March 11, 2012

THE DEVIL IS IN THE DETAILS: IS PAYDAY LENDING A GODSEND, A NECESSARY EVIL, OR AN ENTICEMENT INTO FINANCIAL HELL?

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Ron Elwood\textsuperscript{d1}
Payday lending remains a highly controversial subject. The debate about its merits is polarized. Proponents focus solely on the payday loan as the only source of helpful credit to a segment of consumers excluded from mainstream lenders. Opponents focus solely on the adverse consequences so many customers experience after using payday lenders. Neither side acknowledges arguments, however legitimate, the other makes. Demand for small-amount, short-term loans is undeniable. Absent from most discussions of the subject is an exhaustive comparison and analysis of the myriad of rationales industry attackers and defenders use to justify their positions and conclusions. A deconstruction of the arguments leads to the inescapable conclusion that the justifications for payday lending are not supported by the evidence. Thus, even if consumers have no other alternatives, payday lending is not the answer because any benefits from its use do not outweigh detriments. But neither steering certain credit seekers to mainstream markets that either ignore or exploit them or resignedly accepting a predatory lending system serves those with credit impairments well. The solution to this conundrum lies in a concerted effort by state and federal governments, nonprofits, responsible corporations, faith-based groups, and philanthropic organizations together to develop an alternative and sustainable financial system for those for whom traditional credit is unattainable or undesirable without the exploitation that characterizes payday lending.
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I. INTRODUCTION

A large body of scholarship has emerged – with no shortage of opinions proffered – on the merits of payday lending. Do payday lenders provide bridge financing to borrowers with short-term emergencies and nowhere else to turn? Or are the loans they offer abusively-priced products designed to trap borrowers in an endless cycle of debt? Do payday lenders offer the only available access for cash-strapped and credit-challenged borrowers to small dollar loans? Or do they exploit a flawed market to prey on desperate borrowers, causing society more problems than they address? As one commentator observes: “The answer, of course, depends on whom you ask.” Payday lenders tout themselves as benevolent friends to borrowers in need. Consumer advocates claim the lenders are “wolves in sheep's clothing.”¹

If the demand for short-term, small-amount lending has been demonstrated, serious questions exist whether payday lending is the appropriate response. What is clear is the need to support policies and create new systems to provide a product to fill the demand for small-dollar, short-term loans without placing those who by definition are financially vulnerable at greater financial risk, which in turn, destabilizes the broader micro and macro financial ecosystems within which they function.

The “incendiary national debate” about payday lending continues unabated.² This article identifies the myriad of issues in contention surrounding payday lending, distills the salient arguments on both sides, concludes that, on balance, consumers and society are better off without payday lending, and suggests that a new delivery system is necessary to meet the demand for short-term, small-amount loans. Part II offers a brief history of payday lending. Part III presents and analyzes the critiques and defenses of the payday lending industry. Finally, Part IV offers a recommendation that policymakers, nonprofit organizations, and philanthropies
interested in family financial security join forces to establish a robust, scaled market for small amount, short-term loans at rates and under terms and conditions that do not exploit borrowers.

II. A BRIEF HISTORY OF PAYDAY LENDING

A. Progenitors

Early responses to the demand for short-term, small-amount lending ran the gamut from altruistic attempts to provide credit to pawn brokering to avaricious or even criminal attempts to exploit the financially distressed. Altruistic philanthropic lenders operating in the 19th Century offered either interest-free loans or loans at low, nonusurious interest rates. A more ubiquitous model – the “remedial loan society” – emerged in the 1850s as a means to provide short-term credit at reasonable terms to poor and financially needy borrowers, with “the Collateral Loan Company of Boston, the first of its kind, opening its doors in 1857.” Later, the Provident Loan Society of New York City would become “the largest and most influential loan society in the country.” By 1909, the industry had grown sufficiently to warrant the formation of a new trade group, known as the National Federation of Remedial Loan Associations.

In the late 1800s, less benevolent, for-profit “small loan agencies” emerged, lending “small amounts of money…for short periods of time, at rates often well above the statutory limits.” Some “used a number of subterfuges to [evade usury laws and] hide behind a tissue of legality.” But the true progenitor of the modern payday lender was the so-called “salary lender.” Beginning operations at the turn of the Century, these lenders were also known as “five for six boys” because they made small loans of $5 for a week or two, and received payment of $6 when the loan came due. As with modern payday lending practices, interest rates were extraordinarily high – ranging from 270% to 955% – and rollovers were common.
B. *The First Wave of Reform*

Public outrage over loans carrying triple-digit interest rates, spurred by individual horror stories of financial ruin, precipitated a reform movement. Arthur H. Ham – then director of the Russell Sage Foundation’s Division of Remedial Loans – led a campaign against loan sharks, and in 1913 proposed a model law to more fairly balance consumer and industry interests.

Mirroring the modern day, state-by-state, hand-to-hand combat between payday lenders and consumer advocates, the existing (and then-unlicensed) small loan industry fiercely opposed a series of iterations of what would ultimately become a model reform law. The “illegal lenders successfully parried every attempt by reformers to pass laws that would crowd out the high-rate lenders [and in] every case proposed bills were either defeated in their entirety or amended so that they lacked one or more of the key provisions.”

Eventually, Ham negotiated with a group of small loan lenders calling itself the American Association of Small Loan Brokers in an effort to reach consensus on a new regulatory regime. The reformers agonized over whether to accept what to them was a distastefully high interest in exchange for regulation and at least some rate ceiling designed to drive out the illegal and unlicensed loan sharks.

The parties finally agreed on a Uniform Small Loan Law in 1916. It was eventually enacted in 25 states (and Hawaii before it became a state), and featured an all-inclusive definition of interest, which established a maximum rate ranging from 2% to 3.5% per month (or 36% to 42% annual percentage rate). The new law required payments in manageable installments, costing an estimated 7.5% of the average monthly income of small loan borrowers. Licensed lenders operating under the law experienced relatively low default rates, which ranged from 1.1% to 4.3% of the amount loaned.
C. The Original Industrial Lenders

In 1917, following enactment of the Uniform Small Loan Law, the American Association of Small Loan Brokers renamed itself the American Industrial Licensed Lenders Association. The association’s new name reflected two distinct goals: (1) to differentiate its members from the disreputable lenders who had tarnished the industry’s image; and (2) to signal that the lenders considered the workers to whom the loans were targeted to be industrious contributors to the nation’s progress.

Interestingly, the rebranded association conceived of its business as “an exercise in philanthropy and social welfare, as a way of liberating workers from the clutches of poverty and the loan shark.” Members of the association saw themselves not as agents fostering financial servitude, but rather as facilitators of workers escaping debt and learning money management skills.

As the 1920s came to a close, “[i]ndustrial lending gave way to ‘personal finance.’” In 1929, the lenders’ trade group once again changed its name – this time to the American Association of Personal Finance Companies, signaling the changed emphasis in consumer lending. The major players were Household Finance Corporation (the oldest of the industrial lenders) and the newly formed Beneficial Industrial Loan Corporation.

D. Early Evaders

In contrast to the trade association member lenders, many industry actors had no interest in complying with the new Uniform Small Loan Law. Salary lenders transformed themselves into “salary buyers,” offering “to purchase a consumer's paycheck in advance at a discount [and give] the borrower $20 today for the right to receive the borrower's next paycheck of $24.” In recasting themselves, these lenders claimed the new law to be inapplicable to their business
model. Often, the loans were secured by wage assignments or, if unsecured, enforced by threats of garnishment (which could lead to termination of the employee-debtor).

Other small loan lenders attempted to avoid limits on interest rates imposed by state usury laws by characterizing the difference between the amount loaned and the amount repaid as fees. Some small loan lenders also sought and found loopholes in state laws to justify the excessive rates they desired to charge. Another ploy was to lend under statutes meant to govern building and loan companies, industrial banking companies, or other types of financial entities, in order to avoid regulation under recently enacted small loan laws. In his 1941 treatise, “The Development of Regulatory Small Loan Laws,” F.B. Hubacheck cited the “prostitution” of the Georgia building and loan acts as one of many egregious examples of inappropriate utilization of certain banking laws to elude restrictions imposed by small loan laws.

E. The Rise of the Modern Payday Lending Industry

Daniel Brook and others trace the invention of modern payday lending to a former credit bureau employee named James Eaton, who offered the first payday loan when he opened Check Cashing, Inc. on December 2, 1991 in Johnson City, Tennessee. Shortly thereafter, in 1993, W. Allan Jones, a colleague of Eaton’s from their credit bureau days, opened Check Into Cash. Brook describes Jones’ operation as “the first of the national payday-lending chains.” Jones is generally considered to be the father of the modern payday loan.

The growth of the industry has grown exponentially during the last two decades. In the early 1990s fewer than 200 payday lending stores were operating in the United States. Today, the Wall Journal reports that 23,000 payday lending stores, comprising a $70 billion market, offer payday loans in nationwide. Often cited is the startling fact that payday lending branches
in America outnumber the combined total of McDonald’s, Burger King, Sears, J.C. Penney, and Target stores.47

The meteoric rise of the payday lending industry is attributed to many factors, including: deregulation (or lax regulation) of financial services;48 the abandonment of small loan lending by finance companies;49 the failure of mainstream lenders to provide access to short-term, small-amount loans50 (and the resulting rise of the so-called “fringe” financial industry);51 the rise in the number of borrowers with impaired credit;52 imperfect market conditions;53 and the influence of campaign contributions and high-powered lobbyists on state legislatures.54

Nationally, the industry is dominated by large publicly traded companies.55 Mainstream financial institutions such as Wells Fargo and US Bank, which until recently were content to benefit as unseen financiers payday lenders,56 have begun offering payday loans themselves in the form of ATM advances against directly-deposited paychecks.57 Reportedly, these bank payday loans disproportionately impact elderly citizens; a recent Center for Responsible Lending study found that nearly 25% of bank payday loans were taken by Social Security recipients.58 These loans likely fall outside of the jurisdiction of state regulators.59

III. THE ARGUMENTS

Almost from its inception, the modern payday lending industry has been besieged by critics,60 the subject of intense scrutiny by federal and state regulators,61 and forced into a perpetually defensive posture.62 The industry has fought back, with support from its trade association,63 industry-sponsored studies,64 and influential federal and state political campaign contributions and lobbying efforts.65 The volume and intensity of the claims and counterclaims – critics call payday lenders “loan sharks” while lenders charge critics with perpetuating “myths” about the product – signify the white hot nature of the issue.66
Rhetoric and biases aside, the rise of the payday lending industry has generated significant academic analysis about whether the payday loan product is a consumer blessing or a societal curse. The following deconstructs the varied and plentiful arguments.

A. A Bridge Loan or a Debt Trap?

Payday lenders insist that their customers need a bridge over temporarily troubled financial waters but have been abandoned by traditional markets. Indeed, some borrowers do use payday loans as a solution to a temporary budget shortfall. As one commentator concludes, “If payday lending is used as a short-term emergency support system, the results are not offensive.”

However, critics argue that if the vast majority of borrowers took one or a handful of loans each year, the industry would not be continually embroiled in heated debate regarding the nature and merits of its product. Skeptics claim the signature feature of the payday loan is the creation of debt traps, sentencing borrowers to an endless cycle of debt.

Others suggest, incorrectly, that payday loans serve unbanked Americans. In fact, to obtain a payday loan, a borrower must have a job and bank account.

1. Is the Fundamental Payday Lending Business Model Designed to Entrap?

The industry trade association argues that payday loans are akin to “a financial taxi” meant to “cover small, unexpected, expenses between paydays.” Industry opponents counter that “significant evidence” suggests that the industry does not “truly [intend for] payday loans to be a one-time, short-term product.”

