

SHOW ME THE MONEY!

A Survey of Payday Lenders and Review of Payday Lender Lobbying In State Legislature

U.S. Public Interest Research Group
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The Consumer Federation of America is a non-profit association of 260 groups, with a combined membership of 50 million people. CFA was founded in 1968 to advance consumers' interests through advocacy and education.

U.S. PIRG serves as the national lobbying office for state Public Interest Research Groups. PIRGs are non-profit, non-partisan consumer, environmental and good government research and advocacy organizations with members around the country.

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SECTION 1: EXECUTIVE SUMMARY AND RECOMMENDATIONS FOR REFORM

EXECUTIVE SUMMARY

Throughout the 1990s, the state PIRGs and the Consumer Federation of America (CFA) have documented the effects of financial deregulation on American consumers. One consequence of deregulation of interest rates, high credit card interest rates and high bank fees has been the rapid growth of the so-called predatory lending (or fringe banking) industry, which includes check cashing outlets, payday loan companies, rent-to-own stores, high cost second mortgage companies, sub-prime auto lenders, traditional pawn shops and the growing business of auto title pawn companies. This report examines payday lending in detail.

The report [Section 3] updates a 1998 CFA survey¹ on the consumer costs of payday lending and includes a survey of 230 payday lenders found in 20 states². It finds that payday lenders continue to make short term consumer loans of \$100-400 at legal interest rates of 390-871% in states where payday lending is allowed. More disturbingly, the report finds that payday lenders are exploiting new partnerships with national banks to make payday loans in states, such as Virginia, where the loans are otherwise prohibited by usury ceilings or other regulations.

Second, the report [Section 4] examines the status of payday loan laws and proposed legislation around the country.³

Finally, the report takes a detailed look [Section 5] at payday lender lobbying and influence peddling in three state legislatures. Disturbingly, the report finds that the payday lenders are following the same lobbying strategy that the rent-to-own industry successfully used in the 1980s and early 1990s to enact its preferred version of legislation in nearly every state.⁴ Payday lenders are hiring high-priced hired guns to seek enactment of weak, pro-industry legislation. So far, the strategy is working. Already, the payday lenders have been granted a safe harbor from usury laws in 23 states and the District of Columbia and flourish in states with no usury laws to prevent rate gouging.

If the payday lenders win, consumers, especially low-income consumers, lose. The predatory lenders' goal is to enact state legislation exempting their high-cost, high-risk loans from laws that apply to small loans. Although the report documents how the payday lenders have so far been successful in nearly half the states, increased scrutiny may slow their rapid growth.

¹ See the 8 state survey "The Growth of Legal Loan Sharking: A Report on the Payday Loan Industry," Jean Ann Fox, Director of Consumer Protection, Consumer Federation of America, November 1998, <<http://www.stateandlocal.org/loanshar.html>>

² In the summer and fall of 1999, PIRG and CFA surveyed 25 states and the District of Columbia. We document payday lending in 20 states and didn't find payday lending in the other six. No inference should be drawn about payday loans in the other 24 states, which were not surveyed due to lack of volunteers.

³ See "Safe Harbor for Usury: Recent Developments in Payday Lending," Jean Ann Fox, Director of Consumer Protection, Consumer Federation of America, September 1999 <<http://www.consumerfed.org/safeharbor.pdf>>

⁴ At least 46 states have enacted strongly pro-industry rent-to-own laws. Vermont's law is more balanced. New Jersey's legislature remains the primary rent-to-own battleground. In January, 2000, the state legislature again declined to consider a pro-industry bill despite intense lobbying. Personal communication, Jerry Flanagan, legislative director, NJPIRG, 18 Jan 2000.

RECOMMENDATIONS: The state PIRGs and CFA urge the following reforms:

- States should retain and enforce small loan rate caps and usury laws to protect consumers from exorbitant small loan rates charged by payday lenders.
- States with no small loan or usury cap should enact a cap on small loans and keep licensed lenders under state credit laws. States that have already legalized payday lending should, at a minimum, lower permissible rates and strengthen consumer protections based on the CFA/National Consumer Law Center (NCLC) model act.⁵
- Congress should stop the national bank regulators, notably the Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS), from allowing nationally-chartered banks and thrifts to provide protection for payday lenders from state consumer protection laws, especially since no federal law regulates their activities. Even better, Congress should close the bank loophole, either by enacting a federal usury law that applies to banks or by prohibiting FDIC-insured financial institutions from making loans based on personal checks held for deposit. To set minimum standards for state laws and to rein in the banks, Congress should enact the “Payday Borrower Protection Act of 1999” (HR 1684) sponsored by Rep Bobby Rush (D-IL).⁶
- More states should enact tough campaign finance reforms and lobbying disclosure laws. States should put the data on the Internet to enable citizens to evaluate influence peddling by special interests.

SECTION 2: INTRODUCTION

The state PIRGs and CFA have fought for years to ensure that banks and other lenders treat their customers fairly. Banks continue to raise the fees they charge consumers for bank accounts—gouging some consumers, who pay over \$200 per year in checking account fees according to the state PIRG’s 1999 Big Banks, Bigger Fees report. As CFA reports have indicated, high cost credit card interest and aggressive marketing of credit cards continue to saddle millions of consumers with expensive credit card debt.

