to pay back w/next paycheck
      1. If can't, consider longer-term loan
      2. Very expensive
      3. Usually not FDIC insured
    ii. Use only for emergencies
    iii. Red flags
      1. If advertises terms it doesn't offer
      2. If not given disclosures (APR)
      3. If no waiting period between loans
      4. If approved when have other payday loans to other companies
  b. Refund anticipation loans
    i. Short-term; secured by income tax refund
    ii. Looks like getting your refund early, but actually a loan
    iii. Cost more in the end
    iv. Volunteer Income Tax Assistance; use e-file
  c. Subprime lending – credit extended to high-risk borrowers
    i. Can be legit practice
    ii. Easy for it to be predatory
B. Avoid Predatory Lending
  a. Abusive Prepayment Penalties – high fees for paying off loan early
  b. Kickbacks to mortgage brokers (Yield Spread Premiums)
  c. Loan flipping – lender refinances it to generate fees w/no benefit to borrower
  d. May be sold unnecessary insurance
  e. Asset-based lending – Loan based on value of equity rather than what buyer can afford; may encourage default to get the house
  f. Subprime mortgages even if could qualify for less expensive
C. Get Help When You're A Victim
  a. State's consumer protection division
  b. Lawyer/pro bono legal office

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Theme music up

TERRI: This is the "Money Smart Podcast Network, with Terri and Darryl."

Music crossfade with SFX: We hear very faint "park ambiance" – rustling tree leaves, some birds

TERRI: We're back with more on money and banking. During each podcast we answer our audience's questions with the help experts like Jay Broderick, an experienced credit counselor, who's back with me today.

JAY: Hi, everybody.

TERRI: A few months ago we visited with Tonya, a single mom of two beautiful boys here in Spring Park, Minnesota. Her niece had written in to ask us to help Tonya get out from under her mounting debt. Well, last week we heard from Tonya herself. She wrote:

"I can't thank you enough. Thanks to you, the hospital and credit card company have given me payment plans. My car is paid off! And the best news is, I've found a company that will give me a check for next year's income tax refund early, which will really help out."

We're very glad Tonya's doing better dealing with her debt. However, the note about the tax refund anticipation check set off warning bells.

JAY: I'm glad you called me back, Terri. I see it all too often in my work as a credit counselor. People see what looks like an easy way out of debt, and wind up in worse shape than when they started. I'd hate to see that happen to Tonya – or any of your audience members.

TERRI: I'm with you there. Jay and I are back in the park where we initially met Tonya. In her letter, she said she's usually here this time of day with her kids.

JAY: Where's Darryl?

TERRI: He may join us a little later.

JAY: Oh, should we wait for—

TERRI: —Three words: Ice. Cream. Truck.

JAY: Ohhhh… yeah, we should definitely start without him.

TONYA: *(in the distance, to her son)* Jamieson! What did I tell you about going near the street?

TERRI: Tonya – it's Terri and Jay.

TONYA: From the podcast! *(a little perplexed)* I guess you got my letter.

TERRI: Yes, we did.

TONYA: Now hold on – Jamieson! You get back here. Joe Junior, mind your brother! I have to talk to these nice people. *(to Terri and Jay)* It's good to see you, two, but you didn't have to come all the way out here.

TERRI: Well, Tonya, your letter is the reason why we're here.

JAY: It sounds like you've been doing so well by following the advice we gave you!

TONYA: Yes! I just can't thank you enough. I feel like for the first time in so long our heads are above water.

JAY: And that's great—

TERRI: —but we saw that you‘re considering a tax refund anticipation check.

TONYA: Well, yes. My tax refund might be almost fifteen hundred dollars. With that check I can get that money right away, and it will help me make those new payments on time.

JAY: Tonya, I know it's tough. But did the company tell you about the fees you would have to pay to get that money?

TONYA: *(crestfallen)* Fees? No… I don't think so. Maybe they did, I don't know. What fees?

JAY: Well, let's talk. A refund anticipation check is really a temporary bank account. You usually pay about thirty dollars to set up the account. If you get a paper check instead, you might end up paying a check-cashing fee. And if you put your refund money on a prepaid card, you might get slapped with other fees.

TERRI: Well the fastest and least expensive way for you to get your refund is to file your tax return electronically – or "e-file" – and request direct deposit where your refund is deposited into your own bank account. You could receive your refund in less than two weeks.

