

Lending with grace: Breaking the cycle of payday loans

by [Jesse James DeConto](#) in the [June 27, 2012](#) issue



Often when something goes wrong—when a child gets sick or a car breaks down—people need extra money fast. As former Pittsburgh cop Tony Wiles knows, people who need money fast are vulnerable.

“I grew up in the inner city, so I’ve seen it all,” he said. “Loan sharks, pawnshops and payday loan companies on every corner.”

Wiles hadn't considered doing anything about the issue until Rock Dillaman, his pastor at Allegheny Center Alliance Church, preached a sermon on justice. The pastor planted a seed that led Wiles to develop a low-cost payday lender called Grace Period.

Grace Period is an alternative to the typical payday advance or check cashing service, which charges a flat fee for a small loan that's due when a customer receives his or her next paycheck. For example, a borrower of \$300 might need to repay \$345 at the end of two weeks.

If the financial transaction ended there, these payday lenders would not have earned the label "predator." But many clients' next paychecks have to go for rent and utilities, so they can't pay the loan back when it's due, and the lenders exact fees at a rate equivalent to an annual rate of 300 to 800 percent.

"The average loan gets rolled seven times before it gets paid back," said Dan Krebs, CEO of Grace Period and a former auto dealer who teamed up with Wiles four years ago.

In a two-year study surveying about 11,000 payday borrowers, the Center for Responsible Lending found that the average borrower was in debt for 372 days. Nearly half of the borrowers defaulted, and the typical \$300 loan ballooned to \$466 before it was repaid.

Krebs and Wiles decided to offer an alternative to this cycle. They began talks with Pittsburgh Central Federal Credit Union about a partnership.

"No mainstream organization is helping [the borrowers]," said Krebs. "The idea was for the church to create a credit union. The mission was to bank the unbanked."

Grace Period offers free loans for clients who repay them within 13 days, and it requires a long-term savings program so clients can meet their emergency needs in the future.

"We have people who are actually saving money for the first time in their lives," said Wiles, who is Grace Period's board president. "They look at these programs as a savior."

Lisa Dukes-Garner, a mother of four, knows how suddenly financial crisis can arrive. In fall 2008, her husband died of a heart attack. "Duane always took care of every

little thing about my vehicle,” she said. “When I lost Duane, I started having all these issues with my car.”

Dukes-Garner needed money to rent a car while hers was in the shop so that she could get her youngest son to day care and herself to work. She didn’t know where to turn.

“I’ve never had to ask anybody for anything. People always came to me asking me for something,” she says. “Where was I going to get the money?”

A friend told her about Grace Period. She was able to borrow money for car repairs, rent, groceries and her teenage son’s braces.

Her family had been getting by on her salary as a community AIDS educator and her husband’s salary as a substance-abuse counselor. But now, with household income cut in half, Dukes-Garner worries about every financial detail, including how much spending money to send her son in college. In between paychecks, she sometimes visits food pantries.

“At times I’m really, really low on food,” she says. “I’m not a very prideful person to where I won’t access secondhand stores. I never realized how hard it is, especially when it’s just you trying to take care of everything.”

Because Grace Period automatically withdraws \$100 from her \$900 in take-home pay every two weeks, Dukes-Garner recently paid off all her loans and saved enough so that her next loan will come out of her own account. She’s learned to live on the remaining \$400 a week, so her Grace Period emergency fund was an unexpected blessing.

“I thought that everything that came out of my account was just paying for what I had borrowed,” she said. “You mean I have money sitting there that I didn’t even know was there? That is a beautiful thing. The money that they do take every month is saved for me.”

Credit unions were formed with the goal of offering savings and loan programs to low-income families. Grace Period is not the first faith-based credit union to respond to payday lending. In 1999, Faith Community Credit Union in Cleveland began offering a “grace loan” for borrowers who might otherwise use a payday lender. The emergency loan has lower fees and interest rates and a \$500 monthly credit limit. It

requires proof of employment and \$10 a month in savings. Other faith-based agencies have partnered with local credit unions to offer substitute payday loans. Mission: St. Louis created the Change for Good lending program with Choices Federal Credit Union. The Virginia United Methodist Credit Union offers small short-term loans through its Jubilee Assistance Fund.

“It’s really valuable to have a model of what Christian business can look like,” said Rachel Anderson, faith-based program director at the Center for Responsible Lending.

Grace Period doesn’t make direct loans; it serves as a guarantor, promising to repay Pittsburgh Central Federal Credit Union if a borrower can’t. The agency also funnels the monthly electronic transfers into customers’ credit-union accounts and lends out members’ money to other members in a cooperative format. The Alliance Church brought \$100,000 of its own money to Grace Period, as well as dozens of new credit union customers with another \$850,000 in assets that help offset the costs of the loans to penniless borrowers.

“The loans themselves barely pay for the person who’s processing them,” says Krebs. “Loans don’t make money.”

The initial payday loans are made at 18 percent interest, with \$12-a-week dues paid if the loans are not repaid within two weeks; the rate drops below 6 percent once the original credit union loan is paid off and clients start borrowing from other Grace Period cooperative members. Those fees support seven employees. Because the loans are so small, Grace Period sees no profit. Once Grace Period starts lending borrowers money from their individual accounts, they can earn that money back at \$4 a week—much like getting interest on a bank account.