Unfortunately, the failure of the banking industry to serve all consumers fairly has created a void in the marketplace that the predatory lending industry is rapidly filling. According to the most recent government data, 13.2% of families do not even maintain a checking account and 83% of those families have incomes less than \$25,000.⁷ Many families without bank accounts go to check cashing stores where they pay high fees to cash checks and buy money orders to conduct basic financial transactions.

Consumers seeking small loans find that banks no longer make small loans—if you don’t qualify for a credit card, you are forced to go elsewhere. Although traditional small loan companies still make loans for less than \$1,000, the industry has shifted its attention to larger loans. Payday lenders seek to fill the demand for small loans by making short-term small loans

⁵ For a copy of the CFA/NCLC Model State Deferred Deposit Loan Act, contact CFA, 1424 16th St. NW, Suite 602, Washington, DC 20036.

⁶ United States House Resolution 1684, introduced May 5, 1999, and based on model legislation written by the National Consumer Law Center and the Consumer Federation of America. Also see Marcaurelle, Myra, “Payday Lending Practices Spark Federal Legislation,” 4 Pub. Int. L. Rep., No. 3, Nov 99, pages 7-9, Loyola University Chicago Law School.

⁷ Kennickell, A. et al, “Results From The 1998 Survey of Consumer Finances,” Federal Reserve Bulletin, January 2000, Page 1.

based on personal checks held for later deposit.

Some consumers in the fringe financial market may have errors on their credit reports that cause their denial of traditional credit. Many others have experienced bad credit or no credit, due to either financial hardship or job dislocation. While many people will presume that these predatory lenders (or fringe banks) are "ma-and-pa" stores such as local pawn shops, increasingly they are part of national chains, or may be partnered with banks, or may even be "sub-prime" affiliates of a bank.

The predatory lenders include rent-to-own stores, "traditional" pawn shops, auto title pawn lenders, payday lenders, and sub-prime mortgage and auto loan companies. In our view, and in the view of Congress, all consumers who borrow money or purchase goods over time are entitled to the same rights, no matter what lender they go to. These rights include the right to compare the cost of borrowing over time on the basis of an annual percentage rate (APR) and the right to take advantage of state interest rate or usury ceilings, if applicable, and other state prohibitions on unfair lending practices. Although the two trade groups representing payday lenders told a December forum convened by Senator Joseph Lieberman that payday loans are subject to federal Truth in Lending, model state legislation backed by payday loan trade groups removes these transactions from state credit laws. And, as the surveys illustrate, some payday loan stores continue to claim that these are not "loan" transactions and fail to accurately quote the true Annual Percentage Rate when asked.

Salary lending at the turn of the last century led to a wave of reform to battle "loan sharking" that included state small loan laws and usury caps. In response to the last round of sleazy and deceptive loan practices in the 1960s, Congress passed the Truth In Lending Act and states enacted state Retail Installment Sales Acts, which often included usury ceilings and other rules on small loan practices. Although usury ceilings have been whittled away by deregulation at the federal level, many states have maintained anti-usury and other unfair practices laws designed to prevent interest rate gouging.

How Payday Lending Works

Pay day lenders make small advances based on personal checks held for future deposit, at interest rates approximating 300% APR or higher. For example, you write a check for \$115, and receive \$100, and the lender agrees not to cash your check until your next payday. The actual cost of that loan for two weeks is \$15, which works out to an APR of 390%. If you can't afford to pay it back, in many states you can simply pay the finance charge, or \$15, to "roll it over", still owing \$115 at the end of the month, ratcheting your total finance charges up to \$30 for a \$100 one month loan. Section 3 reports on a survey of payday lenders in 19 states and the District of Columbia.

Payday Lending Legislative Strategy Part 1: Safe Harbor From Usury

The payday lending industry is following the same strategy as the rent to own industry did in the 1980s—it is aggressively asking state legislatures to pass pro-industry legislation that treats their product as a check cashing transaction or service, not as loans. The industry seeks to obtain a safe harbor from coverage by the usury laws that apply to other small loans.

When the industry fails to win safe harbor from usury laws, it often resorts to subterfuge. For example, in response to aggressive enforcement in Texas, some payday lenders have attempted to "sell" consumers certificates in "catalogs." Others claim to "buy" home appliances from consumers, then lease them back for a "rental fee." The courts and enforcement agencies treat these transactions as loans subject to state laws and the federal Truth In Lending Act's

required loan disclosures.⁸ See Section 4 for an updated legislative status of payday lending in legislatures around the country.

Payday Lending Legislative Strategy Part 2: Hide Behind National Bank Charters

When the payday lenders fail to enact their preferred legislation, or seek to quickly move into a new state that may prohibit their activities, they are using a new approach. The payday lenders are forming partnerships with nationally-chartered banks. The firms argue that national banks may export deregulated interest rates from the bank's home state and are exempt from state interest rate regulation in the state where the consumer receives the loan. See Section 4.