Michael Stegman and Robert Faris charge that the payday lender’s true goal is to keep borrowers in a state of “perpetual indebtedness.” Support for this view is substantial, and even bolstered by industry insiders. The Chief Operating Officer of payday lender Cash America, for
instance, offered the following advice to fellow payday lenders at a national conference: “‘[T]he theory in the business is you've got to get that customer in, work to turn him into a repetitive customer, long-term customer, because that's really where the profitability is.’”

Former industry employees as well validate the proposition that loan churning is at the core of the industry’s business model. 77 Michael Donavan, former District Director of Operations for the national payday lender Check ‘n Go, disclosed that the company trained salespeople “‘to keep customers dependent, to make sure they keep re-borrowing … forever, if possible…” 78 While Check ‘n Go’s public relations message characterized its loans as “a service…helping low-wage workers get cash for emergencies and bills,” Donavan revealed that in fact “the company's business model…depended on putting customers deeply in debt by turning their short-term loans into long-term, high-interest obligations.” 79 Cameron Blakely, a former Check n’ Go store manager, divulged that the company made obtaining a loan easy but terminating the lending relationship difficult: “[b]orrowers,” he said, “became ‘like indentured servants.’” 80 Another former industry employee succinctly summarized the fundamental business plan: “‘to get customers to keep getting loans and borrow up to their maximum approval amount whether they wanted it or not.’” 81

Other industry practices, such as incenting repeat borrowing, support the proposition that the goal of the industry is to foster loan churning. According to Graves and Peterson, “[i]nvestigations by federal banking regulators and statements of former payday lending employees confirm that payday lenders create compensation incentives encouraging employees to manipulate borrowers into long-term borrowing.” 82 In addition, ACE Cash Express, one of the largest national lenders, resigned from the industry’s trade association, refusing to “comply
with [best practice] provisions that would have limited the companies' ability to maximize rollovers.**83

Intentionality is clearly at the root of business practices designed to place payday borrowers on a debt treadmill. Nathalie Martin concludes that, “[i]n fact, the debt trap is the business plan.”**84

2. **Is Serial Borrowing In Fact the Norm Among Payday Loan Borrowers?**

According to Valparaiso University Law Professor Alan White, the industry’s claim that payday loans are used only for short-term emergencies is patently false.**85** Indisputable evidence exists that “[t]he vast majority of consumers…do not use payday loans as a temporary fix to manage a single crisis.”**86** As one analyst observes, “the American writing on predatory lending is awash with surveys and empirical data alleging that in reality the opposite is true -- and that many payday borrowers are borrowing for the long-term.”**87**

The Center for Responsible Lending (CRL), which has published numerous studies on the industry, has found that vast majority of borrowers are not one-time users of the payday product.**88** According to the CRL study, nearly one-quarter (24%) of payday loans are made to borrowers who take 21 or more per year and more than 60% are made to borrowers who take 12 or more per year.**89**

The overwhelming body of evidence shows that repeat borrowing is the norm.**90** As Graves and Peterson attest: “Virtually every study or investigation that has explored the issue has found that payday loan borrowers consistently fall into recurring debt patterns, where unpaid loans compound for longer periods of time.”**91** Even the industry’s own studies support these findings.**92**
Serial borrowing appears to be an inevitable consequence of the payday loan transaction. Borrowing a significant amount against the next paycheck ineluctably creates a cash flow problem for the next pay period and little alternative but to either roll over the existing loan or take a new one to make it to the next payday.93

Repeat borrowing is likely even more prevalent than the studies document because the data collected does not include customers who take loans from multiple payday lenders simultaneously – the so-called ‘‘borrowing from Peter to pay Paul’’ syndrome.”94 Finally, the fact that industry profits are generated from and are dependent on serial borrowing from the same customers provides conclusive proof that the occasional loan is the exception and the recurrent loan the rule.95

3. Is Continual Borrowing Merely a Sign of a Satisfied Customer Base?

The industry contends that high volume of repetitive loans only indicates a high degree of customer satisfaction.96 Others counter that the industry’s own claim that it fills a marketplace devoid of alternatives undermines its claim that repeat borrowing equates to a satisfied customer base.97

The industry claims that its record of minimal customer complaints to state regulators is further evidence of the value payday loans provide to customers.98 Detractors argue that there is often little connection between the magnitude of complaints and the degree of customer satisfaction with a product or service. Jessie Lundberg, for instance, contends that the absence of complaints is not necessarily indicative of sanguinity among consumers, explaining that:

Borrowers may not know where to complain, and may not be sufficiently aware of applicable lending laws to know whether their rights were violated. Some borrowers are hesitant to seek help because of the stigma attached to admitting financial problems. In addition, many of the most problematic characteristics of the loans are currently
legal under state laws, and thus do not form the basis for a complaint.99

Another industry observer, Pearl Chin, concurs that customer “silence…may have little to do with customer satisfaction.”100 She identifies an Illinois Department of Financial Institutions report supporting Lundberg’s conclusions that customers are often unaware regulatory agencies, ignorant that certain practices may violate state law.101 She offers the fact that “many borrowers are embarrassed by their financial situation and [are] reluctant to draw attention to their debt-related problems” as a strong reason that few register complaints with government officials.102 In short, the proposition that repeat borrowing reflects satisfied not entrapped customers is questionable at best.

B. Does the Risk Justify the High Cost of Payday Loans?

Annual percentage rates associated with payday loans nationally have been reported to range “between 400% and 1,000%.”103 Industry defenders cite the degree of risk these loans bear to justify these high APR’s.104 Chad Ciccone, for example, argues that payday lending is “inherently risky” because it is premised “on providing unsecured credit to consumers with poor credit history.”105 In his 2006 article favorably comparing payday lending with subprime mortgage lending, Ciccone makes the assertion proven by subsequent events to be inaccurate that “subprime lending, although certainly riskier than mainstream lending, has a place in the market.”106 He concludes that the interest rate on payday loans is “commensurate with the risk.”107 However, empirical evidence does not support his conclusion.

Michael Kenneth counters that payday loans are high cost, but not high risk.108 Even some industry supporters agree. Two of them, Mann and Hawkins, acknowledge that the “overwhelming majority of payday lending transactions do not result in default.”109 Further, as Hawkins points out, repayment of payday loans are “virtually guaranteed.”110
Default rates on payday loans are substantially lower than for other forms of credit, such as credit cards.\textsuperscript{111} Between 2007 and 2010, the payday loan default rate as a percentage of dollars loaned in Minnesota, for instance, was 2.6%.\textsuperscript{112} By contrast, data from the Federal Reserve show that, during that same period, default rate on credit cards averaged 7.1%.\textsuperscript{113}

Significant concerns about industry business practices have been raised by the Federal Deposit Insurance Corporation (FDIC), which reports that payday lenders generally fail to adequately underwrite their loans and remain deliberately ignorant of a borrower’s ability to pay.\textsuperscript{114} The FDIC’s findings are echoed by many others, who criticize the lax or nonexistent underwriting standards employed by payday lenders.\textsuperscript{115} Industry critics make the analogy between payday lenders and loan sharks with respect to the deliberate failure to employ basic underwriting standards when making loans.\textsuperscript{116} In sum, as Charles Bruch asserts, there is simply a “lack of [a] quantifiable, risk-based justification” for the excessively high rates payday lenders charge.\textsuperscript{117}

C. \textit{Is It Fair to Express the Cost of a Payday Loan Using an APR?}

Significant attention has been focused on the use of the annual percentage rate to signal the cost of a payday loan.\textsuperscript{118} The industry insists that application of an annual rate to a two-week loan is inappropriate.\textsuperscript{119} For example, industry defender Aimee A. Minnich maintains that using the APR “distorts the issue and serves only to inflame bias against lenders.”\textsuperscript{120}

However, critics argue that if the borrower’s relationship with the lender extends for a good portion of a year, then using the APR to express the cost of payday credit is perfectly apt.\textsuperscript{121} In fact, data indicates that the typical borrower takes many loans over the course of a year, and thus the use of an annual percentage rate is indeed appropriate to disclose the true cost of payday credit.\textsuperscript{122}
D. Is Payday Lending Linked to Financial Distress and Bankruptcy?

Studies may be found supporting both sides of the question concerning taking payday loans and either financial distress or bankruptcy is interrelated. Industry supporters deny a correlation and one, Jim Hawkins, argues that payday loans actually “insulate” borrowers from financial distress.\textsuperscript{123} He reasons that because payday loans are either capped by statute or limited by lenders to a portion of income, “it is nearly impossible for borrowers to take on unmanageable debt loads.”\textsuperscript{124} Others, like Petru S. Stoianovici and Michael T. Maloney, dismiss any connection between payday lending and bankruptcy.\textsuperscript{125} Dr. Donald P. Morgan, a staffer at the Federal Reserve of New York, and Michael R. Strain, a graduate student, suggest the bankruptcies are more likely in states without payday lending. Their findings are based on a study conducted of the financial aftereffects of a ban on payday loans in Georgia and North Carolina.\textsuperscript{126}

The opposite view holds that if borrowers were not already in financial distress they would not be seeking payday loans in the first place. Hawkins study itself provides contradictory findings on the matter; he at once opines that “the link between fringe banking and financial distress is dubious”\textsuperscript{127} and admits “[t]he clearest link between a fringe banking product and financial distress is payday lending.”\textsuperscript{128} In a recent Quarterly Journal of Economics article, Brian Meltzer finds “no evidence that payday loan access mitigates financial distress,”\textsuperscript{129} and in fact concludes that payday loans actually “increases the likelihood of financial distress.”\textsuperscript{130}

Morgan and Strain’s research on the correlation between payday lending and bankruptcy has been maligned. The Center for Responsible Lending calls their analysis “highly-flawed.”\textsuperscript{131} Specifically, CRL complains that “Morgan and Strain’s data and research methods are not adequate to support these findings... because the authors consistently intermingle data from
Georgia and North Carolina—which outlaw payday lending—with data from states which allow it…and [they] ignore important data that does not support their arguments.”

While a few studies suggest no correlation, a wide variety of other research suggests a strong link between payday lending use and bankruptcy filings. In 2008, Dr. Paige Marta Skiba, Assistant Professor of Law at Vanderbilt University, and Dr. Jeremy Tobacman, Assistant Professor of Business and Public Policy at the Wharton School of University of Pennsylvania, analyzed 145,000 payday loan applications from “a proprietary dataset from a large payday lender” in Texas, matching them to public records. Their study shows “that for first-time applicants near the 20th percentile of the credit-score distribution, access to payday loans causes Chapter 13 bankruptcy filings over the next two years to double.

Jacqueline S. Akins similarly found a greater likelihood of bankruptcy filings among service members accessing payday loans. Leah Plunkett and Ana Luca Hurtado cite “[n]umerous research studies [that] warn of the dangers associated with payday loans, including significantly higher rates of bankruptcies.” Nathalie Martin and Koo Im Tong have found that “the correlation between bankruptcy and payday loans seems to be getting stronger.” Loyola University of Chicago Professor Robert Mayer found that “the typical payday loan…debtor [goes] bankrupt more quickly” than bankruptcy filers without payday loan debt.

Industry supporters reject the notion that payday lending and bankruptcies are linked. The weight of existing evidence, however, suggests otherwise.

