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DELIVERED via e-mail attachment to: consumerpolicy@ontario.ca

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Consumer Policy and Liaison Branch
Ministry of Government and Consumer Services
777 Bay St, 5th Floor
Toronto, ON M7A 2J3

Dear Sirs:

RE: Consumer Financial Protection Consultations

We are responding to questions posed in the discussion paper, “Strengthening Consumer Financial Protections”. As one of Ontario’s largest personal insolvency firms, we see firsthand the impact that alternative financing has on indebted consumers in Ontario. We attended the public consultation held July 20, 2015 at the Evergreen Seniors Centre in Guelph, Ontario and have received the Ministry’s summary of items presented at that meeting. The purpose of this letter is to expand on some of those ideas and to continue our dialogue with Ministry staff.

In addition to our response, we have included a copy of our [2015 Joe Debtor whitepaper](#) for your use. Every two years we compile data pertaining to debt levels, types of debt and at-risk demographics for filing insolvency. A significant portion of our recent findings highlighted alarming trends on the use of payday loans and other alternative financial services. We believe you will find our analysis helpful during your deliberations.

If you have any questions or would like further information about our answers to your questions or our findings, please contact the undersigned. Thank you for the opportunity to participate in this process.

Yours truly,

T.A. Michalos, CPA Trustee
Hoyes, Michalos & Associates Inc.

Consumer Financial Protection Consultations

As licensed insolvency professionals we meet with clients every day struggling to repay high interest loans. For those facing financial difficulty, payday loans have the perception of offering stability between paycheques as they are marketed as an accessible, easy solution to make ends meet. However, these loans come with high interest rates that prove costly, perpetuating a debt cycle that is difficult to break. Below we offer our first hand perspective about the payday loan industry, identify factors driving debtors to use alternative financial services and offer ideas for regulating lenders that will better balance the needs of consumers. As supporting material, we have also attached our 2015 whitepaper titled, "[Joe Debtor: Marginalized by Debt](#)", which outlines our research about the types of debt that people are incurring, including payday loans, as well as specific data relating to key local demographics.

The Need for Consumer Financial Protection

1. What can you tell us about the risks faced by consumers using alternative financial services or with debts in collections?

The greatest risk to consumers using alternative financial services (hereinafter referred to as AFS) is their inability to break the cycle of borrowing. All AFS products come with high interest costs that often makes repayment difficult for those experiencing financial difficulty. Consumers initially use these services because of an immediate need, and it is not clear that adequate consideration is given to how the debt will be repaid or the impact the cost will have on their finances. When one loan cannot be repaid or creates another cash flow shortage, it is common for debtors to take out a second loan from a different lender to repay the first; thus perpetuating a debt cycle. The cycle of borrowing diverts an ever increasing portion of the individual's income to service these very expensive short-term obligations.

The risk to a consumer with debts in collections is a lack of familiarity with the laws already in place that are designed to protect them. Consumers are often intimidated by collectors, not necessarily by anything the collectors do (although there are a number of overly aggressive collectors in the marketplace), but rather, by the pure fact that they have become delinquent on their debts. They feel they have done something "wrong" and may not be able to deal with the problem. Debt in collections is a symptom of a larger financial problem that many people find overwhelming. Debt collection agencies are not the appropriate avenue to deal with these wider issues.

2. What do you think is driving the use of alternative financial services?

Accessibility, convenience and public perception. AFS have always existed in one form or another within our economy. Before payday lending businesses and internet loans, there was "the guy" at work that would lend you money until your next payday. What is different now is that the services are being mass marketed quite aggressively to consumers with little choice or little education about alternatives. People who in the past might not have

considered using AFS, are now hyperaware of these products and are turning to them in a time of financial need. It is a common misconception that the primary users of AFS are the lowest income earners in our society. The truth is that the heaviest users are employed middle class citizens. The commercialized lending industry lures consumers with quick and easy access to money, the convenience of location and hours, and the friendly attitude towards lending. It is much easier and quicker for many consumers to obtain a payday loan or installment loan than it is to apply for a line of credit or loan at a bank. The expansion of AFS into the internet makes this process faster and easier than ever before.