SECTION 3: RESULTS OF A SURVEY OF PAYDAY LENDERS

In the summer and fall of 1999, PIRG and CFA staff and volunteers surveyed payday lenders in 25 states and the District of Columbia.

Nationally, the legal status of payday lending can be broken down into three general categories (See Appendix 1 for detailed list of states):

Category 1: Payday lending is generally banned by a low usury ceiling (interest rate cap) applicable to small loans. [19 states nationally, although as a result of court injunctions (AL) or regulatory interpretations (MI), payday lending is allowed for some entities in at least two ban states. Most recently, Indiana's Attorney General issued an opinion that payday lending is subject to Indiana's state interest rate limits and criminal loansharking laws.⁹]

Category 2: Payday lending is not prohibited because there is no usury ceiling on small loans. [8 states.] In these states, such as Oregon or Illinois, loans are made by licensed lenders, subject to state credit laws and supervision by regulators. The deregulation of interest rates permits payday lenders in these states to charge interest rates that far exceed the typical small loan rate cap.

Category 3: Payday lending is authorized by a specific law that grants safe harbor from usury or interest laws and typically sets maximum fees, size and length of the loan, and other terms. [23 states and the District of Columbia.]

⁸ See Consumers Union, "Wolf In Sheep's Clothing: Payday Loans Disguise Illegal Lending," Austin, Texas, February 1999. < <http://www.consumer.org/finance/txloans/txloans-1.htm> > On 17 December 1999, the payday lender Cash Today settled a lawsuit brought by Texas Attorney General John Cornyn and agreed to pay \$1 million in restitution to Texas consumers and end their loan business known as "deferred deposit" or "payday lending." See press release of Attorney General John Cornyn, 17 December 1999, < <http://www.oag.state.tx.us/> > (Texas v Cash Today, Tex. Dist. Ct., No. 99-02673, 12/17/99).

⁹ Modisett, Jeffrey A., Attorney General, Official Opinion No. 2000-1 Applicability of Statutory Usury Ceilings upon Small-Dollar, Short-Term Loans, January 19, 2000.

RESULTS OF THE SURVEY [INCLUDED AS APPENDIX 2]

Overall, surveyors contacted 230 payday lenders doing business in 19 states and the District of Columbia. Surveyors were not able to locate payday lenders in an additional six states and did not conduct surveys in the other 25 states.

PAYDAY LOANS ARE BEING MADE IN STATES DESPITE USURY CEILINGS

-- Surveyors made calls into 10 of the 19 Category 1 states where payday lending is effectively banned by a usury ceiling on small loans.

-- In 5 of the 10 Category 1 states surveyed (AZ, GA, MD, PA, and VA) payday loans are being made, despite small loan interest rate caps. In some cases, lack of enforcement resources may be the problem. In other cases, out-of-state banks export deregulated loan rates into these states. For example, in Virginia, all payday lenders were doing business through a partnership with a national bank. See below for additional discussion of national bank issues and see Section 4 for additional analysis.

-- Interest rates charged for a \$100, 14-day loan in states with usury caps ranged from 416% to 858% in Maryland, 429% to 650% in Arizona, 780% to 988% in Georgia, 390% to 455% in Pennsylvania, and 455% in Virginia.

-- In the other 5 Category 1 states surveyed, no payday loans were found despite 5-10 phone call attempts (MA, NJ, NY, RI, and VT). Surveyors also made calls into NH during 1999, finding no payday loans. Effective 1 Jan 2000, New Hampshire repealed its usury ceiling, so payday loans may be made there now. New Hampshire is included as one of the 8 Category 2 states, above.

PAYDAY LENDERS USING NATIONAL BANK CHARTERS TO AVOID STATE REGULATION

-- Increasingly, payday lenders in several states also seek to subvert the effect of state usury ceilings by making loans through partnerships with national banks, which assert that state laws do not apply to them. The following results should be considered preliminary, as most stores refused to even answer the question, or claimed they did not know.

-- At least 17 payday lenders reported making loans through national banks, thrifts or state industrial loan companies known to use their bank charters to avoid either usury ceilings (category 1 states) or other payday lending restrictions (category 2 or 3 states).

-- At least ten payday lenders in Arizona, the District of Columbia, Ohio, Pennsylvania, and Virginia reported partnering with Eagle National Bank of Pennsylvania. These include payday lenders in at least 3 states where payday lending is banned by usury or other statutes, including AZ, PA, and VA. [See Section 4]

-- The payday lender "Fast Funding" in both Florida and New Mexico reported doing business through County Bank of Delaware.

-- Two payday lenders in Pennsylvania reported doing business through Crusader Savings Bank, a nationally-chartered thrift in Pennsylvania.

-- Finally, some of the Checkstop payday lenders, which were surveyed in Arizona, Colorado and New Mexico, reported partnering with Web Bank, a Utah-chartered industrial loan company.

