

**TENNESSEE DEPARTMENT OF
FINANCIAL INSTITUTIONS**



The 2008 Report on the Title Pledge Industry

February 20, 2008

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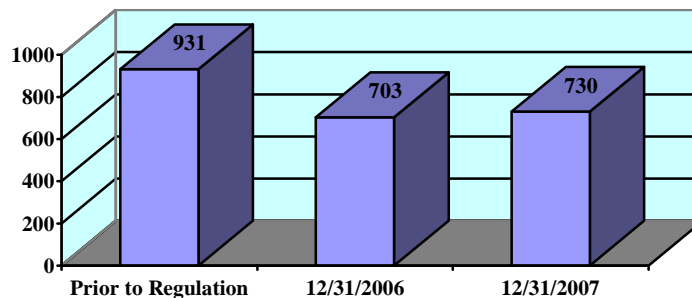
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REGULATORY OVERVIEW

Licensing

Prior to implementation of the 2005 amendments to the Act, the Department determined that 931 title pledge licenses had been issued by Tennessee County Clerks. Tenn. Code Ann. § 45-15-105(a) afforded those persons engaged in title pledge lending on November 1, 2005 the opportunity to continue in operation so long as they filed a license application with the Department by December 31, 2005. As of December 31, 2006, 703 title pledge locations were licensed with the Department. As of December 31, 2007, 730 title pledge locations were licensed with the Department. The Department denied six (6) title pledge license applications in 2007 after it was determined that the applicant did not meet the licensing requirements pursuant to Tenn. Code Ann. § 45-15-106(a)(2) for business experience, character, or general fitness.

The following table illustrates growth/shrinkage of licensed title pledge locations in Tennessee:



Examinations

Prior to the November 1, 2005 effective date of regulation, the Department began the process of gathering information on the title pledge industry. Regulatory oversight has addressed violations identified during the information-gathering stage and subsequently in compliance examinations. The practice of charging more than the statutorily permitted 2% interest and 20% service fee on the outstanding principal balance per month was prevalent before Department regulation. These overcharges have stopped as revealed by on-site examinations conducted in 2007.

For calendar year ending December 31, 2007, 629 on-site examinations were conducted on title pledge locations throughout the state which represents 86% of licensed locations. The 2007 exam penetration rate decreased from the last report due in part to increased focus on examination of the mortgage industry.

The majority of title pledge violations are cleared through the examination function. All licensees are required to provide the Department a written response to examinations within thirty (30) days from the date of the exam. The response must include documentation of the manner in which violations are corrected. The written response is reviewed by exam

management and compared to violations cited in the exam. If the response is considered inadequate, management follows-up with the licensee. If the licensee fails to correct the violations, the matter is referred to the Chief Administrator for appropriate action which may include a request for enforcement by the Legal Division. Apparent intentional wrongdoing, significant refunds, recurrent or company-wide issues requires referral to the Nashville Office.

The following are the violations most frequently identified in examinations:

1) Repossession of collateral during an active renewal period

- With regard to repossession of the collateral during an active renewal period, the lender must refund the repossession charges and the interest and fees collected for that 30 day period. The Department issued Bulletin C-08-1 on January 25, 2008 to the industry to clearly set forth, clarify, and reinforce the position that has been applied through the examination function. This Bulletin was mailed to all licensed locations and posted to the Department website.

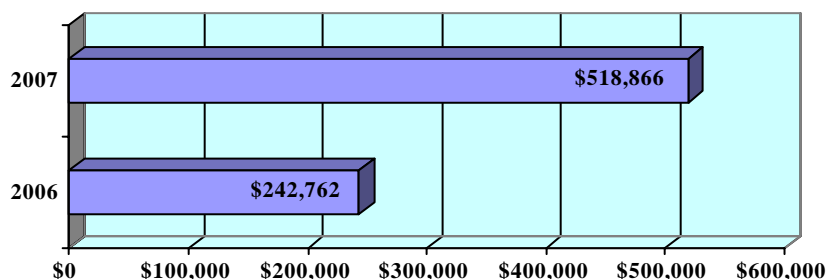
2) Improper application of the principal reductions

- For improper application of the principal reductions, the lender must refund excess interest and fees collected.

3) Lender failed to keep complete records of each transaction

- Regarding incomplete records, the licensee is required to implement controls to provide for a complete set of records going forward.

Examination and enforcement by the Department resulted in refunds totaling \$518,866 in 2007. The following table compares consumer refunds from examinations over the past two years:



Twenty-two title pledge locations were subjected to some form of administrative enforcement beyond the informal corrective action through the examination function. The Department issued Emergency Cease and Desist Orders against six (6) title pledge locations. A Notice of Charges was issued against eight (8) locations seeking refunds and/or civil monetary penalties. A Consent Agreement or other settlement was reached with eight (8) title pledge locations for refunds and/or civil monetary penalties.

Consumer Complaints

For calendar year ending December 31, 2007, the Department received 24 consumer complaints against title pledge lenders. All 24 complaints were reviewed by the Department and either a mutually acceptable agreement was reached between the title pledge lender and the complainant or it was determined that there was no violation of the Title Pledge Act.

The most frequent allegation involved repossession issues which were reported in seven (7) complaints. The documentation received including the complaint, lender's response, as well as the Department's investigation, revealed that the lenders did not violate the Act.

