**Best and Worst Loan Options for Consumers**

The economic and social impacts of COVID-19 are causing financial distress in many households across California. As many Californians wait to receive different forms of financial relief from federal and state governments, others are left searching for ways to get cash fast to meet their short-term needs. Loans can offer some of the most common forms of instant relief. But not all loans help consumers improve their financial situation. *So which loans should consumers avoid?*

**Payday Loan**

Payday loans may appear as an instant form of economic relief, but they are the worst. These short-term loans, often of $300 or less, are designed to be repaid in a single payment, usually by a consumer’s next payday. These loans are incredibly dangerous and financial educators recommend that they be avoided at all costs. They can quickly become [debt traps](http://stopthedebttrap.org/about/whatispaydaylending/) because the high interest, usually around [400% APR](https://oag.ca.gov/consumers/general/payday-loans), causes the borrower to fall into a dangerous cycle to re-borrow to repay the loan. If a borrower falls back on payments, they can be at risk of having their wages garnished, their car repossessed, their bank account closed due to overdraft fees, and eventually fall into bankruptcy.

**Car-Title Loan**

A car title loan is a short-term loan for a small amount of money. To get a car title loan, the borrower has to [give the lender the title to their vehicle](https://www.consumer.gov/articles/1013-car-title-loans), this includes a car, truck or motorcycle. The consumer is typically required to pay a fee to borrow the money and has to repay the loan in 30 days. This loan is dangerous because it uses a person’s vehicle as collateral. Oftentimes borrowers are required to make a copy of their car key and hand it over to the lender. If they are unable to make their payments, the lender can repossess their car.

**Online Personal Loan**

Online loans are tricky. Online lending sites are backed by a variety of lenders like traditional banks or payday. Although the APR will vary depending on a person’s credit score, you can still fall into a loan with and APR as high as 400%. Always research the lender’s reputation and look for signs that the [online loan is not a debt trap](https://www.nerdwallet.com/blog/loans/signs-predatory-online-loan/). If you give any personal information online, be sure it is not a scam.

**Tax Refund Advance Loan**

This is a short-term loan made by a lender that is based on a person’s expected federal income tax refund. In a normal tax year, tax refund loans are offered starting in January through the end of the tax season in April. Taxpayers are generally charged fees and interest to obtain a tax refund loan. The loan amount is usually less than the refund amount. But [fees can range](https://www.cbsnews.com/news/pros-and-cons-of-tax-refund-loans-and-debit-cards/) from $0 to hundreds of dollars. For example, a $59 fee charge for a $500 tax refund is equivalent to [144% APR](https://www.nerdwallet.com/blog/loans/tax-refund-loans-give-cash-now-to-early-filers/). High fees may include an application fee, flat fee to process the refund, additional state fees, all of which can result in a person paying more money than needed for their refund.

**SAFER LOAN OPTIONS**

**Credit Unions**

Credit unions are nonprofit financial institutions that aim to help members save money by providing loans with lower interest rates. For most of these loans, the interest rate is capped at 18% at credit unions, while the average rate for a three-year loan is [9.37%, according to the National Credit Union Administration](https://www.cnbc.com/2020/03/27/americans-may-soon-have-more-loan-options-heres-what-to-know.html). So, it’s a good idea for consumers to explore various loan options at their local credit union.

**Credit Cards**

Credit cards can be a good temporary option for some people. They charge interest rates ranging from 13% - 28%, making them less expensive than other small loans. The APR usually depends on credit score but if the balance can be paid off by the end of the month, a credit card can essentially offer an interest-free loan for 20 to 30 days, depending on the specific card’s terms. Recently, many credit card companies have been offering [0% APR](https://www.marketwatch.com/story/the-best-and-worst-ways-to-get-cash-if-youve-been-affected-by-the-coronavirus-pandemic-according-to-financial-planners-2020-04-10) periods of one year when cardholders call to ask for assistance. This option may be helpful for those needing to get through months of unemployment or emergency expenses. If possible, avoid a cash loan from the credit card and always make the minimum monthly payment to avoid being charged fees and risk accruing costly interest.

**Installment Loans**

An installment loan from a bank allows a person to borrow a set amount of money and repay over a fixed period of time, which is determined when the loan is taken out. This is a better option than a payday loan because this loan allows a borrower to repay in installments over time instead of in full on the next payday. Payments are typically monthly, but can vary. In CA interest rates for installment loans can be no greater than 36-38% APR on $2,500 - $10,000 loans and there is no collateral needed to obtain the loan.

**Other Options** include: borrowing money from a friend or family member, contacting a local church and other religious organizations for funds, visiting regional food banks and community foundations for assistance.

**Conclusion**

Overall, it’s best to go with a loan option that will allow a borrower to avoid harming their credit and recover from paying the loan. It’s also important to research the reputation of the lender and to make sure to review the contract (specifically the [truth in lending statement](https://www.debt.org/credit/your-consumer-rights/truth-lending-act/)) that outlines the interest and other important details of the loan. It’s important to be careful as many financial actors are eager to help but others are waiting to prey on our communities.

TO REPORT FRAUDULENT PRACTICES VISIT

California Department of Business Oversight: <https://dbo.ca.gov/file-a-complaint/>

Federal Trade Commission: <https://www.ftc.gov/faq/consumer-protection/submit-consumer-complaint-ftc>