JAY: Think carefully before paying hundreds of dollars in fees to get the income tax refund that already belongs to you, and that you could get just as fast by filing electronically. For example, perhaps you qualify for free tax assistance from a Volunteer Income Tax Assistance site – or VITA, for short.

TONYA: What is that, exactly?

JAY: VITA is a program coordinated by the Internal Revenue Service that provides free income tax assistance and e-filing. There may be income eligibility restrictions.

TERRI: Tonya, you and our audience members can visit irs.gov or call 1-800-906-9887 to find a VITA site.

TONYA: I didn't know about all this…

JAY: *(gently)* A lot of people don't.

TERRI: And that's why we're here. It's an important topic, and we decided enough to do an entire podcast on products like these. Sometimes these kinds of things are set up to seem like a good idea when, really, they take advantage of good people like you.

TONYA: Oh.

TERRI: So we're here to tell you what to look for and help you understand what you're getting into – as this could have an effect on the decisions you make for you and your boys.

JAY: The people who offer certain types of financial services – not just refund anticipation checks, but pay day loans, and rent-to-own services may not always make the terms very clear. In the worst cases, lenders may actively deceive or exploit borrowers. That's called "predatory lending."

TONYA: That's terrible!

TERRI: Yes, it is. Particularly because there are often alternatives through legitimate banks and credit unions.

TONYA: Maybe you all better set me straight, then. I mean, "fool me once…" What – just a minute. *(to her son, off mic)* Joseph Junior! Give Jamieson back his football! *(to Jay and Terri)* Sorry. What else should I be looking out for?

TERRI: That's a great idea, Tonya. So, Jay, while we've got you here, what other kinds of borrowing might not be in our audience's best interest? What should they watch out for?

JAY: Two of the ways I see people get into trouble are pay day loans and rent-to-own services. A pay day loan is a short-term loan secured by a paycheck. People use pay day loans when they need money right away, and plan to pay the loan back with their next paycheck.

TONYA: OK.

JAY: Let's say, for example, that you go to a pay day lender and borrow two hundred dollars. The lender might make this a two-week loan and charge you thirty dollars as a fee.

TONYA: That's not too bad.

JAY: You write a postdated check to the lender for two hundred and thirty dollars. The pay day lender holds the check for two weeks. At the end of those two weeks, you repay the loan by letting the lender cash the check. Or you can pay off the full amount in cash.

TONYA: So what's the problem?

JAY: Well, for one thing, you're paying an extremely high interest rate. 30 dollars for borrowing two hundred dollars for two weeks is the same as paying seven hundred and eighty dollars to borrow it for a year. That's an "annual percentage rate" – what we call an APR – of three hundred and ninety percent.

TERRI: Wow! Even credit cards usually don't charge more than eighteen to twenty-two percent.

JAY: Exactly. Now, what happens if you can't pay the loan back after two weeks? Most payday lenders allow you to "roll over," or renew, your loan for an additional fee. In this case, you would write another postdated check, this time for two hundred and sixty dollars – two hundred and thirty plus thirty dollars for the additional fee.

TONYA: So I now owe two hundred and sixty dollars. That's even harder to pay off with one paycheck.

JAY: Right. All too often the loan just keeps adding up, and people are never able to pay it off.

TERRI: So, Jay. How should people protect themselves?

JAY: I advise people to build up a savings fund to use for rainy days. If you need to borrow money, be aware of certain red flags that a lender may not be offering products in your best interest.

TERRI: Like what?

JAY: Suppose the company advertises terms that it doesn't really offer, or you're not given a clear statement – called a disclosure – of the finance charge and APR. Those are some signs.

TERRI: It seems like any of these could get you into a level of debt that you could never get out of.

JAY: Right. We've even heard of pay day lenders that have threatened to prosecute their borrowers for writing a bad check – even though they knew that those borrowers didn't have the money when they paid the pay day loan fee!

TONYA: That's just awful. What do people do?

JAY: I tell people to go their bank. Explain the need. See if they can set up a loan that they can pay off over time from a checking account where their paychecks are being direct deposited. It's much cheaper – and *much* safer.

TERRI: What other kinds of borrowing do people need to be careful of, Jay?

JAY: Rent-to-own services. That's when a store sets up a plan for you to rent an item until you pay enough to own it. It may not sound like a loan, but it is – there's a difference between what you would pay to buy the item outright, and the total of the payments. That's like the interest you would pay on a loan.

TONYA: So what's the problem?

JAY: Let's say you wanted to buy a fancy TV for – say – fifteen hundred dollars.