Of equal importance is the fact that those using AFS may not qualify for traditional financial services. Our analysis shows that the people that owed the highest AFS debts typically have significantly lower total debts, including credit cards, bank loans and lines of credit. These individuals are using AFS because the mainstream financial services industry cannot/are not/will not provide them with access to credit. Capacity is not a lending criteria for AFS lenders. At such high rates they can afford to absorb significant loan losses. Given the short-term nature of the credit, the more they lend, the more they make. I was told as a child, “If a bank won’t lend you any money, then you shouldn’t be borrowing”. The rule still holds true, but now AFS make it very easy to break that rule.

What alternative financial services should be considered for legislative / regulatory reform? Which services are adequately regulated today?

It appears that currently there is a legislative “gap” between the Criminal Code and usury laws, as well as some of the existing consumer protection laws in regards to allowable interest charges. The most effective statutory changes should occur at the federal level. AFS products should be explicitly included in any laws that set out allowable interest and other charges.

We also suggest a regulatory framework that requires and enhances the level of disclosure of the true costs of using AFS products in any/all marketing materials. Rather than legislate the products out of existence (which might simply drive them back to the shop floor), it would be more productive to educate the public of the true costs of using these services. The most effective way to do this will be before or at the point of purchase. Clear disclosure in dollars and annualized interest rates, including any and all fees, is preferable to simply saying \$21 interest on \$100. Unfortunately, consumers interpret this to mean 21% interest, which is woefully incorrect.

In regards to debt collections, it is not clear that third party collection agencies always comply with the existing regulations. Many of the individuals we deal with state that they were not notified that a debt had been assigned to a third party until the collectors started calling. When collectors do call, many fail to adequately disclose who they are, under what authority they are calling, and what the debtor’s options are to deal with the debt. It doesn’t

help that many agencies rely upon computerized “demon dialers” that continually redial a debtor’s number until a person answers. Our understanding of the current state of the law is that unless the actual debtor answers the call and speaks with a collector, it does not constitute a call, and therefore, is not covered by existing harassment laws. These unanswered calls create more stress and discomfort than the underlying debt. A balance needs to be established that limits the number of redials in a given period of time versus the collectors needs to reach the debtors.

Proposals

1.1 Which alternative financial services do you think require specific regulation in Ontario?

Are general consumer protection rules that cover all services sufficient?

1.2 What kinds of additional protections are needed?

The challenge for Ontario, and all legislative bodies is to stay ahead (or at least abreast) of new AFS as they come into the market. For example, the most dramatic growth in the AFS sector in the last few years has been for short-term installment loans. These types of loans are for larger amounts than a typical payday loan and are designed to be repaid over an extended period of time (months as opposed to weeks). It is not clear which, if any, regulations these products are subject to. In our experience, the users of these types of AFS are also carrying significant payday loan balances. Intuitively, one might think that the longer term loans were designed to replace payday borrowing – when in fact, they are evolving as a supplement, increasing the total debt load of borrowers.

General consumer protection rules are not sufficient to protect consumers from these new AFS products as the existing laws were not written with a goal of providing future protection. It is very difficult to write legislation that is sufficiently robust to deal with unknown future developments in the marketplace. Having said that, some form of all-encompassing protection, or at least a methodology for bringing new products and services under existing legislative protections needs to be developed.

Additional protections in the form of licensing of both businesses and employees for specific AFS products, as well as enhanced disclosure requirements would be beneficial.

Some consideration should be given to the role of credit reporting in the use of AFS. There is a common misconception that the credit reporting agencies are not-for-profit or government agencies, which we know is incorrect. If AFS businesses were required to report all lending activities to the major credit reporting bureaus and to review a person’s credit report before advancing any loans, the use of AFS products might drop significantly. AFS products are often the final straw for consumers, to the detriment of all of the individual’s creditors.

2.1 Should Ontario regulate the cost of some alternative financial services? Why?

In the absence of clear federal regulations that deal with the allowable interest and other charges that AFS are permitted consumers, the province should provide clear regulations for this industry. By the Ministry's own calculations, payday lenders are charging in excess of 500% interest on an annualized basis, while usury is defined as interest in excess of 60%.

2.2 Would reducing access to these services help or harm consumers? Why?

The real difficulty with these products and services is there is a definite "need" in the marketplace. As previously stated, there have always been individuals that require short-term loans and have been willing to pay a premium for immediate access to cash. As a society, are we better off having these transactions conducted in the "clear light of day" as opposed to back room dealings with less savoury characters?