E. The Payday Lending Market: Efficient or Flawed?

According to a large number of studies, the payday market is seriously defective. Nathalie Martin calls it “classically flawed.” Analysts offer several reasons why this particular market performs sub-optimally.
1. **Rates are Unaffected by Competition**

   Competition lowers or moderates prices when free markets work correctly.\(^{142}\) However, as Ronald J. Mann and Jim Hawkins the payday loan market is not competitive.\(^{143}\) They lament that “there is little reason to be sanguine about the robustness of competitive forces.”\(^{144}\) Lenders typically lend near or at the maximum rates allowed, regardless of the level of competition for their business.\(^{145}\)

2. **Informational Asymmetry Results in Cognitive Consumer Failures**

   That fully informed consumers making rational choices results in “meaningful competition” and properly functioning markets is a fundamental economic axiom.\(^{146}\) But with respect to the payday lending market, the vast majority of borrowers are “imperfectly informed and imperfectly rational.”\(^{147}\) The following explores in depth why the payday lending market operates outside normative economic models.

   a. **Ease of the Transaction**

      On the surface, a payday lending transaction seems simple and straightforward, the antithesis of, say, purchasing a home. The payday loan application is typically short and uncomplicated.\(^{148}\) Indeed, industry boosters often cite as one of the most attractive features of entering into a payday loan transaction its ease and convenience.\(^{149}\)

      The mechanical simplicity of the transaction masks its hidden complexities, while the casual nature of the transaction belies its dangers. The characteristics lenders trumpet are the very ones that entice borrowers to endlessly renew loans. Other inducements to repetitive borrowing include offers of free initial loans, loyalty and rewards programs for frequent borrowing, and cash payments for referrals.\(^{150}\) Lundberg suggests that “the circus-like
storefronts and catchy jingles” of payday lenders mask “darker stories of financial devastation.”

The lure of easy money is a deterrent to a more lasting solution to borrower’s financial shortfalls. Embarrassment over financial difficulties is a common trait among borrowers, leading them to choose the initially friendly storefront lender (or completely anonymous Internet lender) who asks few questions over the more difficult path of confronting debt, admitting financial desperation, and seeking assistance from family, friends, or professionals. 

b. **Lack of Consumer Awareness**

Payday lenders “give the impression that they are providing a valuable product to savvy consumers.” But even industry supporters admit that “payday lending transactions tax the cognitive capabilities of the typical customer in ways that lead to market failures of one sort or another.”

The following factors call into serious doubt industry claims that they serve enlightened customers who make fully informed choices in the marketplace.

- **True Costs of Loan are Not Often Obvious.**

  Consumers of course know the dollar amount of fee charged on a payday loan. However, they suffer from “a deep misunderstanding…of the true cost of the loans.” Consumer confusion stems from, among other things, “math innumeracy” and a lack of understanding of Truth in Lending Act disclosures. Research also suggests consumers fail to take account of the high additional costs in the event of the inability to repay the loan.
Some assert that lenders intentionally withhold or manipulate disclosures to the detriment of full borrower awareness of the costs of the transaction. But even assuming borrowers have the necessary information, they typically do not possess the financial literacy skills to adequately process or analyze it.

In their 2008 analysis in the Yale Journal on Regulation of consumers’ ability to understand Truth in Lending disclosures, Elizabeth Renuart and Diane E. Thompson identify three components of literacy – prose, document, and quantitative literacy – and find that “consumers lack sufficient literacy in all three spheres to face modern credit contracts with any degree of confidence.” This finding is consistent with that of a 1992 national adult literacy study that, alarmingly, showed that “most consumers lack the basic literacy skills to understand and compare loan agreements.”

Even staunch industry supporters acknowledge that textbook economic theories do not apply in the payday loan context. Michael C. Tomkies, in his 2008 article in Business Law Today entitled, Regulating the Subprime Market, touts the payday loan business model “[a]s a short-term answer to temporary credit needs.” Tomkies, however, admits that borrowers may misuse the product because of, among other things, “lack of financial education [or] vulnerability.”

- The Difficulty of Comparison Shopping

Payday loan shopping, unlike shopping for other goods and services, presents barriers for comparison to other financial products. As Mann and Hawkins indicate, for example, “comparing a depository bank's overdraft product to a payday loan requires considerable sophistication.” They also note that consumers with urgent needs for cash likely have “limited
taste for price shopping [and this circumstance] is exacerbated by the small size of the loans, which makes the gains from even a major price difference quite small as an absolute matter.”

c. A Rational, Informed Free Choice?

Under the rational free choice theory, all consumer behavior “is fundamentally rational in character,” based on a cost-benefit analysis, and driven solely by “self-interest.” To adherents of this theory, prohibition or strict regulation of payday lending “is ardently paternalistic,” limits free choice, and harms the financially struggling consumers whom advocates desire to help. This line of reasoning posits that market forces and competition – not regulation – work best to protect consumers’ interests. By this reckoning, as one commentator insists, “[if] a competent adult wants to pay triple-digit interest rates, he or she should not be hindered from doing so.”

While some question whether, in practice, even mainstream markets operate as economic theory suggests, there is no doubt that fringe markets do not follow traditional economic efficiency models. Payday lending markets fail because borrowers do not operate under the rational free choice theory. In fact, one scholar has declared emphatically that “[i]t is now widely recognized that rational choice theory is empirically false.”

A rising new school of thought about how consumers generally – and payday lending borrowers specifically – act in the marketplace is gaining currency. Behavioral law and economics, “a multidisciplinary movement committed to the idea that legal regulation ought to be based upon a more realistic conception of human decisionmaking,” is replacing rational free choice theory as the more accepted explanation for purchasing decisions. Under this more empirical approach, “scholars draw on social science research to demonstrate that people make potentially suboptimal or irrational choices in a wide range of significant life activities – ‘decisions that are unwise even according to their own values and preferences.’” Even
industry supporters agree that “[b]ehavioral economists have offered significant evidence against the rational actor model of consumer decision making.”\textsuperscript{179}

Thus, it may be persuasively argued, borrowers are not acting in an informed and economically rational manner when taking payday loans. As Mann and Hawkins acknowledge, “[i]t is simply not plausible…that a person of ordinary capacity would sensibly decide to borrow money at a rate of 400 percent, using a loan that, in most cases, is likely to remain outstanding for months, if not years.”\textsuperscript{180}

The payday lending market is fatally flawed. As Graves and Peterson note, even our “most venerated economist, Adam Smith, recognized the need for laws placing a reasonable ceiling on credit pricing [and] that the market for loans could never be expected to perform efficiently so long as [borrowers] could be enticed into loans contrary to their own best interest.”\textsuperscript{181}

F. Is the Payday Lending Industry Ethically Challenged?

Some believe that payday lenders have a legitimate place in the spectrum of credit providers.\textsuperscript{182} Others conclude that payday lending business is “unseemly”\textsuperscript{183} because it profits from others’ misery.\textsuperscript{184} Questions have been raised as to whether the industry attracts a criminal element.\textsuperscript{185} Court files throughout the country are replete with actions claiming – and judicial opinions are rife with holdings confirming – attempted evasions of state law and violations of federal law,\textsuperscript{186} state law,\textsuperscript{187} and common law.\textsuperscript{188}

1. The “Rent-a-Bank” and “Rent-a-Tribe” Schemes

When states began restricting the ability to offer payday loans (by enacting bans or instituting rate caps), payday lenders devised a circumvention tactic known as “rent-a-bank” or “rent-a-charter.”\textsuperscript{189} To evade state regulation, lenders affiliated with out-of-state banks owning
charters in jurisdictions with lax or non-existent regulation.\textsuperscript{190} Justification for the utilization of this scheme purportedly lay in the landmark 1978 United States Supreme Court holding in \textit{Marquette National Bank of Minneapolis v. First of Omaha Service Corp.}, which allowed the exportation of interest rates allowed by a bank’s home state to a consumer in another state.\textsuperscript{191}

For a time, this artifice proceeded without interference. Eventually, legal challenges were mounted by State Attorneys General and consumer advocates.\textsuperscript{192} Federal regulators with authority over the banks whose charters were being rented subsequently halted the practice.\textsuperscript{193}

More recently, as states have increasingly prohibited or limited payday lending, a new evasion ploy known as “rent-a-tribe” has emerged.\textsuperscript{194} Some payday lenders have begun legal partnerships with tribal entities in an effort to use the tribe’s sovereign status to claim immunity from state governance and regulation.\textsuperscript{195}

As the payday lending phenomenon has grown, so has disquiet about its deleterious impacts.\textsuperscript{196} Several states have never authorized payday lending and govern short-term, small-amount lending under existing banking or usury laws.\textsuperscript{197} The North Carolina Legislature allowed enabling statutes to sunset in 2001, which placed payday loans under the general statutory interest rate cap.\textsuperscript{198} In 2008, voters in Arizona, by a 60\% to 40\% margin, eliminated payday lending by refusing to overturn the expiration of their statutory authority to operate.\textsuperscript{199} Ohio and Montana have approved ballot initiatives curbing payday lending by instituting a 28\% APR rate cap.\textsuperscript{200} In all, 17 states and the District of Columbia prohibit or severely restrict payday lending.\textsuperscript{201} One of those states criminalizes the practice.\textsuperscript{202}

2. \textbf{Other Evasions of State Law}

Payday lenders have attempted other schemes to directly or indirectly circumvent state laws governing payday loans. Foremost is the ardent quest for loopholes.\textsuperscript{203} In state after state,
lenders have looked for ways to avoid the very laws intended to govern them. In Illinois, payday lenders began offering payday loans extending for 121 days when a law passed requiring installment repayments for payday loans whose terms extended for up to 120 days. Payday lenders in Minnesota, Ohio, and South Carolina obtained licenses in other lending categories in order to either charge higher rates than existing payday lending laws permitted or avoid entirely compliance with payday lending statutes. In Arizona, payday lenders skirted the ban on payday lending by purporting to offer “prepaid debit cards.” Payday lenders in Texas, Florida, and Virginia claimed to offer not payday loans, but rather “credit repair services,” while others have disguised the nature of the loan so as to appear not to be a payday loan and subject to state laws. In other cases, payday lenders have sought to evade state payday lending restrictions by setting up an off-shore shell company or claiming that state laws are inapplicable if loans are made through the Internet.

3. Violations of State Law

Throughout the country, courts are dealing with allegations by consumers, state banking officials, and Attorneys General that payday lenders violate state lending, banking, licensing, consumer credit, usury, consumer fraud, deceptive trade practices, and payday loan laws. Several other judicial actions against lenders have stated viable common law claims. One court chastised national lender Advance America for “injur[ing] the economic health and well-being of the Pennsylvania consumer/borrower by illegally charging sham interest.” The number and scope of these cases suggest inordinately frequent legal transgressions by the industry.

4. Questionable Collection Tactics
When borrowers are unable to repay their payday loans, lenders naturally seek collection. Questions have arisen as to whether certain collection tactics of payday lenders are extralegal. Tales of payday lender collection tactics are almost beyond belief, such as the cases in which payday lenders refused to return a borrower’s vehicle, threatened the borrower with arrest, or locked a borrower in the store until the payday loan was repaid. Court records also indicate a substantial number of allegations and findings of violations of the Fair Debt Collection Practices Act.

F. Are the Alternatives Worse?

One of the central arguments of payday lending proponents is that elimination of the product does not eliminate the financial problems of borrowers; it merely forces the adoption of even less desirable alternatives. Without the payday lending option, promoters warn, borrowers will incur comparatively more costly charges (including overdraft fee and insufficient funds penalties). Others have opined that state economies suffer when payday lending is banned. According to Morgan and Strain, in their study comparing two states that ban payday lending with others that permit it, the inevitable result of payday loan bans is more bounced checks, more complaints to the Federal Trade Commission, and more Chapter 7 bankruptcy filings.

The weight of the evidence, however, does not support a conclusion that payday loans are less expensive than alternatives or that borrowers are better off with payday loans than without them.

1. Do Payday Loans Actually Cost Less than Alternatives?

Countering the frequent refrain that the payday product is cheaper, the Center for Responsible Lending argues that in fact “[t]he typical payday loan is more than twice as
expensive as a credit card late fee, and much more costly than paying bills late.”

