

Small Loans Become Profitable With Employers on Board

FINANCE: Payroll Deductions Are a Key Part of Lowering Risk

By MICHAEL LIPKIN

Borrowers looking for a loan of \$1,000 or less typically have limited choices. Banks say the interest and fees often aren't enough to make the loan profitable, as the origination and servicing costs are just as high as more traditional loans. Payday loans require fast payback and carry high annualized interest rates.

San Diego-based **Employee Loan Solutions**, however, lets workers apply for loans between \$1,000 and \$3,000 and pay it back over a full year. ELS pulls data from the companies it works with to verify a worker's employment and salary, allowing a bank to quickly approve the loan. ELS then has the employer automatically deduct a set amount from every paycheck to pass along to the bank. **Doug Farry**, ELS' CEO, said the program allows companies to offer loans as an employer-provided benefit.

"It's just like a **Costco** card, a gym membership or life insurance," Farry said. "It's easy for them to do and gives us the predictability of knowing how much will be repaid and when."

ELS' service, called **TrueConnect**, doesn't provide the money itself. Partner **Sunrise Banks** in St. Paul, Minn., reviews the information provided by employers and then sends along the cash to the borrower. ELS tells the employer how much the company should deduct



Stephen Whalen

Doug Farry, CEO of Employee Loan Solutions, helped develop TrueConnect, a service that allows workers to apply for short-term loans through their companies.

every pay period, tapping into the same automated payroll infrastructure that handles tax withholding. So far, employers have found about 20 percent of their workers take out a loan, according to Farry.

Free for Employers

TrueConnect is free for employers, besides the work required to plug into ELS' system. Farry said his company generates revenue from the loan interest payments, which are shared with Sunrise. The interest rate is a fixed 24.9 percent APR, which is higher than more conventional bank loans but a third lower than the 36 percent benchmark proposed by the **Federal Deposit Insurance Corp.** for small-dollar loans. It's also far less than the 300 percent or more offered by payday lenders. The loans are also capped so that employees don't spend more than 8 percent of their regular paycheck on the loan.

"There are over 26 million Americans who do not have a credit score," a Sunrise spokeswoman said. "Since **TrueConnect** is offered as an employer benefit, a credit report or a specific loan officer is not necessary since the loan amount is based on the individual's salary."

Farry, a former senior policy adviser to ex-House Majority Leader **Dick Armey**, R-Texas, said he helped come up with the idea for **TrueConnect** when he worked at **Intuit** in the early 2000s. Part of an in-house innovation team, Farry was tasked with finding a new delivery method for Intuit's **TurboTax**. By creating an employer-provided benefit around the tax software and placing a **TurboTax** link on a company's human resources website, Intuit reduced the cost of acquiring customers and could give members a discount.

Intuit also asked Farry to explore co-branding **TurboTax** with payday loan storefronts and pawn shops. Farry said he thought it was a bad idea, but spent a lot of time researching the types of customers who use payday loans. While Farry and the team left for other jobs, they kept thinking about new ways to offer small loans and received a business methods patent in 2008 for what would become **TrueConnect**.

The **FDIC** published the results of a pilot study on small loans in 2010, reporting that few of participating community banks viewed the loans as profitable in the

EMPLOYEE LOAN SOLUTIONS

CEO: Doug Farry

No. of local employees: 7, including contractors

Headquarters: San Diego

Year founded: 2010

Revenue: Undisclosed

Company description: Allows employers to offer quick, small-dollar loans as an employee benefit through a third-party bank.

Key factors for success: ELS helps companies automatically verify their workers employment and salaries to a bank, speeding up the loan approval process. It also provides for employers to deduct regular loan payments from workers' salaries, cutting down default risk for the bank.

short term. Instead, many viewed them as a means to start a long-term relationship that could eventually become profitable.

"Instead of convincing banks to make loans that are money losers on the hopes to recoup it later with goodwill or bigger loans, what if we cut down the cost to make the loan way more efficient?" Farry said.

ELS has dozens of clients with at least 500 employees each, mostly municipalities such as the City of Anaheim, or public school systems and hospitals. The clients are all based in California, Ohio and Minnesota. More companies in six other states are interested, according to Farry, with "two large state governments" also in talks to sign on. He is also trying to secure the City of San Diego and San Diego County.

While employers can figure out how much money their workers are borrowing, Farry said **TrueConnect** allows companies to remove themselves entirely from their employees' personal finances.

"Workers might have gone to HR to ask for advances or a loan against their retirement accounts," he said. "With this, they can just send them to the website. There's actually a greater level of privacy."

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