TONYA: *(wistfully)* That would be nice.

JAY: The store advertises the TV for fifty-five dollars every other week.

TONYA: *(surprised)* I could almost afford that!

JAY: With the fine print, you find out that you have to make that payment for two years in order to own the TV. First off, that is fifty-two payments times fifty-five dollars, or two thousand eight hundred and sixty dollars you will pay for a fifteen hundred dollar TV.

TONYA: Oh!

JAY: Let's say you keep the TV for just a year and then decide to return it. You've paid twenty-six payments times fifty-five dollars, which would be one thousand four hundred and thirty dollars. That's almost the full price and yet you have to give the TV back. Also, the store is the legal owner until you've made all of the payments. If you miss even *one* payment, the terms of the agreement may allow the store to take the TV back and keep your money.

TERRI: So if you made fifty payments on time, and then missed payment number fifty-one for some reason…

JAY: The store takes the TV and keeps – let's see, fifty payments times fifty-five dollars, that's two thousand seven hundred and fifty dollars – of your money.

TONYA: That doesn't make sense. But – now I'm not saying I'm going to buy a big new TV like that – but is there a better way?

JAY: Well, it's very possible that a consumer installment loan would be a better way to go. For example, a bank might offer a two-year installment loan to buy that same TV at an annual percentage rate of twelve percent. With timely payments, you would pay a total of one thousand six hundred and ninety-five dollars over the two years.

TONYA: That's a lot less.

JAY: And the monthly payments would be only seventy dollars and sixty-one cents, compared to fifty-five dollars twice a month for the rent-to-own service. Don't get me wrong – sometimes it may make sense to use a rent-to-own business. But just as with any financial transaction, know your options.

TONYA: Stop that right now!

JAY: I'm sorry?

TONYA: *(to her son, off mic)* Joseph Junior, if you make him cry again there's no video games for you for a week! *(To Terri and Jay)* You all will excuse me for a moment?

TERRI: *(chuckling)* They're so cute. Jay – you mentioned predatory lending. Tell us more.

JAY: When you shop for a loan, you need to be careful to understand what you are agreeing to. And you need to be confident that you are getting the best deal for you. It doesn't matter whether you are shopping for a loan secured by your home, or a credit card, or a car loan. You need to comparison shop and not agree to anything until you take time to understand it.

TERRI: That makes sense. Can you tell me more about what you mean?

JAY: What we've seen are companies offering loan products using deceptive marketing tactics… abusive collection practices… and loan terms that just don't make sense for borrowers. One of the things we've heard a lot about is predatory lending in the subprime market.

TERRI: That's been in the news. What exactly is "subprime?"

JAY: "Subprime lending" is when loans are made to people who are considered to be higher risk. Maybe they've had problems repaying credit in the past, or maybe they have a limited credit history. For that reason, lenders charge higher interest rates and loan fees.

TERRI: OK, like what?

JAY: Some mortgages carry a penalty for paying off the loan early. Those are called "prepayment penalties." Some credit cards targeted to those without credit histories may have considerable fees.

TERRI: Good advice. What else?

JAY: Well, there's something called "credit insurance packing."

TERRI: What's credit insurance?

JAY: It's insurance that will pay the outstanding loan balance to the creditor if you die, or will make monthly payments if you become ill, injured or unemployed.

TERRI: Sounds like a good idea.

JAY: Maybe sometimes. But many times you can accomplish the same thing with traditional life or disability insurance with better benefits -- at considerably lower cost.

TERRI: I see – so what's "packing"?

JAY: You're at closing, and the lender gives you papers to sign that include credit insurance or other benefits that you don't need or didn't want. The premium may even be added into the loan balance, so you're paying interest on it.

TERRI: Yikes.

JAY: The lender hopes you don't notice. If you do, and you object, the lender says that you have to accept it or the loan will be delayed or even denied.

TERRI: That's terrible! But I already got my loan. I guess I don't need to be worried, then.

JAY: Well, be careful because you may receive a call or letter inviting you to purchase or opt into this – or some other product – that will cost you money every month. Your listeners should know that these types of credit protection are optional. A lender cannot condition approval of your loan on whether you buy credit insurance.

TERRI: But some kinds of insurance are legitimate, aren't they?

JAY: Yes. Don't confuse these products with other types of insurance that the lender can require, especially insurance to repair or replace property – such as a home or auto – that serves as collateral for a loan. And, private mortgage insurance – which is protection for the lender if the borrower doesn't repay the loan – can be required for certain home loans.