CRL further calculates that a $1,000 from a finance company for a year carries a lower debt service than a $300 payday loan over the same period. Further, evidence suggests a correlation between taking payday loans and incurring bank fees because activation of the automatic withdrawal feature of the loan leads to greater insufficient fund fees upon default.

Payday lending, even if it may be less expensive initially, turns out to be much more expensive in the long run. As Professor Alan White explains, after taking multiple loans, which most borrowers do, “interest begins to exceed the principal, and it is very difficult to argue that such a transaction has increased a consumer's welfare, even compared to onerous alternatives such as paying overdraft or late fees.”

2. **Invisible Costs Not Included in Any Cost/Benefit Analysis**

External societal costs associated with payday lending adversely impact not only individuals and families, but also other sectors of the state and local economy. For example, in a recent economic study, Professor Melzer found that access to payday lending does not “alleviate [financial] hardship [but] on the contrary, leads to increased incidence of difficulty paying mortgage, rent and utilities bills; moving out of one’s home due to financial troubles; and delaying needed medical care, dental care and prescription drug purchases.”

Another industry critic argues that “payday lending also harms other businesses by capturing disposable income that would otherwise be paid to landlords, utility companies, professional service providers, and other creditors.” Finally, a recent study by economists at Harvard and Oxford Universities found that payday lending, not poverty, leads to involuntary bank account closures, further damaging economic vitality in a community and state.
Payday lending places stress, not only on private sector actors, but also on public sector agencies. As one analyst points to “[m]ounting evidence [that the characteristics of a payday loan] undermine borrowers' financial stability, which in turn increases demands on social service agencies, public assistance programs, and, ultimately, the taxpayer.” Another contends that the spillover effects of payday loans adversely impact other parts of the societal network because “beneath the radar, customers turn to social service organizations to provide assistance with food, clothing, rent, and mortgage payments.”

Perhaps the most tragic impacts of payday lending are those experienced by the borrowers and their families. The United States Department of Defense conducted a study of the impacts of payday loans and other predatory financial products on service members and their families, and concluded in a devastating report on the fringe lending industry that payday lending and other such services “can leave a Service member with enormous debt, family problems, difficulty maintaining personal readiness, and a tarnished career.” At the department’s urging, Congress enacted a cap on interest rates on payday loans to military personnel and their families at 36% APR.

3. Life Without Payday Loans

Proponents proclaim the benefits of payday lending. Aimee A. Minnich, argues for “rational regulation” of the industry, concluding that banning payday loans “unnecessarily restricts consumer access to potentially helpful products.” Opponents argue that society is better off without payday lending. One critic has gone so far as to analogize “peddling payday loans to selling heroin.” Another, acknowledging the booming business of the payday lending industry, suggests that “a large portion of this demand is attributable to hardships created by the loans themselves.”
The only analysis, albeit qualitative, of what payday borrowers themselves experience when a state bans the product is the survey conducted by the Center for Community Capital at the University of North Carolina at the behest of the North Carolina Commissioner of Banks following the elimination of payday lending from that state in 2006. The findings are instructive:

- 90% of former borrowers said payday lending is “a bad thing”;
- 75% indicated that ban made no difference in their lives;
- By a 2-1 margin, former borrowers responded that the ban was more a blessing than a bane.
- Borrowers lamented that payday loans are “easy to obtain” but difficult to discontinue, as many got caught into “taking loans on a regular basis.”

Moreover, the researchers found “no significant impact on the availability of credit” post-ban. In fact, after the ban, personal finance companies in North Carolina increasingly began offering loans under $600 with interest rates capped at the 36% APR. Essentially, former payday borrowers said to the former payday lenders: “Don’t let the door hit you on the way out of the state.”

IV. CONCLUSION

Even payday lending’s most strident critics would agree that a demand exists for small-dollar, short-term loans for a segment of financially struggling consumers. But access to credit at any cost – both financial and human – is unjustifiable, and the market response payday lenders offer is indefensible.

In the wake of the nation’s economic crisis, nontraditional products and practices, such as negatively amortizing loans and credit default swaps, but the fundamental structure of banking system itself has not been questioned, and the banking industry will not collapse by making
conventional loans. In contrast, the payday lending business model has come under fire. Characterized by interest rates that under any other circumstances would shock the conscience, the basic business approach of payday lenders is deliberately calculated to foster perpetual debt; in fact, that is the only way the industry can survive.

The degree to which payday lending has been pilloried, not only by the Department of Defense, but also by state regulators and consumer advocates in virtually every state, cannot be ignored. Despite the desperate attempts to defend its product, the avalanche of evidence leads to the inescapable conclusion that, even if there are no alternatives, consumers are better off without payday lending.

The ongoing, polarizing debate about payday lending leads only to a false choice between two unsatisfactory results: continue to sanction a dangerous and predatory financial product or ignore the fact that the mainstream financial services system simply does not work for many Americans.

The real solution to the never-ending debate over whether payday lending in its current guise should be permitted to exist is to build on and scale existing and successful alternatives. The answer is to create a nationwide system of suppliers of short-term credit whose goal is not to foster perpetual indebtedness, but rather to facilitate individual and family financial stability and growth by offering needed credit under reasonable terms. Credit unions and Community Development Financial Institutions around the country have established a model, providing small amount loans at reasonable interest rates, payable within a brief term, often through an installment repayment plan.247

Payday lending erodes wealth and creates financial insecurity.248 Public policies ought to encourage wealth building and financial stability, which in turn leads to family prosperity and
economic growth. State and federal governments, nonprofits, responsible corporations, faith-based groups, and philanthropic organizations together need to develop a sustainable financial system for those for whom traditional credit is unattainable or undesirable with the exploitation offered by marginal lenders. Creation of such an infrastructure will by no means be easy, but the status quo is unacceptable. But if the will is there, the way will follow.

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1 Jessie Lundberg, Big Interest Rates Under the Big Sky: The Case for Payday and Title Lending Reform in Montana, 68 MONT. L. REV. 181, 182 (2007).


4 Calder, supra note 3, at 120 (identifying the Hebrew Free Loan Society as an example of a philanthropic lender and noting the interest-bearing loans “operating on the principle of ‘philanthropy + 6 percent’”).

5 Id.

6 Id.

7 Id. at 121.

8 Id. at 50.

9 Id. Calder relates the gambit of one lender who required customers to purchase a worthless oil painting to create the illusion of a sale rather than a loan above usury rates. Id.


Id. at 619 (citing William Hays Simpson, *Costs of Loans Under Unregulated Lending*, 8 L. & CONTEMP. PROBS. 73, 74-75 (1941)).

F.B. Hubacheck, *The Development of Regulatory Small Loan Laws*, 8 L. & CONTEMP. PROBS. 108, 121 (1941) (explaining that “[t]he practice of a wage buyer was to go through the motions of purchasing a portion for the earned wages at a discount…which presumably was compensation for waiting until pay day. As such employees are seldom able to repay the full amount from one pay check, and as the wage buyers refuse to take partial payments, the process is repeated indefinitely”).

See, generally, Drysdale & Keest, * supra* note 10, at 620; see also Simpson, * supra* note 12, at 76 (relating the story of Mr. B. “[a] mill employee for 15 years [who], earns $28 a week. He supports a wife and two children. When his wife was sick three years ago, Mr. B borrowed $15 and has regularly paid $3 a month interest ever since. He still owes the $15 but has paid $108 in interest charges”).


See Drysdale & Keest, * supra* note 10, at 620; see also William Trufant Foster, *The Personal Finance Business Under Regulation*, 8 L. & CONTEMP. PROBS. 154 (1941) (quoting a leader in the unlicensed small loan industry as saying: “We all know that such a law will put us all out of business.”).


Id. at 126-27.

Id.

Id.


Collins, * supra* note 11, at 58-59 (describing the definition as “including any ‘consideration contracted for, collected or received by the lender’”).

See Drysdale & Keest, * supra* note 10, at 620. See also Hubacheck, * supra* note 13, at 119.

See Drysdale & Keest, * supra* note 10, at 620.


Calder, * supra* note 3 at 137 (noting also that “industrial” was dropped from the name in 1921).
Id. at 137-138, 142 (listing association actions “‘elevating the tone’ of the small-loan business,” including: moving offices “out of second-floor rooms at the top of narrow, dark stairs”; changing times of business to daylight hours to avoid the impression of the industry as “‘the spider awaiting the casual fly’”; and, rather than promising “‘Quick Money’ and ‘Easy Credit,’” appealing to borrower’s desire to help a family member in time of sickness or need).

Id. at 111.

Id. at 144 (describing lenders’ goals as helping workers “get…out of debt and teach[ing] them to budget their earnings”).

Id. at 147.

Id. at 148.

Id.


Id. at 50, 139 (describing the subterfuge used by salary buyers to evade lending laws and presenting the example of the owner of a chain of business who claimed that salary buyers were “no more subject to usury laws than any other traders in commodity futures”).

Drysdale and Keest, supra note 10, at 619.

Collins, supra note 11, at 55; Nugent, supra note 21, at 5-6.

Nugent, supra note 21, at 10.

Collins, supra note 11, at 65-66 (commenting that “The Industrial Banking Act . . . is currently becoming the haven for unscrupulous lenders of [small loans] for short terms and leads to repeated transactions covering a single continuous indebtedness”). See also Hubacheck, supra note 13, at 128 (citing the misuse of building and loan or industrial loan acts and “discount company acts” in California, Florida, and Missouri); and Nugent, supra note 21, at 10 (identifying the misuse of the Oregon Motor Vehicle Finance Act by small lenders to obtain “exorbitant rates of charge” and the “manipulation” of California’s industrial banking act to produce excessive yields). Another ploy used by lenders of the day charged with violating existing usury and state interest rate restrictions was to claim that the difference between the amount loaned and the amount repaid consists of fees, not interest. See e.g., Collins, supra note 11, at 55, and Nugent, supra note 21, at 5-6.

Hubacheck, supra note 13, at 128. See also Nugent, supra note 21, at 10 (calling the misuse of the Georgia building and loan act “a perversion”).

Daniel Brook, Usury Country: Welcome to the Birthplace of Payday Lending, HARPER’S MAGAZINE, April 2009, at 41-43.

Id.

Id.

45 Brook, supra note 41, at 43. See also GREGORY ELLIEHAUSEN, AN ANALYSIS OF CONSUMERS’ USE OF PAYDAY LOANS 1 (2009).


47 Brian M. McCall, Unprofitable Lending: Modern Credit Regulation and the Lost Theory of Usury, 30 CARDOZO L. REV. 549, 553 (2008).


49 Michael S. Barr, Banking on the Poor, 21 YALE J. ON REG. 121, 152 (2004).

50 Faller, supra note 44 at 125, 133 (noting that “[p]ayday loans do fill a gap in the market that is generally not served by mainstream lenders”). See also Schaaf, supra note 48, at 340 (asserting that that “[t]he large growth of the payday lending industry can be attributed to [among other things] the absence of traditional small loan providers in the small-sum, short-term credit market”); Ronald J. Mann & Jim Hawkins, Just Until Payday, 54 UCLA L. REV. 855, 857 (2007) (asserting that “banks generally refuse to make the short-term, risky loans many of [payday lending] consumers seek”) and Steven B. Potter, Befriending Payday and Small Loan Businesses—A Smart Move for the Banking Industry? 119 BANKING L.J. 636, 636 (2002) (concluding that “[t]he emergence of the payday loan business is a function of traditional lenders’ exit from the small, unsecured loan business”).