The following are representative examples of other complaints received:

Four (4) complaints alleged there were payment processing disputes. The Department's investigation revealed that none of the lenders were negligent in processing consumer's payments.

Three (3) complaints noted customer service issues. These matters are generally subjective and the Department is limited in its ability to resolve these matters. For example, consumers claimed that an employee was rude to them.

Two (2) complaints alleged that rates and fees charged were "excessive". Investigations revealed that the lender was charging rates and fees permitted by statute and the complaints were directly related to the 5% principal reduction required by Tenn. Code Ann. § 45-15-113(d). With the application of the 5% principal reduction, the borrower's payment increased resulting in so-called "payment shock" which triggered the complaints.

One (1) consumer complaint alleged misrepresentation on the part of the lender. In this case, the lender waived the interest and fees, refunded \$979.05, and returned the collateral to the consumer.

Two (2) complaints alleged unlicensed title pledge activity against the same lender. These complaints were referred to the Compliance Division in late December 2007 for possible examination. Based upon on-site examination and investigation by examiners, it was determined that the type of lending activity in question was not subject to the Title Pledge Act.

One (1) complaint alleged a lender was violating the Fair Debt Collection Act by contacting one of his employees at work frequently. The lender took immediate action by terminating the employee responsible.

ANALYSIS OF OPERATIONS

The data which follows is derived from information provided by 672 title pledge locations, representing 175 companies and reflects general results of operations for the time period January 1, 2006 to December 31, 2006. The difference between the 703 locations as of December 31, 2006 and the 672 locations that reported financial results is attributed to 22 locations that were licensed in 2006, but did not begin operating until 2007. The remaining nine (9) locations, although licensed in 2006, closed before the filing deadline for annual report submission.

In September 2007, lenders began renewing their licenses. Tenn. Code Ann. § 45-15-106(i) provides that the license shall expire on October 31 of each year. Each license may be renewed upon application to the Commissioner annually, on or before October 1. A license renewal application packet was sent to all licensees in June 2007. The renewal application packet included a supplemental financial report upon which this data analysis was based.

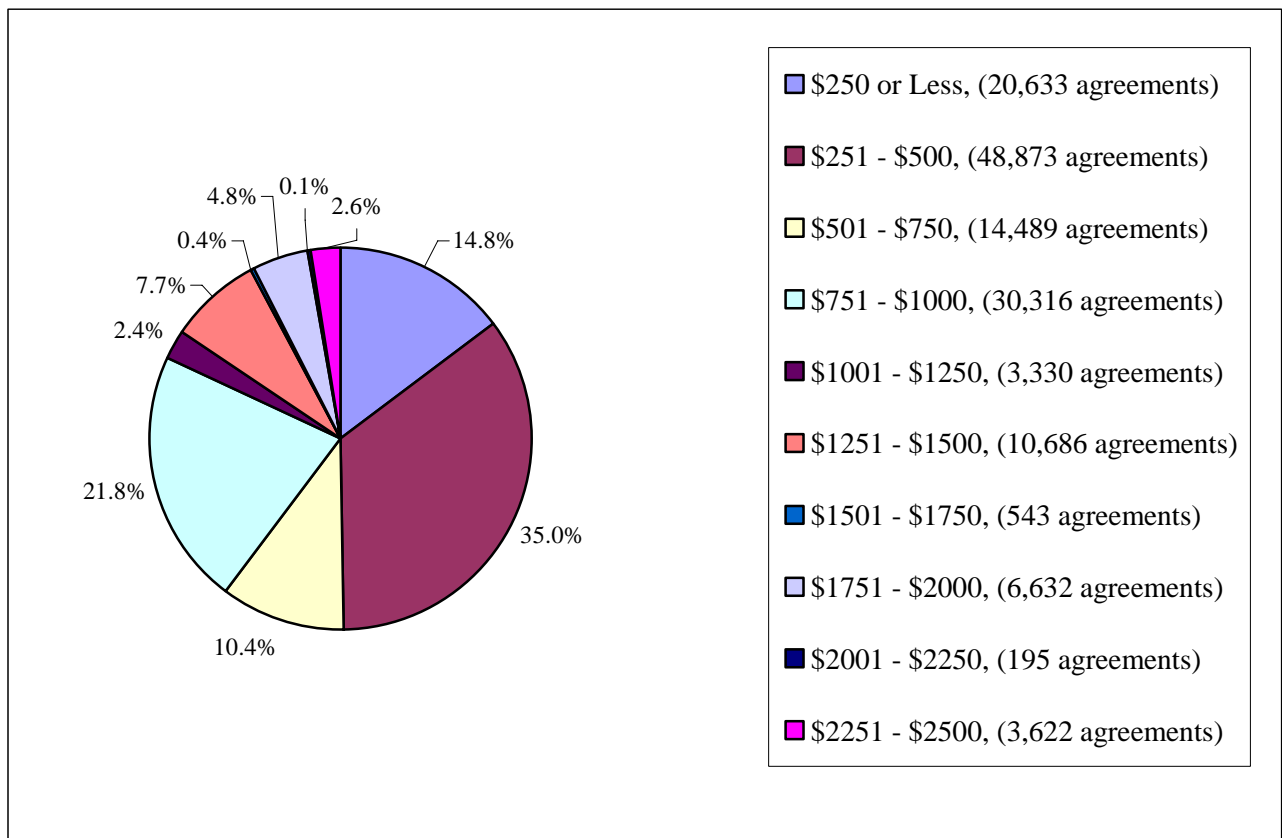
This report requested information on an unconsolidated basis, which meant that companies engaging in more than one line of business were asked to segment their income and expenses and report such data exclusively for title pledge business. Tenn. Code Ann. § 45-15-106(d)(2) states, in pertinent part, that the balance sheet and income statement for the immediately preceding fiscal year end, must be prepared in accordance with generally accepted accounting principles by a certified public accountant or public accounting firm not affiliated with the applicant. The licensee was also required to attest under oath to the truthfulness and accuracy of the information submitted. To further ensure the accuracy of information submitted, the Department has undertaken the on-site examination of randomly selected companies to audit the financial and transaction data submitted. The following presents the results of the financial reports filed with the Department.