STORES DID NOT QUOTE APR ON PAYDAY LOANS

The federal Truth in Lending Act applies to payday loans, according to all the court decisions that have ruled on this question and confirmed by the Federal Reserve Board's published proposed amendment to the Reg Z Official Staff Commentary. Yet, many payday lenders surveyed claim that they are not in the business of making loans and therefore that none of the fees paid for their services are interest. So, it is difficult for surveyors, or potential customers, to obtain information to compare the cost of a payday loan.

-- Nationally, only 85 of 230 (37%) payday lenders quoted even a nominally accurate Annual Percentage Rate (APR) when asked over the telephone. Others claimed they "didn't know," or that the APR was equal to the fee for a two-week loan. [Credit was given if the APR quoted was at least 100%, although actual APRs calculated by PIRG ranged substantially higher.]¹⁰

PAYDAY LENDERS APPEAR TO EXCEED FEE LIMITS

-- In 7 of the 11 states surveyed where payday lending fees are capped by law, 23 out of 151 payday lenders (15%) appeared to charge fees higher than the maximum allowed by the law in that state.

-- In CA, DC, FL, LA, MO, MT, and OH at least one lender quoted fees above allowable maximums. In CO, MN, NC, and TN all lenders' quotes were at or below allowable APRs [allowing 0.1% rounding error].

BOUNCED CHECK (NSF) FEES

Payday lenders routinely compare the cost of their loans to the perceived higher costs of bouncing a check.

-- Yet, over 70% of the payday lenders (161/230) in this survey replied with a specific bounced check fee averaging over \$22 which they impose if a payday loan check is returned for insufficient funds. The quoted bounced check fees ranged from \$7.50 to \$40. The most common charges were \$25 (34% of respondents) and \$20 (34%). Only 6% of respondents said that they wouldn't impose bounced check fees. (Tennessee's law does not permit payday lenders to impose any additional fees for bounced checks.) A payday loan customer's bank would impose an additional bounced check charge.

¹⁰ Quotes provided over the phone are not formal Truth In Lending disclosures. Actual loan paperwork would be required to verify the accuracy of APRs disclosed to customers. Surveyors did not get loans.

MOST COMMON APRs

-- Nationally, the average APR found was 474%. Because different states have different laws setting different fee caps that result in varying APRs, it is not generally appropriate to rank the states. The following data are provided for illustrative purposes.

-- PIRG-calculated APRs for a two week, \$100 loan in the survey ranged from a minimum of 195% to 1092%. Both the high and the low were found in Montana, whose fee cap of 25% of the face value of the check allows a fee of \$33.50 per \$100 check which results in APRs of 871% for a loan repayable in two weeks. Before adopting its payday loan cap in 1999, Montana had no usury limits at all on loans.

-- The most common APR calculated, based on quoted fees, was 390%, charged by 30% of payday lenders, followed by 650%, charged by 13% of lenders.

-- A total of 56% of lenders charged 400% APR or more. Of all lenders, 35% charged more than 500% APR.

-- Fees charged by the same lender varied from state to state. For example, Advance America outlets quoted fees ranging from \$14 to \$25 to borrow \$100. Ace Cash Express outlets quoted from \$12.50 to \$30 for a \$100 loan.

-- In states with no usury cap, interest rates for a \$100 14-day loan ranged from 260% to 572% in Illinois, from 416% to 650% in New Mexico, 273% to 520% in Oregon, and 390% to 780% in Wisconsin.

COST OF LOAN CONFUSED BY FEES BASED ON TOTAL CHECK OR TOTAL LOAN

-- Although most payday lenders quote their fees on the basis of a check for \$100, some lenders include the cost of the loan in the \$100 check. This practice, authorized by some state laws, makes it harder for consumers to determine the true cost of a loan and easier for lenders to charge a higher finance charge than consumers expect. For example, when a consumer calls to find out the cost of borrowing \$100, many lenders will respond "\$15" when their actual fee to borrow \$100 would be \$17.65. It works this way-- you write a check for \$100, and the lender actually gives you only \$85. So, the fee to borrow \$85 is \$15 (or 17.65% of \$85. To borrow \$100, you would need to write a check for \$117.65.) Some of the payday loan costs reported in this survey may actually be understated due to this factor.

SECTION 4: THE PAYDAY LENDING INDUSTRY
Structure, Review of state legislative activities in 1999,
and the role of National Banks

STRUCTURE AND SIZE OF THE INDUSTRY:

Over 10,000 payday loan outlets are operating and one trade group representative projects over \$2 billion in payday loan revenue by next year. The Tennessee Department of Financial Institutions reported to its legislature that licensed payday lenders earned over 30% return on investment in the first nine months of legal operation. Stephens Inc., a Little Rock company, forecasts a potential mature market for 25,000 stores generating \$6.75 billion in fees annually in 2002. Stephens also forecasts that annual volume of business will total 180 million transactions with \$45 billion dollar volume of loans to produce that \$6.75 billion in fee volume.¹¹

Payday loans are offered through a wide variety of outlets, ranging from national chains of stand-alone payday loan companies, to established check cashing locations, to convenience stores, gas stations, pawn shops, and via Internet or 800-number faxed offers¹². Payday loans through ATM terminals are expected. Consolidation in the industry is underway, such as Advance America's buy-out of National Cash Advance.

