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The high costs of payday and title lending in Alabama

How much should people have to pay for financial help in a tight spot? Payday lending and auto title lending are two forms of high-cost credit marketed toward Alabamians who are desperate for short-term cash. These loans carry triple-digit interest rates that can threaten the financial well-being of borrowers who fall behind on payments.

Alabama law allows payday lenders to charge annual interest rates (APR) of up to 456 percent APR and allows auto title lenders to charge up to 300 percent APR. These rates are many times higher than those charged by the typical credit card issuer. They are also far above the 36 percent APR cap that Alabama's Small Loan Act applies to other small, short-term loans.

Payday and auto title loans often result in repeat borrowing and multiple loan renewals. The average American payday borrower has nine transactions per year, according to the Center for Responsible Lending (CRL), while the average title loan customer renews the loan eight times. Title loans carry the additional risk that the lender could repossess the vehicle, leaving borrowers stranded and unable to get to work to provide for their families or pay off other debts.

These lenders say they provide a needed service for low-income people, but many states disagree. Twenty-two states, including Arkansas, Georgia and North Carolina, have placed substantial restrictions on payday loans. About three in five states have outlawed high-cost auto title loans, according to CRL. In 2006, Congress capped interest rates on such loans at 36 percent APR for active-duty military members and their families.

High-cost lending can hurt borrowers, but it also can affect people who have never set foot in a payday or title loan shop. Every dollar spent repaying payday loan interest takes nearly $2 out of the overall economy through reduced consumer spending and increased bankruptcies, according to a recent study by the Insight Center for Community Economic Development. The study calculated that payday lending cost Alabama $47 million – and 697 jobs – in 2011.

Public pressure is making a difference. A bipartisan coalition has pushed the issue to the forefront. Dozens of Alabama cities have imposed moratoriums on issuing business licenses to new payday or title lenders. The state Banking Department issued regulations in 2013 to require use of a common payday loan database, ensuring borrowers don't take out more than $500 in payday loans at any one time. The database will not cover title lenders, which are governed under a different law. New federal regulations also are expected to address, but not solve, the problem.

BOTTOM LINE: Setting more reasonable interest rate limits on consumer loans in Alabama would help ensure that low-income borrowers can afford to repay what they owe.