Demand for New Title Pledge Agreements

For reporting period January 1, 2006 to December 31, 2006, a total of 139,319 new title pledge agreements were made. This figure reflects new agreements made and does not include renewals of these initial agreements.

The following presents a breakdown of new title pledge agreements by loan amount:

Number of Agreements by Size:	Number	% of Total
\$250 or Less	20,633	14.8%
\$251 - \$500	48,873	35.0%
\$501 - \$750	14,489	10.4%
\$751 - \$1000	30,316	21.8%
\$1001 - \$1250	3,330	2.4%
\$1251 - \$1500	10,686	7.7%
\$1501 - \$1750	543	0.4%
\$1751 - \$2000	6,632	4.8%
\$2001 - \$2250	195	0.1%
\$2251 - \$2500	3,622	2.6%
Total Number of Agreements	139,319	100%



Eighty-two percent of new agreements were for \$1,000 or less, while 50% were for \$500 or less. Only 2.6% of new agreements were for \$2,250 or more, with \$2,500 being the maximum loan amount permitted under the Act. During the reporting period, the average amount of a new title pledge agreement was \$557.70.

Market Share of New Title Pledge Agreements

One hundred sixty companies (292 locations) made 1,000 or fewer title pledge agreements. Combined, this group made 40,346 agreements which represented 29% of agreements. Eleven companies (122 locations) made between 1,001 and 10,000 agreements each. Combined, this group made 25,374 agreements which represented 18% of agreements. Four (4) companies (258 locations) made over 10,000 title pledge agreements each. Combined, this group made 73,599 agreements which represent 53% of agreements.

Trend Analysis

The data indicates that 69,002 agreements, totaling \$36,411,055, were outstanding as of December 31, 2005 compared to 83,570 agreements, totaling \$43,299,483 outstanding as of December 31, 2006. Industry growth for 2006 in outstanding receivables was \$6,888,428 or 18.92%. The growth in number of outstanding agreements in 2006 was 21.11% or 14,568. The average outstanding balance per agreement decreased from \$527.68 at December 31, 2005 to \$518.12 at December 31, 2006.

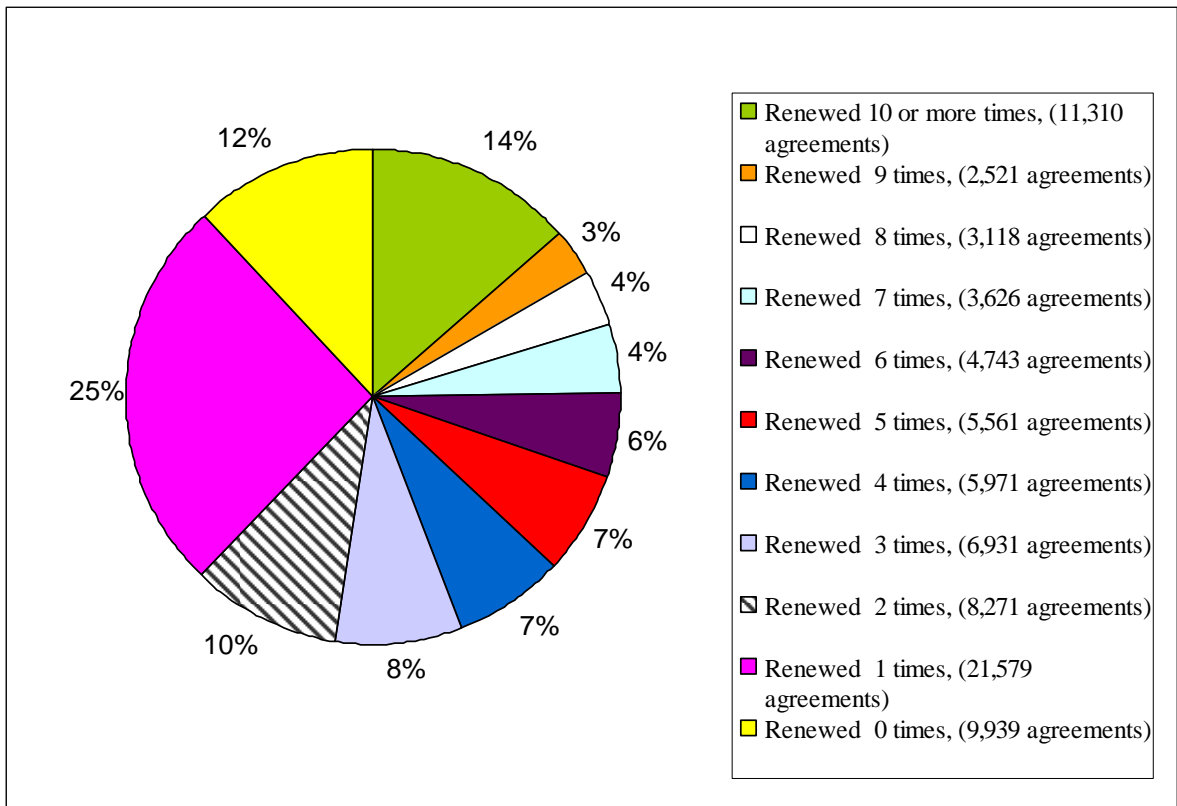
The following analysis is based on agreements that were active as of December 31, 2006. Of the active agreements, 25% had been renewed one (1) time⁽¹⁾ and 49% were renewed between two and nine times. Fourteen percent (14%) renewed 10 or more times.