PAYDAY LOANS RESULT IN HIGH COSTS, PERPETUAL DEBT, AND COERCIVE COLLECTIONS

The most obvious problem caused by payday loans is the high cost for borrowers. The \$15 to \$33.50 fee per \$100 permitted in some states, coupled with the extremely short-term of the loans, results in triple-digit interest rates for small loans and escalating finance charges if loans are not repaid in full on the borrower's next payday. The payday loan industry compares its fees to the cost of deliberately bouncing checks. CFA instead compares payday loan costs to other sources of quick cash loans available to consumers with less than perfect credit ratings. For the Senate forum on payday lending in 1999, CFA's actuary calculated the cost to borrow \$200 and repay it in one month and in three months. **SEE CHART ON NEXT PAGE.**

These loans are designed to keep consumers in perpetual debt. Payday loans are single-payment loans for relatively small amounts (typically \$50 up to \$500) and for very short periods of time (a few days up to two weeks or the borrower's next payday). A borrower has to repay the loan and finance charge in full on the next payday or roll-over the loan by paying the fee and extending the loan until the next payday. In 1999 Indiana's Department of Financial Institutions inspected 47 licensed lenders, reviewing a total of 5,350 customers' files and a total of 54,508 loans. Indiana found an average of 10.19 payday loans per year per customer, with the ten largest lenders averaging 12.05 loans per person per year.¹³ Indiana found that 77% of payday loans are roll-overs of existing loans. The Illinois Department of Financial Institutions also conducted a study of licensees and found that the average customer had 13 loan contracts

¹¹ Stephens Inc., "The Developing 'Payday Advance' Business: The Next Innings: From Emergence to Development, September 28, 1999, page 9.

¹² We found numerous payday loan ads on the Internet. At least one payday lender, Checkstop, is making payday loans on the Internet through an FDIC-insured institution, Web Bank. See <<http://www.checkloan.com/>>.

¹³ Indiana Department of Financial Institutions, Summary of Payday Lender Examinations Conducted from 7/99 thru 10/99.

present in files. The Illinois DFI report to the Illinois Senate concluded that customers are “captive” when unable to end the cycle of rolling over their accounts due to the excessive cost.¹⁴

Escalating triple-digit debt causes financial disaster for some families. The Nashville *Tennessean* reported: “Bankruptcy officials said ‘payday’ lending companies increasingly are showing up as creditors in bankruptcy cases here and around the country in states where legislatures have legalized triple-digit interest rates. Of some 12,400 chapter 13 bankruptcy cases pending in Middle Tennessee, 413 show debts to ‘payday loan’ businesses, records show.”¹⁵

Payday Loan Cost Comparison				
To Borrow \$200 and Repay in One Month:				
Type of Credit	Terms	Finance Charge	APR	Total Payment
Credit Card	19.99% APR	\$8.41	50.46%	\$208.41
Cash Advance	No grace period 2.5% Fee \$2.50 Minimum			
Small Loan	36% APR Cap	\$6.00	36.00%	\$206.00
Payday Loan	\$17.50/\$100 15-day term w/ 1 rollover	\$70.00	457.00%	\$270.00
To Borrow \$200 and Repay in Three Months:				
Type of Credit	Terms	Finance Charge	APR	Total Payment
Credit Card	19.99% APR	\$11.86	35.25%	\$211.86
Cash Advance	No grace period 2.5% Fee \$2.50 Minimum			
Small Loan	36% APR Cap	\$12.10	36.00%	\$212.10
Payday Loan	\$17.50/\$100 15-day term w/ 5 rollovers	\$210.00	457.00%	\$410.00

Chart calculated by CFA actuary.

¹⁴ “Short Term Lending Final Report.” Illinois Department of Financial Institutions, 1999, p. 31.

¹⁵ Sheila Wissner, “Payday loans’ cited in bankruptcies,” *The Tennessean*, April 18, 1999 p.1.

Lenders can and do use coercive collection practices because a personal check is the basis for payday loans. These tactics range from deliberately depositing a check although funds are not available which triggers both the bank's and the lender's bounced check charges, to bringing civil charges for bad check-writing to get triple damages, to threatening or bringing criminal hot-check prosecutions.

Any default on a payday loan, by definition, involves a worthless check. Some state credit laws provide for triple damages when a bad check is used in a retail transaction. Payday lenders in Ohio, for example, sue under the "Civil Damages for Crime Victims" statute O.R.C. §2307.61 which provides triple damages to victims of theft offenses, including bad checks. Inspection of court records in Dayton Municipal Courts Division over eight months in 1999 found 381 actions by five payday lenders. Defaulting customers were charged triple damages, 10% interest on the damages, and court costs. The total dollar amount for the judgments from all 381 cases was \$285,406. In 60% of the cases, wages were garnished.¹⁶

A Tennessee federal judge ruled in 1999 that a check cashing outlet violated the Tennessee consumer protection law by deceptively threatening to prosecute a delinquent customer. The *Turner* court found that the transaction did not involve the passing of a "bad" check since the lender knew the consumer did not have sufficient funds in the checking account when the loan was made to cover the cash advanced.¹⁷ Texas Consumer Credit Commissioner Leslie Pettijohn testified at Senator Lieberman's forum that more than 13,000 criminal complaints were filed in one year in a single precinct in Dallas County by payday lenders.