51 Drysdale & Keest, supra note 10, at 590 (observing that the fringe banking industry “has become a major source of traditional banking services for low-income and working poor consumers, residents of minority neighborhoods, and people with blemished credit histories”). See also Elizabeth Renuart & Diane E. Thompson, The Truth, the Whole Truth, and Nothing But the Truth: Fulfilling the Promise of Truth in Lending, 25 YALE J. ON REG. 181, 196 (2008) (identifying payday lending as part of the fringe financial industry); and Mann and Hawkins, supra note 50, at 857 (observing that fringe credit providers stepped in to make loans mainstream financial institutions refuse to make).


53 Michael Bertics, Fixing Payday Lending: The Potential of Greater Bank Involvement, 9 N.C. BANKING INST. 133, 142 (2005) (finding that the payday lending market exhibits factors of an imperfect market, including “tacit price collusion” and maximization of profit based on buyer need).

54 Creola Johnson, Payday Loans: Shrewd Business or Predatory Lending?, 87 MINN. L. REV. 1, 133 (2002) (citing the payday loan industry’s “strong lobby”); Christopher L. Peterson, Usury Law, Payday Loans, and Statutory Sleight of Hand: Salience Distortion in American Credit Pricing Limits, 92 MINN. L. REV. 1110, 1111 (2008) (observing that the payday lending industry spends “millions on lobbying”); Nathalie Martin, 1,000% Interest-Good
Lori Lothring, Payday Lenders: The Industry, Leaders, Owners, and Regulation (2009) (noting that payday lending “is a lucrative industry dominated by large publicly traded companies” and noting the substantial net income of several players that dominate the market, including Cash America International Inc., Advance America Cash Advance Centers Inc., World Acceptance Corporation, and QC Holdings, Inc.). See also Huckstep, supra note 35, at 205 (indicating that “seven of the largest payday lenders now have publicly traded stock”).

See e.g., Michael Kenneth, Payday Lending: Can “Reputable” Banks End Cycles of Debt? 42 U.S.F. L. Rev. 659, n. 297 (2008) (observing that “Wall Street has earned profits from the [payday lending] industry,” reporting that Citigroup helped to underwrite the initial public offerings…for Dollar Financial, a significant payday lender, and commenting that “banks fear public perception of payday loans [because] most people associate payday loans with exploitation”); Ron Nixon, Dee DePass, and Terry Collins, Borrowing Trouble: Banks have Financed Payday Lenders’ Expansion, STAR TRIBUNE, August 15, 2004 (reporting that “[b]anks have been a main source of business loans for payday lenders at the same time that the banking industry has been pulling branches from low-income areas,” naming dozens of banks, including Wells Fargo, as having “financial relationships with payday lenders,” and identifying what at that time was “the nation's second-largest check-cashing and payday-loan chain [having] a $9 million line of credit with Wells Fargo”); Richard J. Thomas, Rolling over Borrowers: Preventing Excessive Refinancing and Other Necessary Changes in the Payday Loan Industry, 48 WM. & MARY L. REV. 2419-20 (2007) (stating that, “[a]ccording to documents filed with the Securities and Exchange Commission, Wells Fargo has extended millions of dollars of credit to the nation's largest payday loan chain”); and Mann & Hawkins, supra note 50, at 867-68 (averring that most of the large national payday lenders are funded by some of the largest banks).

See e.g., Candice Choi, Big Banks Offer Payday Loans, MIAMI HERALD, August 26, 2011 (citing Wells Fargo, U.S. Bank, and Fifth Third Bank as offering payday loans called direct deposit loans); Chris Serres, Biggest Banks Stepping in to Payday Arena, STAR TRIBUNE, September 9, 2009 (reporting that “the nation’s largest banks -- including Minneapolis-based U.S. Bancorp, Wells Fargo & Co. of San Francisco, and Fifth Third Bancorp of Cincinnati -- are now marketing payday loan-type products”); Thomas Lee, Bridging the Gap: U.S. Bancorp and Wells Fargo Have Gotten Into the Lucrative Business of Letting Customers Borrow Against their Next Paychecks, STAR TRIBUNE, January 22, 2007 (reporting that two of the largest banks in Minnesota were beginning to “offer direct-deposit checking customers cash advances on future paychecks” and quoting a bank representative expressing concern that payday loans carried negative connotations); and Turner Hutchens, Banks Offer Payday Loans for Quick Cash, NASHVILLE BUSINESS JOURNAL, April 3, 2009 (reporting that “Fifth Third Bank and U.S. Bank — respectively the fourth and eighth largest Nashville banks by deposits — have programs offering 35-day payday advance loans to customers with direct deposit paychecks”). See also CENTER FOR RESPONSIBLE LENDING, BIG BANK PAYDAY LOANS (2011) (finding that payday-type lending by mainstream banks is a growing problem).

CENTER FOR RESPONSIBLE LENDING, BIG BANK PAYDAY LOANS, supra note 57.

See, e.g., Nelson v. Citibank., 794 F. Supp. 312 (D. Minn. 1992) (holding that allegations charging national bank with violating state usury law by assessing certain fees were preempted by the National Bank Act).

Adam L. Bodeker, Meghee v. Arkansas State Board of Collection Agencies: Arkansas Shows Predatory Lenders the Door, 63 ARK. L. REV. 645, 663 (2010) (observing that the payday lending has “come under attack in many states”).


See, e.g., Christopher Conkey, Payday Lenders Strike a Defensive Pose, WALL ST. J., Feb. 21, 2007, at A18.
The Community Financial Services Association of America (CFSA), which describes itself as “the national organization dedicated to advancing financial empowerment for consumers through small dollar, short-term loans.” Community Financial Services Association of America, Home Page; at http://cfsaa.com/.

See e.g., Thomas, supra note 56, at 2401, 2404-05 (citing a survey of customers “financed in part by the Community Financial Services Association of America [that] has serious flaws that cast doubt on its results”).

Sewel Chan, A Consumer Bill Gives Exemption on Payday Loans, N.Y. TIMES, March 9, 2010 (attributing the successful maneuver by United States Senator Bob Corker to have a provision removed from draft legislation that would have empowered federal authorities to crack down on payday lenders to the political influence of and “significant” campaign contributions made to him by the payday lending industry). See also Cary Spivak and Patrick Marley, Payday Lenders Giving Lobbyists Big Paydays to Stop Interest Cap, MILWAUKEE JOURNAL SENTINEL, Aug. 2, 2009 (reporting that “more than two dozen influence-peddlers [were hired by the payday lending industry to] fight a proposed 36% cap on interest rates”).


See e.g., Diane Hellwig, Exposing the Loansharks in Sheep’s Clothing: Why Re-Regulating the Consumer Credit Market Makes Economic Sense, 80 NOTRE DAME L. REV. 1567, 1575 (2005) (documenting how “[c]reditors prefer to focus on the narrow circumstances in which borrowers find themselves in a bind, take out a loan to avoid late fees, promptly repay the loan in two weeks, and come out ahead financially”); and Woolston, supra note 52 at 853, 862 (arguing that payday lending “fills the void created by the withdrawal of mainstream lenders from the small loan market”).

See e.g., Testimony of Kirk Williams, payday loan borrower, on H.F. 3533, Before Comm. on Commerce and Labor, Labor and Consumer Protection Div., 85th Leg. (February 29, 2008) (audio available at: http://www.house.leg.state.mn.us/audio/ls85/labor022908.asx) (testifying that he only took out payday loans in emergencies arising because of the “feast and famine” cyclical nature of his profession as a salesman); Testimony of Randy Fowler, payday loan borrower, on H.F. 3533, Before Comm. on Commerce and Labor, Labor and Consumer Protection Div., 85th Leg. (February 29, 2008) (audio available at: http://www.leg.state.mn/audio/ls85/labor022908.asx) (testifying that he took out a payday loan during a financial setback until he was “back on his feet”); and Testimony of Janice Blumlow, payday loan borrower, on H.F. 3533, Before Comm. on Commerce and Labor, Labor and Consumer Protection Div., 85th Leg. (February 29, 2008) (audio available at: http://house.leg.state.mn.us/audio/ls85/labor022909) (testifying that she took out one payday loan to “balance her budget,” repaid it and did not take another one).

Huckstep, supra note 35, at 207.

Johnson, supra note 54, at 1, (describing payday lending practices such as rollovers that “trap consumers…in a permanent cycle of debt”).


Faller, supra note 44, at 131 (asserting that “[t]he majority of borrowers have jobs (or at least sources of regular income), and all have a checking account,” (citing DAVID ROTHSTEIN & JEFFREY D. DILLMAN, POLICY MATTERS AND HOUSING RESEARCH & ADVOCACY CENTER, TRAPPED IN DEBT: THE GROWTH OF PAYDAY LENDING IN OHIO 1 (2007).

Community Financial Services Association of America, About the Payday Advance Service, at http://www.cfsa.net/about_payday_advance_product.html.
Faller, supra note 44, at 131. Faller argues that that “[t]he payday loan, by design, leaves borrowers in a worse predicament than the one that drove them to seek it in the first place.” Id. at 125. See also Drysdale & Keest, supra note 10, at 609 (explaining that the structure of payday loans extends and increases the initial burden that led the customer to the loan in the first place) and Stephanie Ben-Ishai, Regulating Payday Lenders in Canada: Drawing on American Lessons, 23 B.F.L.R. 323, 327 (2008) (commenting that “the very nature of the payday loan…means that rolling over loans is often inevitable for payday borrowers”).


Stephen Koff, Check ’n Go Former Workers Blast Lender, THE PLAIN DEALER, September 13, 2007.


Koff, supra note 77.

Id.

Martin, supra note 54, at 575.

Graves & Peterson, supra note 2, at 643. See also Johnson, supra note 54, at 73-74 (citing ACE Cash Express’ practice of awarding redeemable “bonus points” for each dollar borrowed).

Kenneth, supra note 56, at 692.

Martin, supra note 54, at 577.

Alan M. White, Behavior and Contract, 27 LAW & INEQ. 135, 159 (2009) (asserting that payday loans “are described (falsely) as a short-term credit product”). See also Bruch, supra note 44, at 1273-74 (describing the features of payday loans that prevent borrowers from extricating themselves from continuous borrowing); and Houren, supra note 48, at 569 (arguing that “[r]egardless of whether one is a critic or supporter of payday loans, the two-week loan repayment schedule is inconsistent with the advertised purpose of the loan--to help individuals with emergency expenses”).

Kenneth, supra note 56, at 665. See also Hellwig, supra note 67, at 1575 (stating that the fact pattern “in which borrowers find themselves in a bind, take out a loan to avoid late fees, promptly repay the loan in two weeks, and come out ahead financially…is rare in practice”; and Ben-Ishai, supra note 73, at 326 (finding that there “is strong evidence that these loans are not being used for emergencies but rather for long-term needs”).

Ben-Ishai, supra note 74, at 326.

King & Parrish, supra note 75, at 27 (finding that only between 1.1% and 2.1% take out a single payday loan per year).

Id. at 3. See also Bruch, supra note 44, at 1280 (citing his study’s finding that “77% are getting trapped” in the repeat borrowing problem).

See e.g., Drysdale & Keest, supra note 10, at 608 (reporting that the Indiana Department of Financial Institutions found that 77% of Indiana payday borrowers take out multiple loans each year); INDIANA DEPARTMENT OF FINANCIAL INSTITUTIONS, SUMMARY OF PAYDAY LENDER EXAMINATIONS, 7/1/99 THRU 9/30/99 26 (1999) (reporting an average of 13 loans per customer per year); LESLIE COOK, ET. AL., PUBLIC INTEREST
ISABEL NICHOLSON, CENTER FOR POLICY ENTREPRENEURSHIP AND THE BELL POLICY CENTER, THE TRUTH ABOUT PAYDAY LOANS: HOW HARDWORKING COLORADANS TAKE THE BAIT AND GET CAUGHT IN A CYCLE OF DEBT 8-9 (2008) (finding that 70% of all payday loans were made to borrowers with 11 loans and two-thirds were rollovers); ADMINISTRATOR OF THE COLORADO UNIFORM CONSUMER CREDIT CODE, PAYDAY LENDING DEMOGRAPHIC AND STATISTICAL INFORMATION: JULY 2000 THROUGH DECEMBER 2007 (2008) (reporting that borrowers with 12 or more payday loans accounted for 67% of the annual loans; that nearly half of the loan volume is attributable to borrowers with 16 or more loans annually); Stegman & Faris, supra note 75, at 20 (finding Illinois borrowers took an average of 12 payday loans per year).