Of the 83,570 agreements outstanding as of December 31, 2006, 88% or 73,631 had renewed at least one time and 12% or 9,939 were less than 30 days old and the renewal had not yet come due.

The following illustrates the renewal pattern for the 83,570 outstanding title pledge agreements as of December 31:

Agreements Outstanding as of December 31, 2006		
Renewal Frequency	# of Agreements Renewed	% of Total Outstanding
Renewed 10 or more times	11,310	14%
Renewed 9 times	2,521	3%
Renewed 8 times	3,118	4%
Renewed 7 times	3,626	4%
Renewed 6 times	4,743	6%
Renewed 5 times	5,561	7%
Renewed 4 times	5,971	7%
Renewed 3 times	6,931	8%
Renewed 2 times	8,271	10%
Renewed 1 time ⁽¹⁾	21,579	25%
	73,631	

¹Agreements that were opened in November 2006 and renewed once in December 2006.



* Agreements that were opened in November 2006 and renewed once in December 2006.

The industry repossessed 18,199 vehicles in 2006 due to non-payment. Beginning November 1, 2005, Amendments to the Act require lenders to return any surplus from the sale of repossessed vehicles to the consumer. Because of these amendments, coupled with oversight by the Department, the industry returned a total of \$1,256,068 to consumers in 2006.

Application of the Principal Reduction Requirement

Pursuant to Tenn. Code Ann. § 45-15-113(d), the borrower is required to make a 5% principal reduction beginning with the third renewal of the title pledge agreement. This provision became effective November 1, 2005 and was first applicable in February 2006. With the application of the principal reduction requirement, both the term of the agreement as well as interest and fees will significantly decrease.

The following table illustrates the effects of the principal reduction provision:

	22% Interest/Fees, No Principal Reduction	22% Interest/Fees, 5% Principal Reduction
	<i>Under prior law</i>	<i>Current Law</i>
Original Principal Balance	\$500	\$500
Payoff time	Perpetual	22 months
Total interest/ fees paid at 22 months	\$2,420	\$1,375
Total interest/ fees paid over life of loan	Unlimited	\$1,375

As the previous table reflects, the application of the 5% principal reduction at the third renewal reduces the amount of interest and fee paid over the life of the loan by \$1,045, provided that both agreements are fully satisfied at the end of the 22nd month.

The following scenarios, also based on a \$500 original principal balance, are for illustration purposes only:

- If the 5% principal reduction were to be applied at the beginning of the first renewal (day 31), the interest and fees paid would total \$1,155 and the term reduces to 20 months.
- If the principal reduction amount was increased to 10% at the beginning of the third renewal, the interest and fees paid would total \$825 and the term reduces to 12 months.

In the event the consumer cannot make the scheduled principal reductions, the lender may defer such payment until the end of the title pledge agreement. However, the lender is required to reduce the outstanding principal balance subject to interest and fees by 5% per month whether or not the payment is received. Of the 83,570 agreements outstanding as of December 31, 2006, upon which more than 325,000 renewals were made, there were 17,958 principal reduction deferrals allowed by lenders.

Analysis of Profitability

In analyzing profitability industry-wide, this report focuses on net income before tax, and performs a breakeven analysis based upon interest and fees charged. Net income before tax is the company's revenue from operations less business expenses. In the industry, the revenue is made up of customary interest and fees. Expenses include, but are not limited to, advertising, salaries, rent, utilities, insurance, regulation, repossessions and bad debt expense.

Net income before tax is a more meaningful measure for comparison purposes. In 2006, it was \$9,320,500. The industry is comprised of various business structures including corporations, limited liability companies, partnerships and sole proprietorships. Although the administrative and operational expenses generally run consistent from one business structure to another, income tax will differ because the tax treatment associated with each type of entity varies significantly. For example, certain business structures allow for income generated by the business to be passed through to the owner(s). When income is passed

through to the owner(s), taxes are paid at individual tax rates and the business is not taxed on that income. This renders net income after tax less comparable than income before tax. Even so, income after tax for 2006 was \$8,828,623, a variance of \$491,877. This amount equals .68% of total revenue and is immaterial to this analysis. The combined net income before tax for the 175 companies (672 licensed locations) reporting was approximately \$9.3 million.