The Iowa Attorney General provided an informal advisory opinion to guide regulators on this issue.¹⁸ The Colorado Attorney General's "Report of the Uniform Consumer Credit Code Revision Committee" issued in October noted: "In addition, criminal fraud by check provisions do not apply to bounced deferred deposit loan checks since the lender knew at the time the borrower entered into the transaction that the borrower did not have the funds in his or her checking account to pay the loan. The required intent to defraud is lacking."¹⁹ An Ohio court found "egregious conduct" on the part of a collector of a payday loan that violated the Fair Debt Collection Practices Act. The collector identified himself as a police officer and threatened criminal prosecution.²⁰ The Cook County State's Attorney in Chicago and the Illinois Department of Financial Institutions settled a Consumer Fraud Act case against Nationwide Budget Finance Inc. which was accused of mailing out letters threatening criminal hot check prosecution to consumers behind on their loans.²¹

Consumers trying to make ends meet by getting a quick cash advance on a personal check pay usurious interest rates, often become mired in perpetual debt, and are exposed to coercive collection practices.

STATE LEGISLATIVE ACTIVITY IN 1999 AND PROSPECTS FOR 2000

In September, CFA released a detailed report on payday lending activities in state legislatures in 1999.²² As the report notes, "the majority of state legislatures grappled with

¹⁶ Letter, Legal Aid Society of Dayton, Inc., December 21, 1999, describing law student research.

¹⁷ *Turner v. E-Z Check Cashing of Cookeville, TN, Inc.* 35 F. Supp.2d 1042 (M.D. Tenn. 1999).

¹⁸ Iowa Department of Justice, Informal Advisory #87 (Feb. 18, 1999), Clearinghouse No. 52,156.

¹⁹ Laura E. Udis, Administration of the Uniform Consumer Credit Code, "Report of the Uniform Consumer Credit Code Revision Committee, October 8, 1999, p. 22.

²⁰ *Boyce v. Attorney's Dispatch Service*, 1999 U.S. Dist. LEXIS 12970 (S.D. Ohio April 27, 1999)

²¹ *Illinois v. Nationwide Budget Finance, Inc.*, Final Judgment and Consent Decree, Circuit Court of Cook County, Illinois, December 17, 1999.

²² See "Safe Harbor for Usury: Recent Developments in Payday Lending," Jean Ann Fox, Director of Consumer Protection, Consumer Federation of America, September 1999 <<http://www.consumerfed.org/safeharpr.pdf>>

legislation impacting the fast-growing payday loan industry in 1999 and legislation to establish minimum standards for state laws was introduced in Congress.”

The state by state battle over the legality and limits on payday lending continues as legislatures convene in 2000. As of mid-January, payday loan legislation is filed or expected in a dozen states. Financial regulators in two states, **New Mexico** and **Illinois**, completed required studies of high cost credit and filed reports.

The **Illinois** report on Short Term Lending found a heavy concentration of high cost lenders in heavily populated urban centers. The average APR for payday loans in Illinois was 533% and the average customer earned \$25,131 annually, and had 13 loan contracts on file per lender. The report concluded: “the high expense of a short term loan depletes the customer’s ability to catch-up, therefore making the customer “captive” to the lender.” At least two bills have been filed in Illinois. SB 1275 authorizes short-term loans with no limit on fees or interest. Payday loans may be for up to \$500 with two roll-overs permitted if the original outstanding balance has been reduced by 25%. HB 2900 would set a 24% APR rate cap on short-term loans in a state that presently has no usury limits. Representative Poe’s bill also requires that advertising must include the annual percentage rate for loans. A third bill is expected from Rep. Thomas Dart.

The **New Mexico** study report concluded that better consumer education was sufficient to address unrestricted payday loan and car title loan rates. A minority statement, filed by AARP and New Mexico Public Interest Research Group, called for a usury cap and tougher consumer protections. No inspection of current payday lenders was conducted for the report.

Legislative battles take up where they left off last year in several states. **California’s** Senator Perata has amended his bill to tighten the terms of California’s law permitting payday loans. Key features include a payment plan spread over five paydays, better reporting to state regulators, and application of the fee to the loan amount, not the total check. The California payday loan industry is shopping for an author for their model bill.

Colorado is revamping its Uniform Consumer Credit Code. Senator Dave Owen filed SB 144 to set a 20% fee cap for payday loans with three roll-overs. Under this bill, for a two-week loan, Colorado would permit 520% APR. Currently, under Colorado’s UCCC Rule 7 that allows two payday loans outstanding at one time, lenders split a request for a \$200 loan into two \$100 loans and charge \$25 on each for a total finance charge of \$50. Under SB 144 filed in Colorado, the effective fee will be higher than current rules permit once the loan principal exceeds \$250. This change to a percentage fee cap in Colorado will also provide an incentive to make larger loans, adding to repayment problems for borrowers.

