
With a product design and pricing structure in place you can begin to develop a business plan, policies and procedures for your new loan product. Sound lending policies are essential for all loan products and a payday-alternative loan product is no different. Equally important are descriptive procedures for staff – particularly if this product will be handled differently from traditional loan products. This section contains a sample business plan, policy guidelines, and points readers to sample policies and procedures provided by some of the credit unions included in the guide.

Business Plan
Appendix C of Payday Lending: The Credit Union Way contains a list of business plan considerations that should be addressed as part of a PDL-alternative product.

The following is a sample business plan. It is based on the loan model portrayed in the PDL Excel spreadsheet included in this guide.

Example 1 CU
Payday Alternative Loan (PAL)

Purpose: The PAL is intended to provide members with a low-cost loan option to meet short-term cash needs, reducing dependency on high cost payday loans (PDLs).

Loan Objectives:
- The product will be priced to pay all direct costs in making the loan and provide nominal income to help offset some indirect costs.
- The loan term and income criteria will be set to help make payments manageable for the borrowers.
- The underwriting criteria will limit risk to the credit union to the extent possible, while allowing those with blemished credit to obtain the loan.
- Portfolio and loss limits will be established for PALs and performance will be monitored monthly.
- Staff will be trained to provide intervention counseling to frequent users of the product.
- The overall goal of the product is to give members a safety net during periods of financial crisis, but gradually move them into more productive credit and savings habits.

Loan Parameters:
- Minimum loan amount of $100; maximum of $500
- 18% APR
- $20 application fee charged to all applicants
- Maximum term of 90 days; periodic payments will be set to coincide with the member’s payday
- No traditional credit check will be required, but a subprime credit check will be made to determine payment history, if any, with PDLs; more than one PDL outstanding is grounds for turn down.
  Note: In this situation a traditional credit check should be taken to determine if the member qualifies for a longer-term consolidation loan.
- Loan must be paid in full prior to additional advances
- A maximum of 4 PALs will be allowed in a 12-month period
- Members who receive four successive PALs will be offered intervention counseling by loan staff.
• Any limitations regarding rollovers, number of loans within a specified time period or required cooling off period (i.e., member is prohibited from getting another payday loan until a specific period of time has passed)
• After a certain number of rollovers, will loan term be expanded to help with repayment?
• Will financial education or other intervention points be required?
• Will loan include a forced savings component?
• Credit check required?
• After a certain number of loan advances and timely repayments, will member be moved into a better-priced product?

Specify how loan declines will be handled and how any application fees will be collected. Remember, an application fee, in order to be excluded from the APR calculation, must be charged to all applicants, whether approved or not.

Loan Documentation Requirements:
Specify what is required at time of initial application and with each advance. Examples include:
• Type of application
• Current ID
• Utility bill or other proof of residency
• Proof of income
• Verification of length of employment
• Type of loan note and disclosures
• References

Lending Authority:
Who has the authority to approve these loans initially and with each advance? For example, must the member always see a loan officer or will tellers be able to approve or make subsequent advances?

Loan Portfolio Limits:
Specify any limits as to the number or dollar amount of payday-alternative loans that the credit union will make. Specify any delinquency or charge-off threshold that will cause a review of the program.

Collection & Charge-off Procedures:
Specify collection activities that may be different from traditional loans. Short-term loans should require earlier and more aggressive collection practices. At what point will the loan normally be charged off?

Loans to Employees, Officials, & Family Members:
Will the approval process for payday-alternative loans to employees, officials and their family members be any different from other loans? If so, specify procedures.

Loan Committee and/or Loan Officer Documentation:
What records will be required of loan requests, both approved and declined? Will these loans be any different from other loans? If so, specify records required.

Board Policy Review:
How often will the board review this policy?
Policies & Procedures: A separate loan policy for PAL will be developed and included in our loan policy manual. Procedures for accepting and processing PAL applications will be developed and included in our employee procedures manual.

Measurements of Success:
- At least 1% of our members will use this product and find it of value to them.
- Delinquency and loan loss ratios will remain within the expected parameters.
- Based on usage assumptions, we will save our members approximately $339,000 the first year using PAL versus a payday lender.

Policies & Procedures
The following credit unions provided sample policies or procedures. These can be found in Section 3 as part of each respective credit union model:
- Wright-Patt CU – Model 1
- Northwest Community CU – Model 4
- Hershey Federal CU – Model 5
- Veridian CU – Model 6

Various model policies can also be purchased through the Credit Union National Association (CUNA). For a preview of Credit Union Model Policies: A Framework for Compliance, see: http://buy.cuna.org/download/25627_toc.pdf.

Policy Guidelines for Payday Lending follow, as does the Better Choice Sample Policy.

Policy Guidelines for Payday Lending

Note: Your policies and procedures will be based on the business model, technology and aggressive/conservative approaches of your product.

Loan Name & Type:
For example: Payday Alternative Loan (PAL), a short-term, closed-end loan

Purpose:
For example: The PAL is intended to provide members with a low-cost option to meet short-term cash needs, reducing dependency on high cost payday loans. The product fits the CU’s desire to provide members with products and services that fulfill their financial needs, while building long-term financial relationships with them.