91 Graves & Peterson, supra note 2, at 642. See also Paul Chessin, Borrowing from Peter to Pay Paul: A Statistical Analysis of Colorado’s Deferred Deposit Loan Act, 83 DENV. U. L. REV. 387, 409 (2005) (noting “the most striking aspect of [his] study is the confirmation that Colorado payday loan consumers also often find themselves trapped in a cycle of debt”).

92 Ellihausen, supra note 45, at 44-45 (reporting that nearly 80% of borrowers took at least five loans per year; 65% took at least five; 56% took at least nine; 29% took more than 14 loans per year).

93 Nathalie Martin & Koo Im Tong, Double Down-and-Out: The Connection Between Payday Loans and Bankruptcy, 39 SW. L. REV. 785, 787 (2010) (arguing that “the mathematics of the situation” make it “difficult to imagine” that “payday loans do not create a cycle of debt”). See also Schaaf, supra note 48, at 346 (noting that “high payments required for payday loans result in a very high renewal rate with little or no principal reduction”); and Megan S. Knize, Payday Lending in Louisiana, Mississippi, and Arkansas: Toward Effective Protections for Borrowers, 69 LA. L. REV. 317 (2009) (reporting that “studies show that it is mathematically impossible for typical borrowers to repay payday loans in two weeks”).

94 Chessin, supra note 91, at 419 (acknowledging that his study “does not account for whether an individual consumer obtained, or had outstanding, loans from more than one licensed location”). See also Stegman & Faris, supra note 75, at 20 (noting that studies “understate the real magnitude of the problem because they do not account for a family’s use of more than one payday lender at a time (Peter from Paul syndrome)” and Kenneth, supra note 56, at 667 (reporting that “[o]ften customers take out loans with multiple lenders to pay off the debt from another payday lender”).

95 See e.g., Chessin, supra note 91, at 409 (noting that the “repeat” customer that accounts for the overwhelming majority of the payday lender’s loan volume and revenue, i.e., its ‘bread and butter.’”); Oren Bar-Gill & Elizabeth Warren, Making Credit Safer, 157, 44, U. PA. L. REV. 1 (2008) (finding that “payday lenders target [repeat] customers, amassing 90% of their profits from borrowers who roll over their loans five or more times during a year”) (citing KEITH ERNST, JOHN FARRIS & URIAH KING, CENTER FOR RESPONSIBLE LENDING, QUANTIFYING THE ECONOMIC COST OF PREDATORY PAYDAY LENDING 2 (2004)); Peterson, Usury Law, Payday Loans, and Statutory Sleight of Hand: Salience Distortion in American Credit Pricing Limits supra note 54 at 1126-27 (concluding that “evidence suggests that payday lending profits come disproportionately from repeat borrowers”); and LESLIE PARRISH & URIAH KING, CENTER FOR RESPONSIBLE LENDING, PHANTOM DEMAND 3 (2009) (finding that loan churning “accounts for three-fourths of all payday loan volume”).

96 See e.g., Community Financial Services Association of America, Myths vs. Reality, at http://www.cfsa.net/myth_vs_reality.html#1 (claiming “millions of satisfied consumers have enjoyed the convenience and economic benefits of payday advance services without complaint”); CYPRESS RESEARCH GROUP, PAYDAY ADVANCE CUSTOMER SATISFACTION SURVEY 4 (2004) (reporting “high overall levels of satisfaction [77%] with [survey participants’] recent payday cash advance experience); Ellihausen, supra note 45, at 9 (finding that “[b]y far most payday advance customers were satisfied with their most recent new advance,” with 42% of customers
“very satisfied” and 33% “somewhat satisfied”); and Schaaf, supra note 48, at 349 (noting that payday lending industry maintains “that the customer has a very high degree of satisfaction”).

97 Johnson, supra note 54, at 79-80 (stating that most payday borrowers have “no alternative means of getting a short-term loan”).

98 See e.g., Lundberg, supra note 1, at 199. See also Chin, supra note 48, at 739 (relating that “[i]ndustry advocates…cite the low number of complaints”).

99 Lundberg, supra note 1, at 199.

100 Chin, supra note 48, at 739-740.

101 Id. at 740 (citing Julia Nienaber, The Cost of Cash; Potential Legislation of Payday Loans, or Advances on Pay Provided by Financial Service Companies, ST. GOV’T NEWS, Jan. 1, 2001, at 141).

102 Id.


104 See e.g., Aimee A. Minnich, Rational Regulation of Payday Lending, 16 KAN. J.L. & PUB. POL’Y 84, 84 (2006) (arguing that payday borrowers “are considered too high a credit risk for mainstream financial institutions” and consequently payday “loans are riskier”).


106 Id.

107 Id.

108 Kenneth, supra note 56, at 688.

109 Mann & Hawkins, supra note 50, at 885.


111 According to the Federal Reserve, credit default rates averaged: 4.84% for 2005; 4% for 2006; 3.99% for 2007; 5.52% for 2008; and 9.16 for the first three quarters of 2009. FEDERAL RESERVE BOARD, CHARGE-OFF RATE ON CREDIT CARD LOANS; ALL COMMERCIAL BANKS (November 16, 2009). See also Matt Phillips, Credit Card Update: Bank of America Leads in Default Rate Rise, WALL STREET JOURNAL June 16, 2009 (reporting that “[c]redit card default rates continued to rise in May, reaching 10.1%” and forecasting “a peak of 11.25% in mid-2010”); and Stephen Bernard, Moody’s Reports Increase of Nearly 50 Percent, and Expects Trend to Continue, SYRACUSE ONLINE, October 18, 2008 (reporting that the August 2007 and August 2008 credit card charge off rates were 4.61% and 6.82%, respectively).


113 The Federal Reserve Board, supra note 111. Data is from 2005 through the first three quarters of 2009.

Payday Lending” and warning against depository institution involvement with payday lenders because, in part, of their “limited underwriting of the borrower’s ability to repay”).

115 See e.g., Graves & Peterson, supra note 2, at 641 (asserting that “payday lenders engage in minimal underwriting”); Peterson, Usury Law, Payday Loans, and Statutory Sleight of Hand: Salience Distortion in American Credit Pricing Limits, supra note 54, at 1126 (averring that “payday lenders do not use underwriting guidelines to determine borrowers' ability to repay”); Lundberg, supra note 1, at 190 (stating that “payday loans, title loans require no underwriting”); Chessin, supra note 91, at 420 (conveying the results of a state regulator’s analysis that payday lenders did not perform underwriting with the diligence exhibited by other more responsible lenders); and Potter, supra note 50, at 636 (suggesting that “[p]ayday lenders have adopted underwriting principles that are practical and in their own self interest (allow the lender a handsome profit”).

116 See Brook, supra note 41, at 1005 (likening payday lenders to loan sharks to the extent that, for both, running credit checks is inefficient); and Baker and Breitenstein, supra note 3, at 594-95 (noting that neither payday lenders nor loan have strict credit standards).


118 Compare Mann & Hawkins, supra note 50, at 903 (claiming that APR disclosures, though providing “a good comparison mechanism for loans generally,” are “ineffective” for payday loans) and Michael A. Satz, How the Payday Predator Hides Among Us: The Predatory Nature of the Payday Loan Industry and Its Use of Consumer Arbitration to Further Discriminatory Lending Practices, 20 TEMP. POL. & CIV. RTS. L. REV. 123, 129 (2010) (expressing concern about the “unduly high cost of credit to the payday customer,” with APR’s for loans ranging from 390% “to an astounding 910%”).

119 See, e.g., Thomas, supra note 56, at 2423 (arguing that “[c]alculating fees as an APR does not make sense for payday loans”).

120 Minnich, supra note 104, at 91.

121 King & Parrish, supra note 76, at 3.

122 Steven M. Graves & Christopher L. Peterson, Predatory Lending and the Military: The Law and Geography of "Payday" Loans in Military Towns, 66 OHIO ST. L.J. 653, 662 (2005) (arguing that expressing the cost of payday credit as an APR is appropriate “because these loans often compound for durations coming close to or exceeding a year”).

123 Hawkins, Regulating on the Fringe, supra note 110, at 1386.

124 Id. at 1361.


127 Id.

128 Id. at 1364.

130 Id. at 5419.

131 CENTER FOR RESPONSIBLE LENDING, PAYDAY LOANS: A STEPPING STONE TO DEBT, REDUCED CREDIT OPTIONS AND BANKRUPTCY (2009).

132 CENTER FOR RESPONSIBLE LENDING, CRL CRITIQUE OF “PAYDAY HOLIDAY: HOW HOUSEHOLDS FARE AFTER PAYDAY CREDIT BANS” BY DONALD P. MORGAN AND MICHAEL STRAIN (2008) (calling attention to the facts that: (1) “[t]he returned check data used to report increases for Georgia and North Carolina after payday lending was banned includes not only these two states, but also returned checks from Alabama, Louisiana, South Carolina, southern Mississippi, and Tennessee—states where payday lending is legal”), thus inappropriately using “the Federal Reserve’s regional check processing centers…as proxies for state credit markets” (emphasis in original); and (2) “the authors fail to account for several factors that greatly influence a person’s chances of filing for bankruptcy protection, including health insurance coverage, foreclosures, divorce rates, and demographic factors such as income”).

133 Dr. Skiba conducts research in the area of behavioral law and economics. See Paige Marta Skiba, Curriculum Vitae, Vanderbilt University; available at http://law.vanderbilt.edu/facultyresources/faculty/221cv.pdf. Dr. Tobacman specializes in, among other things, behavioral economics and consumer credit in the broad subject area of Business and Public Policy. See Jeremy Tobacman, Curriculum Vitae, Wharton School, University of Pennsylvania; available at http://bpp.wharton.upenn.edu/tobacman/cv.pdf.

134 PAIGE MARTA SKIBA AND JEREMY TOBACMAN, DO PAYDAY LOANS CAUSE BANKRUPTCY 1, 8 (2009).

135 Id. at 1.


140 See, e.g., Faller, supra note 44, at 139 (averring that “[t]he payday lending market is a failed market”).

141 Martin, supra note 54, at 614.

Mann & Hawkins, supra note 50, at 883 (acknowledging that market forces for payday loans have failed “to drive prices to a competitive level”). See also Faller, supra note 44, at 139 (noting that “competition has not driven down prices”); Chin, supra note 48, at 740 (finding that competition has not lowered prices of payday loans); and Chessin, supra note 91, at 408-09 (stating that “competition among payday lenders appears to have little to do with what lenders charge consumers”).

Mann & Hawkins, supra note 50, at 882.

See e.g., Chessin, supra note 91, at 409 (finding that “finance charge amounts appear to be highly inelastic”); Chin, supra note 48, at 741 (finding that, despite competition, payday loan “rates [have] clustered at the cap set by state legislatures”); Mann & Hawkins, supra, note 50, at 882 (asserting that “[r]esearch indicates that payday lenders almost uniformly charge the highest rate permissible in their jurisdiction”); and CALIFORNIA DEPARTMENT OF CORPORATIONS, REPORT TO THE GOVERNOR AND THE LEGISLATURE: CALIFORNIA DEFERRED DEPOSIT TRANSACTION LAW 15 (2007) (finding that “almost every [payday lender in the state] charges the maximum fee, with very little fee competition”).