The following table provides more detail on income and expenses for the industry:

Income Statement Summary		
(175 reporting companies, 672 locations)		
		% of Revenue
Revenue	\$ 72,125,249	
Employee Salaries	15,891,949	22%
Bad Debts	11,394,220	16%
Repossession Expense	3,227,022	4%
General Operating Expenses	<u>32,291,558</u>	45%
Net Income	\$ 9,320,500	

Title pledge lenders record revenue when the customer enters into an agreement to borrow money. The customer is legally obligated to pay back the principal, interest and fees. If the customer fails to pay their debt or, in other words, defaults on the loan, the lender's recourse is limited to taking possession of the collateral. If the customer fails to redeem it during a twenty-day holding period, the lender has 60 days to sell it. Unless all proceeds from the sale offset the debt, the balance due is considered uncollectible by the lender and is subsequently charged-off. This amount is classified as bad debt expense on the income statement. In some cases the lender cannot locate the collateral and, as a consequence, the entire debt is deemed uncollectible and charged-off against accounts receivable. Lenders charged-off approximately \$13.6 million due to non-payment of all or part of the original principal balance. This charge-off amount represents approximately 17.5% of the total dollar amount of loans made which was \$77,698,729.

Overall, the title pledge industry generated approximately \$72 million in revenues during 2006. Forty-five percent of revenue was paid toward general operating expenses including but not limited to rent, utilities, advertising, regulation and supplies. The next largest expense category for the industry was employee salaries which made up 22% of total revenues. Bad debt and repossession expenses accounted for 20% of revenues with net income making up 13%. Owner compensation was reported to be \$5.1 million, representing approximately 55% of net income. Although the industry as a whole was profitable, there was a wide disparity in the level of profitability within the industry.

The following table provides more detail on net income of the industry:

Net Income	Number of Companies	Number of Locations	Average Net Income per Company
More than \$1 million	3	74	\$1,394,701
\$100,001 - \$1 million	20	197	\$202,439
Zero - \$100,000	129	224	\$30,919
Loss	23	177	(\$126,128)

Twenty-three companies (177 licensed locations) reported a loss. Another 129 companies (224 licensed locations) reported less than \$100,000 of net income. These combined companies represent 87% of the industry. Twenty companies (197 licensed locations) reported net income of between \$100,001 and \$1 million dollars and three (3) companies (74 licensed locations) reported net income greater than \$1 million.

In order to better understand the difference in net income of the industry, the following table provides a breakdown of expenses for companies producing different levels of net income illustrated above.

In the following table, the expenses are expressed as a percentage of revenues:

Allocation of Revenue by Income Level				
Net Income	Bad Debt / Revenue	Repossession Expense / Revenue	Employee Salaries / Revenue	General Operating Expenses / Revenue
<i>Industry Average</i>	<i>16%</i>	<i>4%</i>	<i>22%</i>	<i>45%</i>
More than \$1 million	21%	5%	18%	39%
\$100,001 - \$1 million	13%	5%	21%	32%
Zero - \$100,000	11%	4%	23%	39%
Loss	16%	4%	29%	69%

For companies that had a loss, employee salaries accounted for 29% of total revenues, which was 7% higher than the industry average. In addition, these companies had bad debt expense of 16%, which was on par with the industry average. For companies that had net income of one million or more, employee salaries accounted for 18% of total revenues, which was 4% lower than the industry average. These companies had a bad debt expense of 21%, which was 5% higher than the industry average.

Analysis by Company Size

The business structures of the 175 companies, as of December 31, 2006, consisted of 31 sole proprietorships, 7 partnerships, 56 limited liability companies (LLC), and 81 corporations. Companies range in size from one (1) location to over 100 locations.

In regards to the number of lenders operating in Tennessee based on company size, the following table provides a snapshot as of June 30, 2006 (previous reporting period) and December 31, 2006 (current reporting period):

Company Size	As of June 30, 2006		As of December 31, 2006		Number of Locations increase or (decrease)
	Companies	Locations	Companies	Locations	
Single location	141	141	109	109	(32)
Small (2-9 licensed locations)	54	195	54	185	(10)
Medium (10-24 licensed locations)	8	123	9	135	12
Large (25 or more licensed locations)	3	186	3	243	57

The analysis that follows categorizes title pledge locations into four categories and shows the allocation of revenue based on company size expressed as a percent.

Allocation of Revenue by Company Size					
Company Size	Bad Debt Expense	Repossession Expense	Employee Salary Expense	General Expense	Net Income
Single Location	6%	5%	22%	41%	26%
Small Company (2-9 locations)	9%	3%	22%	45%	21%
Medium Company (10-24 locations)	19%	4%	24%	33%	20%
Large Company (25 or more locations)	20%	5%	22%	52%	1%

The data and analysis that follows will group the 672 locations into one of four categories and provide additional profitability statistics for each group.

Single Location Title Pledge Lenders

Income Statement Summary		
		% of Revenue
Revenue	\$ 10,415,974	
Bad Debt	\$ 658,494	6%
Repossession Expense	\$ 566,743	5%
Employee Salaries	\$ 2,247,092	22%
General Expenses	\$ 4,279,269	41%
Net Income	\$ 2,664,376	

- For this category, total net income of \$2,664,376 represented 29% of the industry total of \$9,320,500;
- Of the 109 companies (109 licensed locations), 19 companies or 17% reported a loss;
- \$6.1 million of outstanding accounts receivable represented 14% of the industry total of \$43.3 million;
- Bad debt expense of \$658,494 represented 6% of the industry total of \$11,394,220; and
- Repossessions of 4,998 vehicles represented 27% of the industry total of 18,199, with related expenses of \$461,322.