The payday loan industry is trying again in **Indiana** to get a “deferred presentment” bill enacted. SB 287 allows an 18% fee on loans of up to \$500 and three roll-overs of loans. Indiana’s Attorney General issued an opinion January 19 that raises the stakes for industry legislation. Mr. Modisett opined that payday lenders cannot avoid Indiana’s loansharking statute by referring to their charge as a “service fee” rather than interest. Indiana’s small loan cap of 36% also applies. A lender violates the loansharking law by charging more than double the regulated rate. Since Indiana payday lenders charge more than 72% APR, the legal status of the industry is under threat under both laws.

Competing bills are filed in **Florida**. The industry’s HB 553 would set fees at 15% of the loan, with a \$500 maximum loan and a two-roll-over limit. Opponents of payday lending support HB 661 which clarifies that cash advanced on a personal check held for deposit is a small loan transaction, capped in Florida at 30% APR. Florida’s money transmitter regulations

that open the door for one-time payday loans by licensed check cashers would be overruled by this bill.

Wisconsin held a hearing in November on Senator Robson's SB 96 to impose a 36% APR cap on payday loans. Amendments to SB 96 set a 5% cap on loan fees and on subsequent roll-overs and set a minimum loan period of 30 days. Industry supported Assembly Bill 612 merely requires disclosures such as telling customers that a payday loan should only be used in an emergency, and comparing what it would cost to pay off a loan in full after one pay period with what it would cost after eight rollovers. Rep. Tim Hoven's bill contains no rate caps or other restrictions. (See Section Five for more information about Florida, Illinois, and Wisconsin.)

In **Kentucky**, Representative Jack Coleman is renewing his effort to reign in the payday loan industry. HB 73 as originally filed makes payday lending subject to the Kentucky small loan act. Observers expect the bill to be amended to at least apply the fee cap to the loan, not the total check.

Several states where small loan laws and usury caps prevent triple-digit payday lending will be battlegrounds to legalize this form of credit. Industry bills are expected in **Arizona, Alabama, and Virginia**. Carry over legislation in **Georgia** has been amended to authorize payday loans with a 15% cap on up to \$500 loans, with one renewal. Georgia HB 515 sets no minimum loan term and does not prevent serial loans (where the borrower pays off one loan and immediately writes a new check to start over.)

In **Maryland**, consumer advocates are seeking legislation to strengthen enforcement tools and funding for the Financial Commissioner. An opinion from the Maryland Attorney General's office held that payday lending is subject to Maryland's small loan law²³, but little enforcement of Maryland's 33% APR small loan cap has been attempted. Industry legislation to legalize payday loans is expected in Maryland.

Michigan's Attorney General filed a Notice of Intended Action against a national payday loan company in 1999. A public hearing on HB 4808 to legalize payday loans was held in October, but no further action has occurred. The Michigan industry bill would cap fees at 18% of the loan for up to \$500 with four roll-overs and serial loans are authorized.

PAYDAY LENDERS PARTNER WITH BANKS TO EVADE STATE LAWS²⁴

Partnerships between banks and companies in the fringe banking market are a growing trend in the payday loan field. As an investment advisor newsletter to the industry notes, "we see a trend afoot to utilize some sort of national bank charter lending program to permit the product in states that are unwilling to act on legislation to allow the product."²⁵ One such partnership between a national bank in Pennsylvania and the nation's second largest chain of check cashers is being challenged in a national RICO class action suit filed in federal court in Los Angeles. The *Phanco* case alleges that Eagle National Bank has "rented" its national bank charter to allow Dollar Financial Group's check cashing outlets to circumvent otherwise applicable state law restrictions.²⁶ Eagle is making payday loans in at least three states, Arizona, Texas and Virginia, where these loans are illegal for state-licensed lenders. The *Phanco* case also alleges that Eagle makes loans that do not comply with state payday loan laws, such as California's.

²³ Rowe, Kathryn M., Assistant Attorney General, Letter to The Honorable Thomas L. Bromwell, November 24, 1999.

²⁴ This section adapted and updated from "Safe Harbor for Usury."

²⁵ Stephens, Inc. "The Emerging Business of Deferred Presentment," April 1, 1999, p. 6.

²⁶ *Phanco v. Dollar Financial Group*. Case No. CV99-1281 DDP (C.D. Cal., filed Feb. 8, 1999).

The legal theory underlying the use of national banks to make payday loans is “exportation.” As currently interpreted, a 1978 Supreme Court decision is being used to argue that banks with certain kinds of privileged charters are able to ignore the usury laws in the borrower’s home state. By chartering the bank in a deregulated state, the bank claims the right to export its home state’s lack of regulation all across the country irrespective of whether their practices would be illegal for payday lenders in the borrower’s home state.