See e.g., David W. Barnes, One Trademark Per Source, 18 TEX. INTELL. PROP. L.J. 1, 28 (2009).

Bar-Gill & Warren, supra note 95, at 44.

See e.g., PaydayLoanUnion.com; http://paydayloanunion.com/ (claiming that it takes “just a few minutes to fill out our short online payday loan application form”); Payday Online; http://www.paydayonline.com.au/index-v1.php (urging prospective borrowers to “[c]omplete our short application form [that] takes around 3 or 4 minutes”) (emphasis in original); and Payday America; http://paydaysamerica.com/ (inviting customers to “[f]ill out our easy, fast, and secure form”).

See e.g., Faller, supra note 44, at 131 (noting the ease and convenience of the transaction) and Kenneth, supra note 56, at 669 (claiming that people who use payday lenders do so “primarily because of the convenience and privacy that the product offers” and to avoid “the stigma of admitting to friends, family, or a financial institution that you cannot make ends meet”).

Martin, supra note 54, at 573-74.

Lundberg, supra note 1, at 182.

See e.g. Hellwig, supra note 67, at 1585 (pointing out that consumers are embarrassed because of their financial problems).

Chin, supra note 48, at 727.

Mann & Hawkins, supra note 50, at 881.

Id.

Martin, supra note 54, at 563.

Id. at 616.
Hellwig, supra note 67, at 1595. See also Ben-Ishari, supra note 74, at 353 (citing a 1992 study finding that “50 per cent of Americans (including those with a university degree) were unable to understand the terms under [the Truth in Lending Act], or even know where to look for these terms”) (citing Alan White & Cathy Mansfield, *Literacy and Contract* 13 STAN. L. & POL’Y REV. 233, 253 (2002)).

Mann & Hawkins, supra note 50, at 882 (postulating that “[t]he customer is less likely to be sure, however, of costs that might relate to an unsuccessful transaction, such as bank fees in an amount unknown to the customer standing at the payday lender’s retail counter” and “the costs she would incur if her failure to repay the payday loan ultimately results in financial distress”).

See e.g., Ben-Ishai, supra note 74, at 326, 353 (contending that “[m]any payday lenders hide basic information about their loans from consumers,” time disclosures to occur after the contract is signed, and exploit consumers with “English-language difficulties”); White, supra note 85, at 161 (arguing that “[t]he essence of the payday loan product is a deception”); Chin, supra note 48, at 741 (arguing that payday lenders, with “extensive knowledge about the credit market…take advantage of the unequal bargaining power of the parties resulting from asymmetrical access to information [because] the typical borrower…is unsophisticated about her credit options”); Christopher Peterson, *Truth, Understanding, and High Cost Consumer Credit: The Historical Context of TILA*, 55 FLA. L. REV. 807, 896 (2003) (asserting that research shows that “[p]ayday lenders systematically delay divulging accurate comparative price information such as the annual percentage rate of their loans”); and Knize, supra note 93, at 326 (quoting a former manager of a payday loan store admitting that “she and her coworkers… would not talk about [the APR] or explain what it meant”).

MARIANNE BERTRAND AND ADAIR MORSE, UNIVERSITY OF CHICAGO, INFORMATION DISCLOSURE, COGNITIVE BIASES AND PAYDAY BORROWING 12 - 14 (2010) (finding payday borrowers are not financially literate).

Renuart & Thompson, supra note 51, at 207 (describing prose literacy as “the ability to read and write,” document literacy as “the capacity to extract and use information from different places in documents and from different documents” and quantitative literacy as the facility to manipulate and understand information conveyed in numbers,” such as “calculating the interest on a loan”).

See Ben-Ishai, supra note 74, at 353.


Id.

Mann and Hawkins, supra note 50, at 882.

Id. at 883.


Graves & Peterson, supra note 2, at 646.

Chin, supra note 48, at 723.


Graves & Peterson, supra note 2, at 646.

See e.g., Hellwig, *supra* note 67, at 1589 (contrasting economic models of free markets which assume full knowledge of costs and benefits, which lead to maximization of self-interest with the “reality [that the] fringe credit market [including payday loans] contrast sharply with this assumption”).

Bertrand and Morse, *supra* note 161, at 4 (challenging the assumption that all payday borrowing reflects informed and rational behavior).


Mann & Hawkins, *supra* note 50, at 884.

Graves & Peterson, *supra* note 2, at 693-94.

See e.g., Minnich, *supra* note 104, at 107 (claiming “consumers can benefit” from payday loans).


Robert Mayer, *Payday Loans and Exploitation*, 17 PUBLIC AFFAIRS QUARTERLY 197, 212 (2003) (arguing that the payday lending industry is “unsavory” because it profits “from other people’s hard circumstances”).

See e.g., Adam J. Levitin, "Hydraulic Regulation: Regulating Credit Markets Upstream," 26 YALE J. ON REG. 143, 187 (2009) (stating that, prior to 2004, “many payday lenders began ‘renting’ national banks' charters to circumvent state usury laws”). See also American Bank & Trust of South Dakota v. Hager, No. 1:04CV964, 2006 WL 399289 M.D. N.C. Feb. 16, 2006 (granting motion to dismiss bank’s petition to compel arbitration to resolve the complaint involving a scheme between it and Cash into Cash to evade North Carolina’s ban on payday lending); Goleta Nat. Bank v. Lingerfelt, 211 F.Supp.2d 711 (E.D. N.C. 2002) (denying payday lender and bank’s motion to enjoin state officials from enforcing state lending and consumer protection laws against payday lender); Goleta National Bank v. O’Donnell, 239 F.Supp.2d 745 (S.D. Ohio 2002) (granting regulator’s motion to uphold its action to enjoin payday lending activity conducted by ACE Cash Express using Goleta National Bank’s authority); Peoples Nat. Bank v. Office of the Comptroller of the Currency of U.S., 227 F.Supp.2d 645 (E.D. Tex. 2002) (granting agency’s motion to dismiss complaint of payday lender’s bank that the agency violated federal law and the bank’s constitutional rights by issuing an unsatisfactory examination rating due to its practice of engaging in payday loan transactions in association with Advance America); West Virginia v. CashCall, Inc., 605 F.Supp.2d 781 (S.D. W.Va. 2009) (denying payday lender’s motion to dismiss action brought by the State alleging, inter alia, that non-bank entity which marketed consumer loans participated in alleged scheme with out-of-state bank designed to avoid state usury laws); Georgia Cash America, Inc. v. Strong, 649 S.E.2d 548 (Ga. Ct. App. 2007) (dismissing appeal by payday lender involving allegations it entered into a sham partnership with the bank in order to claim that it was only making loans on behalf of the bank and, thus, secure immunity from Georgia’s usury laws on federal preemption grounds); and People ex rel. Spitzer v. County Bank of Rehoboth Beach, Del., 45 A.D.3d 1136 (N.Y. App. Div. 2009).
2007) (holding that a genuine issue of material fact existed regarding allegations that a payday lender, using Rehobeth, made payday loans where the annual interest rate exceeded the maximum interest rate permitted).

191  Marquette Nat. Bank of Minneapolis v. First of Omaha Service Corp., 439 U.S. 299 (1978) (holding that the National Bank Act authorized a national bank based in one state to charge its out-of-state credit card customers an interest rate on unpaid balances allowed by its home state, even when that rate is greater than that permitted by the state in which the bank’s customer resides). In the payday lending version of the importation of foreign rates, local lenders “sought to piggyback on national banks’ ability to export their home states’ higher or nonexistent usury caps…structuring transactions so that a national bank or thrift would make the loan to the consumer followed by the payday lender’s automatically purchasing the loan from the bank.” Levitin, supra note 190, at 187. See also Houren, supra note 48, at 577 (explaining that “[p]ayday lenders partner with national banks chartered in states that do not cap interest rates on small loans; they then export rates to other states, regardless of whether those other states have usury laws or rate ceilings that apply to payday lending”).

192  Levitin, supra note 190, at 187 (reporting that, in 2001 and 2002, “a series of suits were filed in state courts by state government agencies and consumers challenging national banks’ ability to ‘rent’ their charters to payday lenders in order to circumvent state usury laws and small loan laws”).

193  King & Parrish, supra note 76, at 6 (describing how “[b]ank regulators shut down the payday lending ‘rent-a-bank’ model over the course of several years, with the final regulator, the FDIC, effectively putting an end to the practice in 2005) (citing FEDERAL DEPOSIT INSURANCE CORPORATION, PAYDAY LENDING PROGRAMS REVISED EXAMINATION GUIDANCE (March 1, 2005)). See also Angela Littwin, Testing the Substitution Hypothesis: Would Credit Card Regulations Force Low-Income Borrowers into Less Desirable Lending Alternatives? 2009 U. ILL. L. REV. 403, n 92 (2009) (averring that the OCC and FDIC actions eliminated “rent-a-charter” agreements).

194  See Ameriloan v. Superior Court, 169 Cal. App. 4th 81, 97 (Cal. Ct. App. 2008) (describing the state’s contention in a suit against a payday lender claiming immunity from state law based on tribal sovereignty as “part of a “‘rent-a-tribe’” scheme”)

195  See Cash Advance & Preferred Cash Loans v. State, 242 P.3d 1099, 1102 (Colo. 2010) (remanding the case to district court to determine whether relationship between the defendant lender and tribe met the factors enumerated which would grant the business tribal sovereign immunity).

196  See, e.g., Satz, supra note 118, at 123.

197  States in which general usury or general lending rate caps apply include: Arkansas; Connecticut; Georgia; Maine; Maryland; Massachusetts; New Jersey; New York; Pennsylvania; Vermont; and West Virginia. None of these states have authorized payday lending. Parish and King, supra note 95, at 30.


199  See Craig Harris, Vote May Be the End of Payday Lenders, ARIZONA REPUBLIC, Nov. 10, 2008 (reporting that voters “overwhelmingly rejected…a ballot initiative financed and written by the loan companies to allow them to continue charging high interest rates on small [payday] loans”).

200  Laura Johnston, Ohio Voters Keep the Cap on Short-term Loans, THE PLAIN DEALER, Nov. 5, 2008 (reporting that “Ohioans voted overwhelmingly to cap payday loan interest rates at 28 percent, upholding a state law challenged by the loan industry” and that 64% of the electorate “approved keeping the caps”) and Matt Volz, Montana Voters Approve Payday Loan, Real Estate Tax Initiatives, MISSOULIAN, Nov. 3, 2010 (reporting that “about 73 percent of voters approved the payday loan cap”).
States banning or restricting payday lending include: Arkansas; Arizona; Connecticut; District of Columbia; Georgia; Maine; Maryland; Massachusetts; Montana; New Hampshire; New Jersey; New York; North Carolina; Ohio; Oregon; Pennsylvania; Vermont; and West Virginia. Parish & King, supra note 95, at 30.

See Glenn v. State, 644 S.E.2d 826 (Ga. 2007) (denying challenge to constitutionality of state law criminalizing the making of payday loans).

Martin, supra note 54, at 563 (citing the ability of “crafty lenders [to] quickly adapt to new legislation by finding loopholes that undermine any consumer protection provided by the new regulatory laws”).