Small Title Pledge Lenders (2-9 Locations)

Income Statement Summary		
		% of Revenue
Revenue	\$ 13,975,549	
Bad Debt	\$ 1,247,506	9%
Repossession Expense	\$ 456,374	3%
Employee Salaries	\$ 3,009,883	22%
General Expenses	\$ 6,390,424	45%
Net Income	\$ 2,871,362	

- For this category, total net income of \$2,871,362 represented 30% of the industry total of \$9,320,500;
- Of the 54 companies (185 licensed locations), seven (7) companies (30 locations) or 13% reported a loss;
- \$7.6 million of outstanding accounts receivable represented 18% of the industry total of \$43.3 million;
- Bad debt expense of \$1,247,506 represented 11% of the industry total of \$11,394,220; and
- Repossessions of 2,688 vehicles represented 15% of the industry total of 18,199, with related expenses of \$440,346.

Medium Title Pledge Lenders (10-24 Locations)

Income Statement Summary		
		% of Revenue
Revenue	\$ 17,218,442	
Bad Debt	\$ 3,334,588	19%
Repossession Expense	\$ 744,654	4%
Employee Salaries	\$ 4,037,317	24%
General Expenses	\$ 5,603,986	33%
Net Income	\$ 3,497,897	

- For this category, total net income of \$3,497,897 represented 38% of the industry total of \$9,320,500;
- Of the nine (9) companies (135 licensed locations), three (3) companies (40 locations) or 33% reported a loss;
- \$9.0 million of outstanding accounts receivable represented 21% of the industry total of \$43.3 million;
- Bad debt expense of \$3,334,588 represented 29% of the industry total of \$11,394,220; and
- Repossessions of 3,243 vehicles represented 18% of the industry total of 18,199, with related expenses of \$610,263.

Large Title Pledge Lenders (25 or More Locations)

Income Statement Summary		
		% of Revenue
Revenue	\$ 30,515,284	
Bad Debt	\$ 6,153,632	20%
Repossession Expense	\$ 1,459,251	5%
Employee Salaries	\$ 6,597,657	22%
General Expenses	\$ 16,017,880	52%
Net Income	\$ 286,864	

- For this category, total net income of \$286,864 represented 3% of the industry total of \$9,320,500;
- Of the three (3) companies in this category, one reported a loss;
- \$20.6 million of outstanding accounts receivable represented 47% of the industry total of \$43.3 million;
- Bad debt expense of \$6,153,632 represented 54% of the industry total of \$11,394,220; and
- Repossessions of 7,270 vehicles represented 40% of the industry total of 18,199, with related expenses of \$2,189,502.

BREAKEVEN ANALYSIS

A breakeven analysis is another financial tool which provides a specific level of price, or interest and fees in this case, at which a company is profitable. A major component of the breakeven analysis is the profit margin. Profit margin illustrates how much of every dollar of gross revenues a company retains in earnings after expenses. The profit margin is calculated by dividing net income by total revenues. Total revenues and expenses reported by the industry as a whole on their financial reports as of December 31, 2006 are noted below.

Revenue	\$72,125,249	100%
Expenses	<u>\$62,804,749</u>	<u>87%</u>
Net Income	\$ 9,320,500	13% (profit margin ratio)

By dividing net income of \$9,320,500 by total revenue of \$72,125,249, the profit margin ratio of the title pledge industry was 13%. This means that, on average, for every dollar of revenue made, thirteen cents (\$.13) went to net income. Net income, often referred to as “the bottom line”, is equal to the income a business has after subtracting costs and expenses from total revenue. It can be distributed among the owners or held by the entity as retained earnings. In 2006, seven cents (\$.07) of every dollar of revenue went to the owners; whereas, six cents (\$.06) went to retained earnings, totaling \$5,164,888 and \$4,155,612, respectively. Of every dollar, eighty-seven cents (\$.87) was used to offset business costs and expenses.

Companies Charging Only 22%

Since the breakeven analysis is designed to determine a specific level of interest and fees necessary to be profitable, it is appropriate to look only at those title pledge lenders charging 22%, versus a lower amount. It was determined that 59% of locations (394 locations) charged 22% (2% interest/20% service fee) on all agreements.

The following amounts were compiled from income statements.

Revenue	\$27,882,428	100%
Expenses	<u>\$22,352,749</u>	<u>80%</u>
Net Income	\$ 5,529,679	20% (profit margin ratio)

Lenders charging 22% reported \$27,882,428 in gross revenue resulting in a profit margin ratio of 20%. This means that for every dollar of revenue generated twenty cents (\$.20) went to net income. Therefore, on a \$100 loan at 22%, lenders earned \$22, of which \$4.40 (\$22 x .20 profit margin ratio) went to net income. Seventeen dollars, sixty cents (\$17.60) of the \$22 was used to defray costs.

The analysis below translates the profit margin into the actual amount of interest and fees that was necessary for the company to breakeven.

