

## **Payday Loans: Be Aware of these Dangerous Loans**

### **Easy Money Doesn't Come Free**

From Jeremy Vohwinkle, former About.com Guide

During these turbulent economic times millions of working Americans are facing, payday loans are becoming a popular source of short-term financing. This has been especially true for low-income families. Payday loans are easy to get and don't require any sort of credit check, but are they really a good idea?

A payday Loan is a small cash loan given to an individual based on the fact that the loan is expected to be repaid with their next paycheck. It's basically like getting part of your next paycheck early. The repayment period is based on how frequently you get paid. The borrower is expected to show proof of employment and a bank statement. The loan applicant then writes a post-dated check for the amount of the loan plus fees. Some states require the check to be dated for the day the borrower receives the money. Under this circumstance the borrower signs a contract stating the check will be held by the lender until the agreed date of repayment. This contract becomes necessary because many states no longer allow for a person to write a post-dated check.

On the date the loan comes due, the recipient of the loan comes into the lending store to pay the loan off. If it is not possible for the person to come into the store, the loan company can deposit the check directly into their bank. If the borrower finds they cannot repay the loan at that time, the loan may be extended which may involve additional fees. Failure to repay these loans can result in the lender threatening criminal prosecution or check fraud.

### **The Downside of Easy Money**

These loans usually carry a high price tag. Finance charges are from 15 to 30 percent of the amount being borrowed. Since it's 15 to 30 percent on just a few weeks, it's comparable to getting a loan with an annual percentage rate of nearly 800 percent.

Because payday loans are so easy to get and lack the traditional credit checks, companies often prey on lower income neighborhoods knowing they are more likely to obtain one of these loans. The down side to this is most of these people are already experiencing financial hardship and borrowing money with such a high interest rate just makes matters worse. In addition, many of these people find themselves unable to repay the loan when it comes due. This situation leads to additional bank charges for bounced checks and the cost of the loan, or they have to extend the loan causing even more fees. Many of these people trap themselves in a vicious cycle. They pay the loan off on the next payday, but discover they do not have the funds needed to cover their expenses. They then find themselves going back for another payday loan. This cycle can continue indefinitely since there is no limit on how many times a person can get this type of loan.

## Payday Loan Alternatives

There are many alternatives to getting a payday loan. The best thing you can do to avoid these types of loans is to create a budget so that you afford paying the bills. Cut out as many unnecessary purchases as possible. Put that money into a savings account. Even the loose change found around the house can be put into savings. Set a budget for groceries, cell phones and fuel consumption. This can be accomplished by only purchasing the items that are needed when in the grocery store. Look into cell plans that offer a base rate for the most frequently called numbers. When running errands, try to do as many of them in one trip as possible, to conserve fuel instead of making several trips.

Another alternative to a payday loan in the event of an unexpected expense is getting a pay advance on your paycheck from your employer. Many employers offer this to their employees in emergency situations. Employers want to keep good employees happy. While this won't always work, and you won't be able to make it a habit, if you are facing a true emergency and bring it up with your employer there's a good chance you can get some sort of financial assistance.

You may also want to consider a pawn shop. Most people have something of value that can be pawned such as old jewelry, tools and electronics that can be used as collateral for a short-term loan from the pawn shop. You get cash for your item and you can still come back and repay the loan and get your item back. If you can't repay the loan, the pawn shop keeps the item you gave them. So, you ended up basically selling your item to them. This is often a better alternative than getting an unsecured payday loan and being hit with exorbitant fees and finding yourself in a dangerous debt spiral.

While not ideal, credit card advances can also be an alternative to a payday loan. Even though interest rates are applicable with a credit card advance, it can be very helpful for a one-time emergency situation. Ideally, you'd have an emergency fund set up to cover a financial crisis, but a credit card will work in a pinch and instead of paying 700 percent APR on a payday loan you'll only be left with maybe 25 percent APR on the credit card. It's not great, but it's still better than payday loan charges.

Finally, asking friends or family for a loan to help get through a hard time is another possibility. Most people have relatives or friends who will loan them money needed to help with unforeseen expenses or emergencies. Little to no interest is usually added to these loans and arrangements can sometimes be made to pay the loan back in installments over time. Of course, the favor may be asked of you someday and money can ruin relationships, so this should also be another last resort.

<http://financialplan.about.com/od/creditdebtmanagement/a/Payday-Loans-Are-Dangerous.htm>