Eligibility:
Outline who is eligible to receive this loan. Examples include:
- Age requirement
- Member in good standing
- Established member for some time period
- Checking or direct deposit requirements
- Income requirements
- Length of employment requirements
- Has not caused the credit union a loss or is not in bankruptcy

Loan Parameters:
Outline loan specifics. Examples include:
- Loan limits
- Repayment period
- Interest rate and any fees
- Acceptable methods of payment
- Any limitations as to number of outstanding payday or payday-alternative loans
Loan Underwriting Criteria:
- At least 18 years of age
- Must be a member of the credit union for 90 days
- Minimum monthly income of $1,000 gross, if employed, or $800 if receiving Social Security, disability or pension
- Proof of income must be provided
- Provide current photo ID
- No delinquent loans or negative shares > 15 days old
- Not in Chapter 13 or bankruptcy (reported through subprime credit check)
- Two references are required

PAL Portfolio Limit: The maximum aggregate amount of PALs outstanding will not exceed 3% of the credit union’s net worth, which at this time will limit outstanding PALs to $400,000.

PAL Loss Limit: The spreadsheet analysis projects a loss ratio of 2.2% of total loans made in one year. If loss ratios exceed 4%, a review of loan parameters, underwriting criteria and collection activity will be conducted.

First-Year Loan Projections: The spreadsheet analysis for the first year is attached as part of the business plan. In summary, the following assumptions were made:
- 1% of our members will use the product during the first year
- 75% of these members will consistently use the product – two to four times during the year
- The average outstanding loan amount will be $300
- Loan loss ratio as a percent of total loans made is projected to be 2.2%
- The delinquency ratio as a percent of borrowers is projected to be 12%
- Time to generate a loan is estimated at 30 minutes, given the fact it is a new product
- Collection time is estimated at 30 minutes per delinquent borrower

First-Year Loan Results:
- A total of 601 advances are expected the first year, producing total loans of $180,225
- These loans will generate $8,110 in interest income, $12,015 in application fee income, and $360 in late payment fee income
- Loan loss expenses are estimated to be $3,965
- Net income after labor, cost of funds, and loss expenses is projected to be $10,141

Collection Procedures: Because these loans are short-term in nature and are made to riskier borrowers, collection procedures will vary from our traditional loans, as follows:
- Telephone contact will be attempted when the loan is 3 days past due
- After 10 days, a late notice is mailed and late fee charged
- After 30 days, cure notice is sent
- At 45 days, the loan will generally be charged off unless collector believes borrower has intent to make arrangements for repayment

Marketing PAL: A soft launch is planned for the first year until the credit union has had some experience with volume and repayment history. The following methods are planned to inform members about PAL:
- A flyer will be mailed to members currently using PDLs as determined through ACHs and verification and collection efforts from payday lenders. The flier will notify the member of our PAL product.
- Employees will be trained to refer members to the PAL product when members appear in financial distress, have overdrawn share accounts, or are turned down for other loans.
- After 6 months of favorable experience, PAL flyers will be added to lobby displays and will be included as a loan option on our Web site.
Better Choice Sample Policy

The ________________ is designed to help ESTABLISHED members who need a small dollar loan to carry them until they receive their next regularly scheduled income check. The loan is designed for members to use instead of borrowing from a for-profit payday lender.

______________ loans are for emergency situations, and not for an ongoing solution to member liquidity issues. The credit union’s goal is to educate members on wise financial management and budgeting so that the need for such emergency loans diminishes over time.

<table>
<thead>
<tr>
<th>Initial Credit Limit</th>
<th>$250.00 will be granted to new borrowers.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Subsequent Credit Limit</td>
<td>$500.00 limits are available after a borrower completes 12 months at the $250.00 level with no repayment issues.</td>
</tr>
<tr>
<td>Interest Rate</td>
<td>Variable, set by management, and may change at any time after proper notice is provided. Currently 18%.</td>
</tr>
<tr>
<td>Interest Rate Method</td>
<td>Simple interest.</td>
</tr>
<tr>
<td>Repayment Terms</td>
<td>Advances must be paid in full within 30 days. Subsequent advances are not permitted until previous advances are repaid.</td>
</tr>
<tr>
<td>Credit Life/Disability Insurance</td>
<td>Not available.</td>
</tr>
<tr>
<td>Loan Deferments/Amendments</td>
<td>Not available.</td>
</tr>
<tr>
<td>Payment</td>
<td>By cash, payroll deduction, or automatic transfer.</td>
</tr>
<tr>
<td>Fees</td>
<td>Application fee.</td>
</tr>
</tbody>
</table>

To qualify for a ________________ loan, a Member must:

A. Be at least 18 years of age and legally capable of entering into a binding contract.
B. Be a Member in Good Standing at the time the loan is applied for and/or at the time each advance is made.
C. Be an Established Member at the time the loan is applied for and/or at the time each advance is made. An Established Member is one who has belonged to the credit union for a minimum of 90 days and who has no "_____" record during the past 12 months.
D. Be employed by the same employer for a period of six months, or be receiving verifiable fixed income for a period of at least six months, and must provide proof of income at the time the loan is applied for and/or at the time each advance is made.
E. Sign the Truth-in-Lending Disclosure and all associated loan documents. This includes a special document that highlights the penalties that may be imposed for failure to repay the loan as agreed.
F. Not in the process of filing for bankruptcy under any chapter of the bankruptcy code.

No minimum credit score for the borrower is required. However, the credit union may run a credit check to better serve members for future loans and to provide counsel on their current financial status.

The credit union will strongly suggest/recommend that members using the ________________ loan attend credit counseling education courses as may be offered by ____________________________________________________________________.

This Management Guideline is approved by the President/CEO on the date below, and replaces all existing management policies and guidelines related to ________________ loans.