An interesting response to this need might be to allow mainstream financial institutions access to this market. We don't know if there are regulatory reasons why a schedule A bank can't offer short term micro-loans. An argument could be made that overdraft protection provides this service, but in our experience, users of AFS products often do not have access to mainstream financial services. It should be noted that although overdraft protection is expensive, relative to other financial products, the cost of using overdraft is quite reasonable in comparison to AFS products.

Payday Lending

3.1 How would you describe the impact of payday lending on individuals and on communities?

Initially, payday lending satisfies an immediate need for cash. Unfortunately, it creates a cycle of borrowing that most individuals cannot break. Like any short-term solution, the underlying problem still exists and in fact, a payday loan exacerbates financial difficulties in that the cost of payday loans increases a household's cash shortfall, resulting in more borrowing.

3.2 What other alternatives exist for persons using payday loans?

You would think that individuals would turn to lines of credit, cash advances on credit cards, overdraft protection and other financial products available from traditional financial institutions, but for various reasons, AFS users do not and quite often, cannot. In some cases it is because they have exhausted their access to these products, in many others, it is because the consumer didn't qualify (or didn't think they would qualify) for these products.

3.3 What does a better alternative look like? Could it succeed if it was in competition with payday lending?

3.4 Are there similar consumer protection concerns with potential substitutes?

3.5 Are there other fundamental changes that should be made to how the industry operates in Ontario or regional differences in the need for the industry?

The underlying concept behind all AFS products is a need for immediate access to funds. The various forms of AFS may be evolving, but the basic features remain the same: easy access to money, convenience and a friendly and an unthreatening attitude towards lending. For any type of alternative to truly compete with AFS they would have to directly respond to these features. It is unlikely that traditional financial institutions will do so.

4.1 Are these the right factors for a review of the maximum total cost of borrowing? Should some be dropped or modified? Are there missing factors?

The total cost of borrowing should be inclusive of any/all fees paid by the consumer, including the additional costs that may be added in a default situation. In the absence of regulation, the market would likely allow interest and other charges significantly higher than current rates. Similarly, if regulatory changes were made, effectively reducing rates and administrative fees, most lenders would continue to operate – AFS products are highly profitable.

5.1 Should the Act restrict borrowers from seeking simultaneous loans from multiple payday lenders?

5.2 Would a central tracking system strengthen protections for payday borrowers? What would the impact be on the payday lending industry?

As previously suggested, there may be a role for Canada's existing credit reporting agencies to become involved in this process. It has been estimated, based on jurisdictions that have implemented payday lending tracking systems that the cost per loan is approximately \$1.50 (this is the figure used by Ministry staff during public consultations). Rather than create a new system, we expect the credit reporting agencies could provide a similar service at these rates. If a consumer's credit report was accessed before new loans were approved, regulations could be created, limiting access to credit based current levels of debt. For example, total payday lending could be limited to the equivalent of 50% of a consumer's last paycheque. If current borrowing disclosed on the report exceeds that amount, no new loan would be advanced. Similarly, if the intent was to restrict the frequency of borrowing, the report would display the consumer's borrowing history. The real advantage of using the existing credit reporting system is that it provides easy access to a more complete picture of an individual's financial situation. Simple ratios and analytical tools could be created directing the consumer to different levels of financial education and/or assistance. The only concern, as previously stated, is that there is a real need for these services and a balance must be struck so that they are not driven underground.

6.1 Should payday lenders be required to limit how much they lend to reflect borrowers' circumstances?

6.2 Is a proportion of net income an appropriate means of restricting the amount lent?

6.3 If general lending standards are set, what should they consider (e.g., rent, groceries, utilities)?

Presumably lenders are able to determine how much they can safely lend consumers without dramatically increasing the risk of default. Certainly, reporting payday lending and referring to a person's credit report would provide lenders with a much clearer picture of an individual's ability to repay their debts. It might make sense to add a simple budget calculation to lending documents that requires a consumer to demonstrate how a payday loan is to be repaid, without simply relying on a revolving loan.

7.1 Should Ontario rely only on a waiting period between payday loans? If so, how long?

In the absence of some form of tracking system, restrictions between loans may be unenforceable. If a consumer cannot borrow from lender A they will simply go down the street to lender B.