See Betsy Sundquist, Payday Lending Loophole Targeted in Minnesota, ST. PAUL LEGAL LEDGER CAPITOL REPORT, Mar. 5, 2010 (describing the use by certain payday lenders of an Industrial Loan and Thrift license to evade restrictions under Minnesota’s Consumer Small Loan Act, regulating payday lending); Bob Driehaus, Lenders Thwart Ohio Law Intended to Limit High Interest on Payday Loans, N.Y. TIMES, Apr. 15, 2009 (reporting that “more than 1,000 stores have obtained licenses to issue short-term loans under different laws that permit higher rates” than the 28% cap under Ohio law); and Seanna Adcox, SC Bill Would Close Loopholes in Payday Lending, BUSINESS WEEK, Feb. 16, 2010 (relating allegations of legislators and advocates that payday lenders are attempting to skirt a recently enacted law setting rate and term restrictions and requiring the use of a database by lending under a different license).

Woolston, supra note 52, at 875.

Id. at 878.


Electroweb Media, Inc. v. Mycashnow.com, Inc., No. 1:02-CV-133, 2007 WL 1485216 (E.D. Tenn. May 18, 2007) (denying payday lender’s motion to quash service of process to owner of business who admitted setting up an off-shore shell corporation to evade taxes and litigation).

See e.g., Quik Payday, Inc. v. Stork, 549 F.3d 1302 (10th Cir. 2008) (requiring Internet lender to obtain a Kansas lending license) and Cash America Net of Nevada, LLC v. Com., Dept. of Banking, 8 A.3d 282 (Pa. 2010) (denying motion for declaratory judgment that banking department’s requirement that Internet lender obtain lending license is unlawful).

See e.g., Ferrell v. Express Check Advance of SC LLC, 591 F.3d 698 (4th Cir. 2010) (affirming grant of consumer’s motion to remand to state court of complaint that payday lender violated the South Carolina Deferred Presentment Services Act by engaging in unfair, deceptive, and fraudulent practices; the South Carolina Consumer Protection Code by engaging in unconscionable conduct; and the South Carolina common-law duties of good faith and fair dealing); Hooper v. Advance America, Cash Advance Centers of Missouri, Inc., 589 F.3d 917 (8th Cir. 2009) (denying payday lender’s motion to compel arbitration in complaint alleging Advance America violated various provisions of Missouri’s Merchandising Practices Act and Missouri’s payday loan law, and generally engaged in unfair, deceptive, and illegal lending practices); Dennison v. Carolina Payday Loans, Inc., 549 F.3d 941 (4th Cir. 2008) (denying payday lender’s motion to overturn lower court’s remand to state court of complaint alleging company violated South Carolina law prohibiting unconscionable loans); Davis v. Cash For Payday, Inc., 193 F.R.D. 518 (N.D. Ill. 2000) (granting plaintiff’s motion for class status certification for alleged violations of,
inter alia, the Illinois Consumer Fraud and Deceptive Trade Practices Act, and for entering into unconscionable contracts); Sharp v. Chartwell Financial Services Ltd., No. 99 C 3828, 2000 WL 283095 (N.D. Ill. Mar. 6, 2000) (denying payday lender’s motion to dismiss borrower’s complaint alleging violations of, inter alia, the Illinois Consumer Fraud Act); Gilkey v. Central Clearing Co., 202 F.R.D. 515 (E.D. Mich. 2001) (granting class certification to plaintiffs alleging payday lender violated, inter alia, the Michigan Consumer Protection Act); Flowers v. EZPawn Oklahoma, Inc., 307 F.Supp.2d 1191 (N.D. Okla. 2004) (granting consumers’ motion for remand to state court regarding allegations that payday lender violated Oklahoma Consumer Credit and engaged in usury and fraud by charging excessive interest); Donnachie v. Frank S. Falzone & Assoc., PPLC, No. 1:10-CV-0429, 2010 WL 3191891 (M.D. Pa., Aug. 11, 2010) (denying payday lender’s motion to dismiss complaint for violation of Pennsylvania’s Fair Credit Extension Uniformity Act “engaging in false, misleading or deceptive representations” while attempting to collect on a debt and Unfair Trade Practices and Consumer Protection Law for provided information to debt collectors about an alleged loan consumer had already settled); Purdie v. Ace Cash Express, Inc., No. Civ.A. 301CV1754L, 2003 WL 22976611 (N.D. Tex. Dec. 11, 2003) @ *1 (granting plaintiffs’ motion for class certification, final approval of settlement and award of attorney’s fees in action alleging lender violated, inter alia, state statutes regulating small loans, the Texas Deceptive Trade Practices Act and other state consumer protection laws); Alternative Financial Solutions, LLC v. Colburn, 821 So.2d 981 (Ala. 2001) (alleging violation of the Alabama Small Loan Act); F & G Financial Services, Inc. v. Barnes, 82 S.W.3d 162 (Ark. 2002) (denying payday lender’s interlocutory appeal challenging class certification in class action against lender for usury in payday loans); Cash America Net of Nevada, LLC v. Commonwealth, Dept. of Banking, 8 A.3d 282 (Pa. 2010) (affirming banking agency’s ruling that lender was engaged in payday lending without a license at usurious rates); and Felts v. CLK Management, Inc., 254 P.3d 124 (N.M. Ct. App. 2011) (denying payday lender’s motion to compel arbitration regarding allegations that lender “engaged in online lending practices in direct violation” of New Mexico Unfair Practices Act and the New Mexico Small Loans Act). See also Dan Browning, Minnesota Sues ‘Payday Lenders,’ STAR TRIBUNE, Sept. 6, 2011 (reporting that the Minnesota Attorney General took an action against five Internet lenders for making loans without a license and otherwise in violation of Minnesota payday lending law).

212 See e.g., Dienese v. McKenzie Check Advance of Wis., LLC, No. 99-C-50, 2000 WL 34511333 E.D. Wis. Dec. 11, 2000) (granting, in part, plaintiff’s motion for class certification in complaint that payday lender’s loans were unconscionable). Georgia Cash America, Inc. v. Strong, 649 S.E.2d 548 (Ga. Ct. App. 2007) (dismissing appeal by lender in case involving allegations of conversion of funds through a predatory lending scheme, and theft by deception, fraud, and conspiracy); and Johnson v. Cash Store, 68 P.3d 1099 (Wash. Ct. App. 2003) (denying payday lender’s motion to vacate default judgment in her action alleging that payday loan agreements were unconscionable).


214 Minnich, supra note 104 at 90 (citing a 2001 survey of payday lending in Franklin County, Ohio suggesting that payday lenders repeatedly violate Truth in Lending Act and Ohio state laws).

215 See e.g., Midwest Check Cashing, Inc. v. Richey, 728 N.W.2d 396 (Iowa 2007) (affirming small claims court judgment against debtor for payday loan on which she defaulted).


See, e.g., Smith v. Steinkamp, 318 F.3d 775 (7th Cir. 2003) (denying payday lender’s motion to compel arbitration regarding allegations that the lender violated the Fair Debt Collections Practices Act); Conner v. Howe, 344 F.Supp.2d 1164 (S. D. Ind. 2004) (holding that attorney retained by payday lender violated the Fair Debt Collections Practices Act by attempting to collect more in interest than is allowed under law); Ward v. Lombardo, Davis & Goldman, LLC, No. 11–CV–114A, WL 2600642 (W.D.N.Y., June 29, 2011) @ *1 (finding collection agency hired by payday lender violated federal Fair Debt Collection Practices Act, including harassment; false and misleading representations; abusive language; failure to send validation information; and threats to take actions that cannot legally be taken or that are not intended to be taken); Bullock v. Abbott and Ross Credit Services, L.L.C., No. A-09-CV-413 LY, 2009 WL 4598330 (W.D. Tex. Dec. 3, 2009) (awarding damages against collection agency hired payday lender for violations of, inter alia, the Fair Debt Collection Practices Act); Hazelwood v. Bruck Law Offices SC, 244 F.R.D. 523 (E.D. Wis. 2007) (certifying class in suit alleging violations of the Fair Debt Collections Practices Act by attorney hired by a payday lender); and Payday Today, Inc. v. Hamilton, 911 N.E.2d 26 (Ind. Ct. App. 2009) (affirming summary judgment against payday lender for violation of Indiana Uniform Consumer Credit Code-Small Loans and the federal Fair Debt Collection Practices Act).

See e.g., Mann & Hawkins, supra note 50, at 858 (arguing that “the elimination of payday lending would protect consumers who would then be drawn to other, even riskier sources of cash”). See also Peterson, Truth, Understanding, and High-Cost Consumer Credit, supra note 160, at (explaining that “[c]lassical economists consistently argued that legislating interest rates only forces the high-risk loan market underground”).

See e.g., Douglas W. Buchanan, Update: State and Federal Servicemembers Civil Relief Legislation and Cases, 61 CONSUMER FIN. L.Q. REP. 348, 349 (relating payday lending industry counterarguments to industry critics that “payday lender fees are lower than the bounced check fees, over limit fees, late charges and the like that their customers would be forced to pay if payday loans were unavailable”) and Thomas A. Wilson, The Availability of Statutory Damages Under TILA to Remedy the Sharp Practices of Payday Lenders, 7 N.C. BANKING INST. 339, 342 (2003) (explaining that “payday lenders argue that alternatives such as bounced check fees are usually more expensive than a payday loan”).

See e.g., Morgan & Strain, supra note 126, at 26 (concluding from their study that Georgia and North Carolina “are not better off since [they] outlawed payday credit”).

Id. at Abstract. But see CENTER FOR RESPONSIBLE LENDING, CRL CRITIQUE OF “PAYDAY HOLIDAY: HOW HOUSEHOLDS FARE AFTER PAYDAY CREDIT BANS” BY DONALD P. MORGAN AND MICHAEL STRAIN, supra note 132 (assailing the methodology used by Morgan and Strain and attacking their conclusions).

CENTER FOR RESPONSIBLE LENDING, FACT V. FICTION: THE TRUTH ABOUT PAYDAY LENDING INDUSTRY CLAIMS (2001) (displaying a chart comparing a $255 payday loan in North Carolina (pre-ban) to a late fee and bounced check fee on a $255 credit card bill and a $255 check, respectively, and finding the APR on the payday loan is 391% while the comparative APR’s are 202% and 141%, respectively).

Id.

CENTER FOR RESPONSIBLE LENDING, PAYDAY LOANS PUT FAMILY IN THE RED: RESEARCH REFUTES INDUSTRY CLAIMS THAT PAYDAY LOANS PREVENT OVERDRAFT FEES (2009) (citing, among other evidence, “[r]egulator data from Florida and Oklahoma” showing that about 25% of payday borrowers experience a “‘return event’” in any given 12-month period).

White, supra note 85, at 161-62.


Melzer, supra note 129, at Abstract.
Graves & Peterson, supra note 2, at 646 (citing RICK JURGENS, NATIONAL CONSUMER LAW CENTER, UTILITIES AND PAYDAY LENDERS; CONVENIENT PAYMENTS, KILLER LOANS 26-28 (2007)).


Lundberg, supra note 1, at 182.

Id. at 201.


Minnich, supra note 104, at 101.


Hellwig, supra note 67, at 1576.


Id. at 4.

Id.

Id. (finding that more former borrowers reported that ban was helpful than harmful).

Id. at 14-15.

Id. at 4.

Id. at 19-20.

See Richard Piersol, Credit Unions Launch Alternative to Payday Loans, THE LINCOLN JOURNAL STAR, Oct. 19, 2011 (describing Nebraska credit union loans of up to $500 at 18% APR, payable within 60 days); LAUREN K. SAUNDERS, LEAH PLUNKETT, AND CAROLYN CARTER, NATIONAL CONSUMER LAW CENTER, STOPPING THE PAYDAY LOAN TRAP 19-21 (2010) (describing alternative payday loan products offered by
credit unions in Connecticut, Florida, Iowa, Maryland, New York, New Jersey, North Carolina, Virginia, and Washington, and a Community Development Financial Institution lender offering small dollar loans in California and Texas).

248 Faller, supra note 44, at 125 (asserting that “[p]ayday loans are a wealth-depleting product”).