

Predatory Financial Services

What are Predatory Financial Services?

Predatory financial services take advantage of consumers. This resource highlights some common types of predatory financial services and how to avoid them.

Predatory financial services and practices can be defined by a few main characteristics:

- Impose unfair or abusive terms
- Persuade the borrower to agree to unfair terms through deceptive, coercive, or exploitative actions
- Benefit the lender and makes it more difficult for the borrower to repay the debt
- Takes advantage of a borrower's lack of knowledge about loans, loan terms, and finances

What are the most common types of predatory financial services?

Pay Day Loans

Pay day loans are high-cost, small loans averaging \$350 that usually must be repaid in a single payment after two weeks. In some cases, you may be able to extend them, or "roll them over." While they can seem like a short-term solution, these loans come with high fees, and interest rates ranging from 200% to 500%, which make them very difficult to pay back. Pay day loans are illegal in some states, due to interest rate caps, but regulations vary widely. The best alternative to a pay day loan is to build up an emergency fund. It's okay to start small and build up a fund over time. Even one week's pay saved could help you avoid taking out a payday loan.

Auto Loans

Auto dealerships can take advantage of the consumer through a variety of tactics. They can mark up the interest rates, offer subprime loans with poor terms to borrowers with poor credit, and tack on useless loan products that come with a hefty price tag.

Rent-to-Own

Companies such as Rent-A-Center offer a service called Rent-to-Own. They allow you to rent out big ticket items such as furniture or televisions for a flat weekly payment. These weekly payments add up, however, and you can end up paying double, triple, quadruple, the original price of the item.

Pawnshop Loans

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Pawnshops offer short term (usually 1-4 months) loans using an object of value as collateral. If you don't repay your loan, the pawnshop gets to keep your item. Interest rates on these loans vary state by state, however, pawnshops often charge additional per month service fees. Nonpayment of a pawnshop loan won't affect your credit score, and there will be no collection action taken.

Refund Anticipation Loans

While as of 2013, refund anticipation loans are no longer legal, several other financial products exist that promise to get you your tax refund faster:

- **Prepaid debit cards:** Many tax preparation companies will offer the option of a prepaid debit card as a way for consumers to expedite their tax refund. These cards carry activation and monthly maintenance fees.
- **Refund anticipation checks:** These are short-term loans that allow you to wait to receive your tax refund before you pay your tax preparation fee. The lender usually charges a fee of \$30 to \$35 and the preparer might charge an additional fee of \$25 or more. Tax preparation companies such as H&R Block and Jackson Hewitt all offer some version of the RAC.
- **Personal loans not tied to a tax refund:** Some tax preparation companies will offer a personal loan, based off your credit, not the size of your refund. These small, short term loans carry high fees and annual percentage charges.
- **Non-bank refund anticipation loans:** Lenders other than banks such as consumer finance companies are still legally allowed to make refund anticipation loans, and they are often riskier and more expensive than the traditional refund anticipation loans.

How can I avoid these services and products?

- **Be wary of unsolicited offers:** Loans offers through the mail, telephone, email or social media, or door-to-door solicitations are generally disreputable. Any lender you work with should be licensed.
- **Avoid overpromises:** Avoid lenders who promise to grant loans regardless of credit history.
- **Take your time:** Don't rush into signing anything, and never sign anything you don't understand. It's also a good idea to have a friend or lawyer check the paperwork as well. Never sign any documents that have blank spaces.
- **Say no to extras:** Decline additional, unnecessary services that are tacked onto the loan such as credit insurance.
- **Ask for a list of fees in writing:** Lenders should be willing and able to explain their costs to you and give you an estimate of the costs before you apply.
- **Steer clear of the "quick fix":** In general, avoid high cost, short term loans. Dipping into an emergency fund or even putting it on a credit card is a far better option.

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- **Do your research:** Unfair interest rates and prices are easy to weed out if you have done some research and shopped around. Also check to see if there are consumer complaints against the company offering you the product.
- **Talk to your financial coach:** Reach out to your coach if you suspect a service may be predatory or “too good to be true.”

What can I do if I've already used one of these services?

A first step is to determine if the loan or product is illegal in your state, or whether your state is already taking action against the company that offered you the product. The consumer affairs division of your state's Attorney General's Office should have this information. Do not repay a loan that is illegal in your state. Instead, speak with your financial coach about other steps you can take.

If the loan or product is legal, your best option is to pay off your loan as quickly as you can, or if possible, refinance with fairer terms. This will help to reduce the big financing charges associated with many of these products.

Sources:

- <https://www.debt.org/credit/predatory-lending/>
- <http://responsiblelending.org/issues/auto-loans/auto-loans-problem>
- <http://consumer-law.lawyers.com/consumer-contracts/problems-with-rent-a-center.html>