Now another thing – sometimes predatory lenders will steer borrowers into higher cost mortgages even when they could qualify for a less expensive, typical loan.

TERRI: That could really get you into trouble.

JAY: Another client of mine, Alice, had ten thousand dollars in credit card debt. But she got a letter offering to refinance her home. The lender never even asked her income!

TERRI: Unbelievable.

JAY: She took out a forty thousand dollar subprime refinance loan. It ballooned to sixty-five thousand dollars almost immediately because of fees and penalties she didn't anticipate. All too often the lender pressures a customer to default under these kinds of situations – and the lender gets to take ownership of the home.

TERRI: That really makes borrowing sound dangerous.

JAY: Look, Terri, federally insured financial institutions are well regulated. There are new rules that protect borrowers now. And if a consumer cannot resolve a problem with these lenders, they can contact a federal regulator for assistance. It just pays to protect yourself and make sure you know who the lender is and the terms of the loan.

TERRI: OK. How does our audience do that?

JAY: Here's some basic advice. First – pay your bills on time and make sure you have a good credit history. Review it by examining your credit report at least once a year.

TERRI: We talked about that in our podcast on Being Able to Borrow.

JAY: Good. Next, be a smart consumer. Shop around for the best deal. Don't respond to ads that make lending sound cheap and easy. Take your time before choosing a loan or lender, and don't get pressured into making a decision before you're ready. If a lender won't give you the information you need to comparison shop. Run, don't walk!

TERRI: OK.

JAY: Get some help. Ask your friends, a family member, or a credit counselor like me for advice. Take somebody along when you talk to a lender.

TERRI: I'm going to take you up on that!

JAY: Be careful of offers to refinance a loan right after you just refinanced it. And be really careful of home improvement contractors who promise to get you a loan – that's not their business.

TERRI: No, it isn't. What about the loan itself?

JAY: I tell people to make sure to read and understand the loan documents before you sign them, and keep copies of everything the lender gives you. Ask if your mortgage has a "balloon payment." That means that most or all of the loan amount comes due on a specific date. Those payments may be illegal – and you should really make sure terms like that make sense to you. Ask if your mortgage has a mandatory arbitration clause. If so, understand what it means for you.

TERRI: Uh huh. How about those optional add-on products that were marketed – such as insurance that says it will make your loan payments if you become disabled or get laid off?

JAY: The lender cannot condition approval of your loan on whether you buy a debt cancellation, debt suspension or credit insurance product. There may be better alternatives to credit life insurance, such as a life insurance policy purchased separately. Don't confuse these products with other types of insurance that may be required, especially insurance to repair or replace property (such as a home or auto) that serves as collateral for a loan, and private mortgage insurance (protection for the lender if the borrower doesn't repay the loan) that lenders can require for certain home loans.

TERRI: Jay, that's a lot to remember. These predatory lenders sound like they can be very good with their sales pitches. What if someone feels they've been a victim? Can they do anything?

JAY: Absolutely. They can contact the Consumer Financial Protection Bureau, at www.consumerfinance.gov or (855) 411-2372. I also recommend contacting your state's consumer protection division, or a lawyer. People who have limited income may be eligible for free legal services, called "pro bono" programs.

TERRI: Our audience can find those kinds of programs in the community services pages of the phone book, or on the Internet at "ABAnet.org / legalservices / probono."

JAY: There's a great booklet put out by the Federal Trade Commission on avoiding home improvement scams. It's called "Home Sweet Home… Improvement" and you can get it on the Internet at 'FTC.gov" or by calling the FTC..

TONYA: *(off mic, but coming closer)* Now you stay right there until I tell you! *(to Terri and Jay, maybe sighing a little)* Mothers raise their daughters. We just let our sons grow up. But I love 'em.

TERRI: Tonya, I hope we've convinced you to think twice before signing up for that tax refund anticipation check.

TONYA: You know you did.

JAY: If you're still having trouble managing your debt, let's talk. There may be more ways I can help you.

TONYA: I'd like that.

Theme music up

TERRI: Thank you for joining the "Money Smart Podcast Network, with Terri and Darryl." We hope this podcast will help you protect yourself while borrowing. Right now – it's a beautiful day in the park, and we're going to sit here for a while and just enjoy the peace and quiet.

TONYA: *(off mic)* Jamieson! I thought I told you to stay put! You get yourself out of that tree right now!

TERRI: Or we might be leaving sooner than expected….

Music fades