		Rate		Break Even
Revenue	\$27,882,425	100% x 22%	=	22.0% 17.6%
Expenses	<u>\$22,352,749</u>	<u>80%</u> x 22%	=	<u>17.6%</u> <u>17.6%</u>
Net Income	\$ 5,529,679	20% (profit margin ratio) x 22%	=	4.4%* 0

** Annualized, the net return on each \$100 in receivables would be \$52.80.*

It appears from this analysis that if these lenders had charged 17.6% instead of 22% on their loans, they would have made just enough revenue to offset total expenses without making a profit. A rate higher than 17.6% would have generated a profit, and anything less would have resulted in a loss. The tabulations above are based on industry averages.

The following tables give the break even point according to company size:

Single Location Title Pledge Lenders

		Rate		Break Even
Revenue	\$9,678,624	100% x 22%	=	22.0% 15.8%
Expenses	<u>\$6,988,691</u>	<u>72%</u> x 22%	=	<u>15.8%</u> <u>15.8%</u>
Net Income	\$2,689,933	28% (profit margin ratio) x 22%	=	6.2%* 0

** Annualized, the net return on each \$100 in receivables would be \$74.40.*

The 28% profit margin ratio for this category was determined by dividing net income of \$2,689,933 by total revenue of \$9,678,624. Again this means that for every dollar of revenue generated about twenty-eight (\$.28) cents went to net income. On a \$100 loan at 22%, lenders earned \$22 of which \$6.20 (\$22 x 28% profit margin ratio) went to net income, and \$15.80 (\$22 x 72%) was used to defray costs. If lenders in this group had charged their customers 15.8% instead, they would have made just enough revenue to offset expenses without making a profit. The break even rate for this category would be 15.8%. The foregoing analysis was also used in each of the following categories even though the profit margin ratio varies.

Small Location Title Pledge Lenders (2-9 Locations)

		Rate		Break Even
Revenue	\$10,908,365	100.0% x 22%	=	22.0% 17.6%
Expenses	<u>\$ 8,704,626</u>	<u>79.8%</u> x 22%	=	<u>17.6%</u> <u>17.6%</u>
Net Income	\$ 2,203,739	20.2% (profit margin ratio) x 22%	=	4.4%* 0

** Annualized, the net return on each \$100 in receivables would be \$52.80.*

Medium Location Title Pledge Lenders (10–24 Locations)

		Rate		Break Even
Revenue	\$ 2,289,930	100.0% x 22%	= 22.0%	20.1%
Expenses	\$ <u>2,098,588</u>	<u>91.6%</u> x 22%	= <u>20.1%</u>	<u>20.1%</u>
Net Income	\$ 191,342	8.4% (profit margin ratio) x 22%	= 1.9%*	0

**Annualized, the net return on each \$100 in receivables would be \$22.80.*

Large Location Title Pledge Lenders (25 or More Locations)

		Rate		Break Even
Revenue	\$ 5,005,509	100.0% x 22%	= 22.0%	20.0%
Expenses	\$ <u>4,560,844</u>	<u>91.1%</u> x 22%	= <u>20.0%</u>	<u>20.0%</u>
Net Income	\$ 444,665	8.9% (profit margin ratio) x 22%	= 2.0%*	0

**Annualized, the net return on each \$100 in receivables would be \$24.00.*

Companies Charging Less Than 22%

Thirty-three (33) companies (278 locations) in the industry charged between 10% to 21%. The following figures are not fully depictive as one large company had a sizeable loss for the year, and to have included it would have skewed the results significantly.* For the remaining companies, eighty-four cents (\$.84) of every dollar was used to offset expenses; whereas, companies charging (22%) across the board spent eighty cents (\$.80).

*Revenue	\$32,619,176	100%
Expenses	<u>\$27,408,773</u>	<u>84%</u>
Net Income	\$ 5,210,403	16% (profit margin ratio)

The following comparison shows that the profit margin ratio of companies charging 22% was higher than for those averaging lower rates.

	<u>22%</u> (142 Companies / 394 locations)		<u>Less Than 22%</u> (32 companies / 178 locations)	
Revenue	\$27,882,428	100%	\$32,619,176	100%
Expenses	<u>\$22,352,749</u>	<u>80%</u>	<u>\$27,408,773</u>	<u>84%</u>
Net Income	\$ 5,529,679	20%	\$ 5,210,403	16% (profit margin ratio)

With regard to companies charging 22%, bad debt expense was equal to 16% of gross revenue. Had bad debt expense been lower, the overall breakeven would likely have been less than 17.6%. In fact, when you segregate companies by size, the following table shows that the breakeven point for 2006 was considerably lower for the groups which had less bad debt expense.

The following table represents the bad debt expense of companies charging 22%:

Company Size	Bad Debt Expense / Revenue	Breakeven
Single location	5.8%	15.8%
Small (2-9 licensed locations)	9.6%	17.6%
Medium (10-24 licensed locations)	20.4%	20.1%
Large (25 or more licensed locations)	25.8%	20.0%

It appears that the single greatest impact management might make on costs is its control of bad debt expense.

CONCLUSION

Title Pledge lending in Tennessee continues to be a significant segment of the financial services sector. Based on reported information, 139,319 title pledge transactions were initiated during the reporting period. The total dollar volume of these new agreements amounted to \$77,698,729.