8.1 Should there be a restriction on the number of payday loans a borrower can take out in the year?

Similarly, in the absence of a tracking system this may be unenforceable. As opposed to restricting the number or frequency, perhaps with every subsequent loan from a lender, the total interest and other charges already paid should be disclosed, along with the current charges. Perhaps, by showing the cumulative cost, the consumer will decide to borrow less. Similarly, when an initial loan is taken out, the lender could be required to disclose a projected total cost if the loan is simply rolled over. We assume the industry has statistics on how often loans are rolled over, so an accurate prediction of the total cost of borrowing could be disclosed.

9.1 Should payday lenders be required to provide an extended payment plan to frequent borrowers?

9.2 If yes, when should an extended payment plan be required (e.g., when the borrower has received more than X number of loans in Y number of periods)? Why?

One suggestion that we have heard is to require each subsequent loan from the same lender to be at a declining cost so that after a certain number of loans, the interest might become nominal. This suggestion is predicated on the assumption that the lender would be required to continue to lend at the lower rates. If they were not, they would simply refuse to renew a loan, forcing the individual to another lender that would start at the new loan, at higher rates.

You could argue that the new internet based installment loans were designed to provide this very service. They are larger loans with repayment terms over months instead of weeks. What we have observed is that this is the fastest growing segment of AFS products, and three quarters of the individuals that we meet with who have these types of loans, also have payday loans. The new product has simply increased total indebtedness, not relieved any pressure. If credit reporting rules were introduced for payday lenders they should also be introduced for all other forms of AFS borrowing.

10.1 Should Ontario control the total cost of defaulting on loans?

Definitely. As previously suggested, consumers should be provided with the costs of defaulting in clear, easily understood language, at the time of borrowing. An argument can be made that the reason AFS products have such high interest and other charges is the inherent risk of default. To not restrict the additional costs that may be added when an actual default occurs, seems unfair. Default charges should be included in the total cost of borrowing and subject to the same restrictions as other charges and interest on the account.

11.1 Would you add anything to the information that currently must be provided?

11.2 Is too much information currently being provided?

We suggest adding two additional pieces of information in a clear, easy to understand format: the projected cost of borrowing in real dollars, as well as an annualized interest rate, and the total cost of borrowing in the event of a default. The first requirement would provide the borrower with a more realistic total cost of borrowing. Rather than saying the \$300 loan will cost \$63 in two weeks, it would say, most people re-borrow three times (as an example), so the projected cost of borrowing is \$189. The second would emphasize the consequences of defaulting on the debt.

12.1 Do you think information could be provided more effectively to consumers?

12.2 Are fewer words and more information graphics preferred?

Keep in mind that very early in our comments we advised that there is a misconception as to who is using AFS products and services. The heaviest users are the middle class. That does not mean they would not benefit from a simplified presentation, but it is important not to focus on the needs of the less-sophisticated members of our society.

13.1 Do promotional rates create risks for consumers?

13.2 If promotional rates create risk, what is the appropriate means to reduce this risk?

If we agree that the vast majority of AFS users enter into a cycle of debt, then promotional rates should not be permitted at any time. Frankly, promotional loans are the equivalent to a drug dealer handing out free samples in a school yard. No more needs to be said.

14.1 Should payday lenders be permitted to buy gift cards from consumers? If not, why?

14.2 Should payday lenders be restricted in the types of services they can offer?

14.3 Are consumers better served by having fewer services at an alternative financial service provider like a payday lender?

14.4 Is a gift card purchase different from purchasing gold, money transfer, and other services offered by some payday lenders? Do all services offered by payday lenders require additional scrutiny because their clients are likely under financial strain?

14.5 Should payday lenders be under an obligation to provide the regulator with advance notice of other services they propose to offer? Should their ability to provide other services be subject to approval?

As long as there is appropriate disclosure of the costs associated with any of these services and the businesses and employees are properly trained and licensed to provide these services, we are inclined to allow the market to decide what an AFS business should or should not do. Using gift cards as an example: if the card was purchased from a retailer, then the retailer is obliged to simply “cash the card” – if the consumer is made aware of this fact and still wants to sell it to a payday lender at a discount, then so be it. We would hope that if they are properly informed they would not, but we suspect they still will...

