



## Know dangers of quick cash

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Last week, we learned that it is OK to borrow money to fund a "good debt" purchase like a college education, a home or a business venture. We also learned that the best places in which to obtain these loans are banks and credit unions.

Yet there are other institutions that will lend you money that do not have your best interest in mind. The most common type of loan you will want to avoid at all cost is a payday loan. Also called a cash advance loan, a payday loan is given to borrowers when they need a small amount of money to cover expenses until they receive their next paycheck. Once they receive their next paycheck, the payday loan plus a more-often-than-not high fee must be repaid.

One trip to a payday lender can cost you more than you think, with the average payday borrower shelling out \$800 to borrow \$325.

Many of the people who can least afford this expense make the mistake of frequenting these establishments and taking out these expensive and high-risk loans. Below is more information about payday loans and other debt traps you will want to avoid:

■ **Payday loan stores** that allow a borrower to take out quick cash for an upfront finance fee. The lender gives you a small cash loan which is due in full when you receive your next paycheck (usually a two-week term). The borrower gives the lender a check for the price of the loan plus the finance fee. If the borrower does not pay back the loan in full, the payday lender will cash that check. And if that check bounces due to the borrower not having sufficient funds in his or her checking account, the borrower will also have to pay a bounced check fee on top of the loan's finance fees. And these finance fees typically range from 15 to 30 percent of the



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Avoid debt traps like payday loan shops.

### KEY POINTS

- You will want to avoid taking out a payday loan at all costs. Also known as a cash advance loan, a payday loan is given to borrowers when they need a small amount of money to cover expenses until they receive their next paycheck. Once they receive their next paycheck, the payday loan plus a more-often-than-not very high fee must be repaid.
- In addition to payday lenders, some of the other debt traps you will want to avoid include refund anticipation loans (RALs), pawnshops, title pawn lending, rent-to-own stores and buy here/pay here car financing. In each of these examples, what begins as one trip to get quick cash or access to something you wish to own can quickly put you in a debt trap or lead to the repossession of some of your most prized possessions.
- The best way to avoid entering into these expensive and risky loans and financing arrangements is to prepare a budget that details how you will cover your monthly expenses and to stash at least six months' pay into an emergency fund.

amount for the two-week period, which translates to rates ranging from 390 to 780 percent when expressed as an annual percentage rate (APR).

■ **Refund anticipation loans (RALs)** are short-term loans secured by a taxpayer's expected tax refund. RALs are offered by tax preparation outlets and they give customers instant access to tax refunds instead of waiting for

a tax refund to arrive by check in the mail. Like loans from payday loan stores, RALs come with sky-high interest rates.

■ **Pawnshops** offer loans by holding objects of value as collateral. The pawnbroker returns the object when the loan is repaid, usually at a high interest rate. If the borrower doesn't repay the loan by the due date, the pawnbroker sells the item.

■ **Title pawn lending** is a form of short-term lending in which instant cash loans are provided using a car title as collateral. Interest rates are usually very high (notice a pattern here?), and in many instances, lenders will repossess cars for a fraction of their value when the loan is not repaid on time.

■ **Rent-to-own (RTO)** stores rent furniture, electronics and other consumer goods for the short or the long term. The consumer can own the item after paying many times the standard retail price. Extremely high interest rates, commonly around 300 percent, are factored into the payments. If the consumer misses a payment, the item is repossessed.

■ **Buy here/pay here** is used by car dealers to finance mostly old, used cars that require a large down payment. This down payment is often equal to the car's value. Customers are then put on a biweekly payment plan to pay off the outstanding balance. If the car breaks down or the borrower cannot make the payments, the dealer repossesses the vehicle in order to sell it again.

In all these examples, what begins as one trip to get quick cash or access to something you wish to own can quickly put you in a debt trap or lead to the repossession of some of your most prized possessions.

The best way to avoid entering into these expensive and risky loans and financing arrangements is to prepare a budget that details how you will cover your monthly expenses and to stash at least six months' pay into an emergency fund. It may not be fun to save, but in the end it beats shelling out your hard-earned money to pay off outrageous interest rates or risk losing your belongings.

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## Math behind scams

Sometimes it helps to calculate the actual cost of high interest/high risk loans in order to understand just how much financial harm they may pose to you.

### Small, high-interest loans

You borrow \$500 at 24 percent interest for 12 months. Your payments are \$47.28/month.

What are your total payments assuming you pay on time with no late penalty fees? How much did you pay in interest? How much will your loan cost if you opt for a 24-month repayment period of \$26.44/month?

### Payday lenders

You write a \$550 check to a payday lender for a \$500 loan that must be repaid when your paycheck comes through in two weeks. How much money will this loan cost if you pay the entire amount in two weeks?

If you can't pay the entire amount, the lender collects the interest and agrees to flip your loan for another two weeks for an additional \$50. How much does the loan now cost you? How much will it cost if your initial

loan is flipped four times?

### Pawning your car title

You pawn your car title (\$1,000 value) to get a \$500 loan. You pay weekly installments of \$103.30 for 10 weeks. How much will this \$500 loan cost you if you make all 10 payments on time?

After eight weeks of paying on time, you miss the ninth payment and the lender takes your car. How much did this \$500 loan cost you now?

### Rent-to-own

You decide you can't live without a TV, but without cash to purchase one you visit a rent-to-own store. You agree to make 52 weekly payments of \$18 for a 19-inch color TV (\$300 if purchased at an appliance store). You will own the TV if you make all the payments on time. How much did you pay above the \$300 value? How many TVs could you have purchased for the total amount you paid?

Remember: Make a budget and stick to it so you don't end up in these debt traps.

## CAREER CORNER



Victoria Snyder

**Name:** Victoria Snyder

**Occupation:** Project Leader in the Services Technology department at GE Transportation

**Typical day:** I primarily work on projects with our Service Teams on locomotives that have been shipped to our customers and are covered by our service contracts. I work with our durability engineers, who study the locomotives' performance in the field and develop and test various ways to keep them operating at their top level to optimize customer productivity.

**To do well in this job:** A person must be good at and enjoy problem solving. They need a strong background in math and physical sciences. They also need excellent oral and written communications in order to relay technical information to various groups of people.

**Favorite part of job:** The people I work with—they are talented, smart and exceptional at what they do. They challenge me to do more than I thought I could, and I am always learning from them.

**Education:** I received a bachelor's degree in electrical engineering from Penn State-Behrend.

Circle articles in your newspaper that discuss the state of the American economy. How would you describe our current economy? Do you believe it is getting better or worse? Would you expect that more people are turning to payday lenders with the economy being in the shape it is? Legislators often consider regulating payday lenders. What would you write to your representatives about regulating this industry?



Check out these Web sites to learn more:

www.teachmeaboutmoney.org  
www.eriefcu.org/savings/financial-literacy

www.unitedwayerie.org/financial-stability  
www.goerie.com/nie

www.erie.ja.org  
www.eriebc.edu