Information gathered shows that the industry as a whole was profitable although there was a wide disparity in level of profitability. During this period, the single location lenders representing 109 locations fared the best from an economic return standpoint. These locations doubled the average profit margin for the industry as a whole and correspondingly had the lowest bad debt expense ratio.

An important market trend appears to be that the number of smaller companies is declining while the largest companies are expanding their locations. If it is the case as we believe that the largest companies sometimes offer rates less than 22% and at times significantly less, then it may be the case that some small companies cannot compete and some borrowers may benefit by receiving a lower rate. That may also explain why the larger companies may be reflecting relatively smaller returns during the reporting period. A lowering of rates could be a consideration that might still permit a segment of the industry to operate depending on the level of rate reduction. With a wide disparity in bad debt expense among companies, we continue to speculate that the current rate provides enough cushion and perhaps incentive for some companies to operate at a less than optimum efficiency. Whether rates are lowered statutorily or not, there appears to be some competitive market forces in place that might reduce rates where competition exists. However, as we have noted there appears to be a trend toward consolidation and in those areas of the state where there is little or no competition, rates are not likely to move downward by market pressure.

While attention, deservedly so, is placed on the rates and practices of title pledge lenders, we also see a more fundamental need facing a segment of Tennessee consumers. The lack of financial literacy among some citizens is a serious concern and we believe it is often a root problem for some of the ills we see in the financial services sector.

We understand that some individuals are hampered by circumstances outside of their control such as a serious illness that may force a short term need for “fast cash” but we also know anecdotally of individuals that do not understand that title pledge transactions are not meant for long-term financing of basic necessities. Ironically, we have received complaints from borrowers who do not like the principal reduction feature of the Act because it interferes with their desire or need to enter into long term transactions even though principal reduction helps to prevent such borrowers from being mired into long term debt.

With the exception of unexpected events that may seem to force some to seek out fast cash, we believe that a lack of a basic understanding of financial concepts has permeated generations of Tennessee families and has created an environment that perhaps supports some of the numbers reported herein.

But there is some progress being made. We are certainly glad to see that a personal finance class will soon become mandatory in Tennessee schools.

In recent years we have added financial literacy as another segment of our core operations and have reached out through public service announcements, workshops and partnerships with other public and private entities.

This Department is partnering with efforts such as the Smart Tennessee program out of the University of Memphis which seeks to educate students in basic financial concepts. We have worked for many years with organizations such as the Tennessee Jumpstart Coalition and others that have done much to promote financial literacy. The Department is also encouraging Tennessee’s mainstream banking community to consider making small dollar loans and there are Tennessee banks and credit unions providing alternative loan sources.

As we have for many years, this Department will continue to concentrate on the licensee-focused areas of applications, examinations and enforcement actions. While these three traditional areas of operation are very important, we realize that more attention needs to be placed directly on consumers before the receipt of consumer complaints. Not only is financial literacy a key for the welfare of the individual, but we believe it is a key factor for the health of well meaning financial institutions and ultimately for the Tennessee economy.

ADDITIONAL INFORMATION

Number of Title Pledge Licensed Locations by County

# OF TPL LOCATIONS		COUNTY
12/31/2006	12/31/2007	
4	5	ANDERSON
8	9	BEDFORD
2	2	BENTON
0	1	BLEDSOE
12	11	BLOUNT
7	8	BRADLEY
5	6	CAMPBELL
3	3	CANNON
5	6	CARROLL
3	3	CARTER
3	3	CHEATHAM
3	3	CHESTER
6	6	CLAIBORNE
4	5	COCKE
9	8	COFFEE
8	7	CUMBERLAND
77	81	DAVIDSON
2	2	DECATUR
4	4	DEKALB
13	13	DICKSON
5	6	DYER
2	3	FAYETTE
1	1	FENTRESS
5	5	FRANKLIN
13	14	GIBSON
3	4	GILES
9	8	GREENE
8	8	HAMBLÉN
33	34	HAMILTON
3	3	HARDEMAN
4	4	HARDIN
3	4	HAWKINS
5	5	HAYWOOD
6	6	HENDERSON
3	2	HENRY
2	1	HICKMAN
1	1	HOUSTON
3	3	HUMPHREYS
1	1	JACKSON
3	4	JEFFERSON
0	1	JOHNSON
40	35	KNOX

# OF TPL LOCATIONS		COUNTY
12/31/2006	12/31/2007	
2	2	LAUDERDALE
7	8	LAWRENCE
2	3	LEWIS
3	2	LINCOLN
4	5	LOUDON
4	4	MACON
19	20	MADISON
6	6	MARION
4	6	MARSHALL
17	16	MAURY
9	10	MCMINN
4	4	MCNAIRY
5	7	MONROE
12	12	MONTGOMERY
3	3	MORGAN
7	7	OBION
3	3	OVERTON
0	1	POLK
13	15	PUTNAM
5	6	RHEA
5	4	ROANE
8	10	ROBERTSON
33	34	RUTHERFORD
3	3	SCOTT
4	4	SEQUATCHIE
9	9	SEVIER
90	105	SHELBY
1	1	SMITH
1	1	STEWART
17	18	SULLIVAN
18	19	SUMNER
7	6	TIPTON
1	2	TROUSDALE
1	1	UNICOI
7	8	WARREN
13	12	WASHINGTON
1	1	WAYNE
2	4	WEAKLEY
3	4	WHITE
3	6	WILLIAMSON
16	18	WILSON