The founders of Grace Period aim to show that the model is sustainable. “Unless it’s self-supporting, nobody’s going to duplicate it,” said Krebs.

Grace Period presented its model at the past two conferences of the Christian Community Development Association, and the agency is encouraging alternative payday lending, which is taking root across the country. The founders of Just Money Advisors, a nonprofit financial planner with clients in 25 states, are working to open another Grace Period in Louisville, Kentucky. The Louisville group plans to team up with the LouChem Federal Credit Union to open its first storefront in 2012 and half a dozen more locations in the coming years.

The key to success is requiring a yearlong commitment to direct deposit savings if a customer doesn't pay off the initial debt within the first two weeks. The direct deposit requirement not only forces people to save but also shields Grace Period from having to handle cash in crime-ridden neighborhoods where payday lenders proliferate.

"That part is genius," said Just Money executive Andy Loving, a Baptist minister turned socially responsible investment adviser. "We know that money habits die hard. To think that you're going to be able to give people a better choice and they're going to stop digging a hole for themselves is just not realistic. After eight or nine months of this, a light begins to go on."

"Here in Louisville, there are more payday loan stores than there are McDonalds, Starbucks and KFCs combined," Loving said. "The church is always going to have to be in that place of helping folks in emergencies, and there's nothing wrong with that. But when we have the capability and the capacity of moving past that, we should be doing it. This is not rocket science."

Dillaman, the pastor at Allegheny Center Alliance Church, came to Allegheny Center in the 1980s, when most white churches were moving out of Northside. He decided to move into the neighborhood and convinced the congregation to stay. At the time, the 400-member congregation had only one African-American member, while the neighborhood was 60 percent black; after decades of growth the church now has about 1,000 black members.

Alliance has initiated other community development efforts: Urban Impact offers nighttime and weekend youth activities, like tutoring, sports and the arts; Bistro to Go employs 30 people in the neighborhood center. The church spent \$200,000 to buy a bar that was attracting crime to the neighborhood, and it plans to redevelop the site. Two physicians at the church helped found the Northside Christian Health Center for low-cost medical care.

"We made a commitment to stay here and embrace a more holistic and, I think, a more biblically faithful approach to ministry," says Dillaman.

The church also gives about \$200,000 a year in direct financial assistance to neighbors in need. CRL's Anderson said churches' efforts can help wean people off payday lenders, but the situation also calls for political action to cap interest rates. Payday lending is thriving in states where the industry has been able to weaken

antiusury laws. Most states allow fees of 10 to 20 percent over a two- to four-week loan period, which can quadruple principal loan amounts over a year's time. Connecticut, Delaware, Idaho, Maine, Nevada, New Jersey, New York, Oregon, South Dakota, Utah, Vermont and Wisconsin currently have no limits on payday loan fees. Opponents have fought back and succeeded in prohibiting triple-digit interest rates in 17 states, including Montana, where a voters' referendum recently set a 36 percent interest rate cap after the Conference of Catholic Bishops and the United Church of Christ organized in support of the cap.

Anderson also cited the Industrial Areas Foundation's 10 Percent Is Enough campaign, which has been lobbying for a cap on the federal credit card rate (see ["The people's interest,"](#) *Christian Century*, January 12, 2010). Similar movements are under way in Missouri, Mississippi, Louisiana, New Hampshire and Alabama.

"It's knit into the teaching of many faiths that using a loan to exploit someone is not just abusive but immoral. Payday lending is a modern-day form of usury," Anderson says. "We need good regulations to work hand-in-hand with good business."

Loving insists that churches and ecumenical service agencies must add alternative payday loans to their ministries. The mainstream cash-advance industry generates tens of billions of dollars in revenue each year on the backs of desperate people, and right now there are few alternatives.

"We're not putting them out of business any time soon," Loving noted.

Four years into Grace Period's existence, its backers in the Alliance congregation have increased their assets at the credit union to more than \$1 million—and that's not counting 3,000 Grace Period borrowers who have begun to save. The credit union loaned \$1.5 million to Grace Period clients in 2010, and more than \$11,000 a month comes from customers' own savings accounts.

"The whole idea is to get people to the point where they're using their own money," said Krebs. "Things happen. It's not luck. My car breaks too. Everybody's car breaks. You've got to have a plan."

Realistically, said Krebs, Grace Period for most clients simply offers a cheaper loan than they might get at a place like Advance America. Encouraging personal financial reform is a much greater challenge. In fact, Grace Period has found that only about 3 percent of clients actually reform their financial habits. Others continue to pay giant

interest rates for rent-to-own furniture or huge fees for early refunds offered through tax preparation franchises.

“I give everybody an opportunity to benefit completely, and whether they choose to do it, I can’t control,” said Krebs. “Sometimes you get somebody who took this little thing and applied it to more parts of their lives.” But even with its limited impact, Grace Period is keeping customers out of the cycle of predatory lending. Said Krebs: “We’re keeping people from going to places that are really going to take advantage of them.”