15.1 How would consumers be affected by amending the legislation to permit a delay in making the loan available in online payday transactions?

One of the most attractive features of payday borrowing is the immediate access to cash. If that access was delayed, borrowing would likely decline. If you believe online borrowing is often done on impulse, then a delay might prove a useful deterrent.

16.1 Should Ontario’s inspection authorities under the Payday Loans Act be expanded to include unlicensed payday lenders and loan brokers?

Based on the way this question is phrased, we assume that the authorities do not currently exist. If this is true, it is very troubling. If payday and other AFS regulations are tightened, we expect the unlicensed (underground) industry will increase. The only way to address that increase will be to bring them into the regulatory umbrella, at the very least by including them in any inspection regimen.

Remittances

Our practice is not involved with, or exposed to, the types of transactions this section deals with. As such we will not be responding to questions 17.1 to 18.1.

Debt Collection

19.1 Do you agree with the proposed expansion of the CDSAA to include any person who has purchased a debt or debts that is or are in arrears?

19.2 What additional exemptions may be required to avoid capturing situations that arise in the course of various normal business transactions? Would the following be sufficient?

- A business that purchases a debt or debts through acquiring or merging with a business in a transaction that includes the transfer of accounts receivable,**
- A business that enters contracts and then assigns rights to payments under them to a third party, when it continues to collect payments on behalf of that third party,**
- A business that acts as a billing service through which third parties bill for goods or services provided (e.g., as is done on the Enbridge billing service and by many wireless suppliers),**
- A business that acquires a debt or debts through the seizure of accounts receivable under a security agreement, or**
- A person to whom the contract that gave rise to the debt was assigned for the purpose of financing the transaction.**

19.3 What provisions of the CDSAA regulation should be adjusted if the proposed amendment is made?

We agree that any subsequent purchaser of the debt or the rights to collect on the debt should be disclosed to the borrower. In fact, all of the items listed as possible exemptions should also be disclosed to the borrower to avoid confusion and ensure transparency.

20.1 Do you agree with the proposal to adjust the timing and content of initial notices?

20.2 Do you have suggestions for the information that would be useful for debtors to receive in initial notices?

We agree with the proposed changes, but caution that collectors must restrict the content of the initial contact to verification and authority as to the form of future contact. Collectors should be prohibited from commencing any collection action during this first contact. We suspect that this may be difficult to enforce.

21.1 Do you agree with the proposal debtors be able, at some point, to require contact continue only in writing?

21.2 What period of time or number of verbal contacts should be given before invoking this requirement, in order to give collection agencies a reasonable opportunity to engage in negotiation?

We are under the impression that under current regulations, this right already exists. Perhaps we are mistaken. Our greatest concern is with the use of electronic dialers and the frequency of those calls. These unanswered calls cause more stress and anxiety than any other form of contact between a collector and the consumer. Limiting the frequency of these calls would greatly reduce the number of complaints the Ministry receives about collection practices.

Other Matters Worthy of Consideration

In addition to the questions posed in your paper, we would like to suggest two other areas that are worthy of consideration and review. The first involves something we call debt consultants. These are individuals and businesses that charge fees to provide financial advice (regarding debts) to the public. The industry appears to be unregulated and a significant portion of their work consists of charging individuals a fee and then referring them to a licensed trustee in bankruptcy to file a consumer proposal. Debt consultants are particularly active in the immigrant and other at-risk communities. Their pitch is to offer to reduce debts by up to 70% while avoiding bankruptcy. That much is true, but in order to obtain this relief a person must file a consumer proposal with a licensed trustee. Trustees provide this same information for free, so it is troubling that consumers are being charged a fee for free information.

The second involves credit repair. Very recently we have discovered businesses that offer to repair an individual's credit by lending them money, which they hold as collateral, to establish a payment history. A typical example might be a loan of \$1000, repayable at the rate of \$100 per month for 15 months. At the end of the 15 months, the \$1,000, which was held as collateral, will be returned to the consumer. Effectively, the consumer paid \$500 for the service. What is frustrating about these types of transactions is that a \$1,000 loan is insufficient to rebuild an individual's credit history and 15 months of payments are insufficient to establish a pattern of responsible borrowing.

We will be pleased to expand upon either of these other matters, or any of our responses to your questions should you be so inclined. Thank you for the opportunity to share our opinions and insight into this matter.