Texas’s Consumer Credit Commissioner testified in mid-December that “There is no judicial precedent that directly supports this concept of using the theory of exportation of interest rates to make payday loans.”²⁷ When banks market credit cards nationally, consumers deal directly with the bank in response to card offers. In payday lending, the consumer only contacts the local outlet, such as a pawn shop or check casher, to apply for and receive the loan.

In a letter²⁸ to the nation’s chief national bank regulator, Comptroller of the Currency John Hawke, CFA, U.S. PIRG, Consumers Union and other consumer organizations noted that Eagle’s activities appear to violate the intent of the Riegle-Neal Act. A central premise behind interstate banking as allowed by Riegle-Neal was that national banks would comply with state laws. The Conference Report²⁹ noted “utmost concern” for the ability of states to protect its citizens. The letter charged that Eagle’s use of its bank charter to export its activities without regard for state law ignores Riegle-Neal.³⁰

On 30 November 1999, the Comptroller replied that although “payday loans raise significant consumer protection concerns,” he believes that “In the final analysis, there may, practically speaking, be little that bank regulators can do to eliminate abusive payday lending practices that comply with existing law.” Hawke takes the view that national banks, and state banks, may “export their home state interest rates and other finance charges” and that his agency, the OCC, “simply does not have the authority to set maximum interest rates.” The Comptroller concludes that instead of OCC action on national bank participation in payday lending, the solution is “consumer education.”

The **Pennsylvania** Attorney General condoned the use of national bank charters to circumvent Pennsylvania’s Consumer Discount Company Act in settling a case involving McKenzie Cash Advance, the Cleveland, Tennessee-based company which operates two payday lending chains in that state. Instead of agreeing to cease making loans in violation of Pennsylvania’s small loan act as other payday lenders have done, National Cash Advance agreed to affiliate itself with a federally insured financial institution and to register as a Pennsylvania loan broker.³¹ National Cash Advance uses Crusader Savings Bank, a federally chartered thrift in Philadelphia, to make loans that would otherwise be illegal under Pennsylvania’s small loan act.³² Pennsylvania banks are exempt from small loan laws and there is no limit on fees that Pennsylvania banks may charge for loans.

²⁷ Pettijohn, Leslie, Texas Consumer Credit Commissioner, Testimony for Senate Forum on Payday Lending, December, 1999.

²⁸ For a copy of the 27 July 1999 letter, see < <http://www.stopatmfees.com/newpage61.htm>>

²⁹ Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, H.R. Conf. Rep. No. 651, 103rd Cong., 2d Sess., at 53 (1994)

³⁰ California Reinvestment Committee, Consumer Federation of America, Consumers Union, Greenlining Institute, National Community Reinvestment Coalition, National Consumer Law Center, U. S. Public Interest Research Group, Woodstock Institute, Letter Re: Eagle National Bank and “Payday Loans,” Addressed to The Honorable John D. Hawke, Jr., Comptroller of the Currency, July 27, 1999.

³¹ Press Release, Attorney General Mike Fisher, Pennsylvania, April 22, 1999.

³² www.nationalcashadvance.com

Comments filed with Treasury by Consumer Federation of America and the National Consumer Law Center in an Advance Notice of Proposed Rulemaking proceeding indicated that banks are partnering with check cashers, pawn shops, and other fringe bankers to provide “voluntary” EFT’99 accounts through which the federal government can electronically distribute federal benefits to recipients. An informal survey of accounts across the country noted that these entities were expecting to make payday loans to federal recipients, secured by anticipated deposit of social security checks and other benefits.³³

A start-up bank applied in 1999 for a Delaware bank charter to provide nationwide electronic banking, including payday loans. Axxess Bank plans to “only” charge 200% interest for advances secured by anticipated deposits of social security benefits as one of several account options for unbanked or underbanked consumers³⁴. The Delaware Community Reinvestment Action Council expressed concerns about Axxess Bank’s planned high-cost payday loans at a public hearing before the Delaware Bank Commissioner although the bank organizers offered some concessions in the design of the overdraft loans.³⁵

On 15 December 1999, US Senator Joseph Lieberman (D-CT) held a public forum on payday lending. In that event, Lieberman called the doctrine of interest rate exportation “wrong.”³⁶ Other bank/payday lender partnerships mentioned at the Lieberman forum include Utah-chartered industrial loan company Web Bank, Banco Popular which makes payday loans through Texas check cashing outlets, Goleta National Bank of California (partnership with Ace Cash Express), and County Bank of Delaware (Fast Cash Funding, Cash Reserve, and the now-defunct Delaware Bank Card).

Other Consumer Banking Preemption Battles: Lifeline Checking and ATM

Surcharge Bans: The doctrine of interest rate exportation is one area where national banks and the OCC are abusing stronger state consumer laws. National banks, supported by the OCC, have also used other preemption theories in their efforts to ignore state low-cost lifeline banking laws. Although in 1995 the OCC announced, as required by Riegle-Neal, that it was reconsidering its preemption of the 1992 New Jersey Checking Account law, it has failed to act further and its preemption determination remains in place. More recently, national banks and the OCC have mounted vigorous opposition to the enforcement of state and local ATM surcharge bans, despite the lack of federal regulation on either matter and clear language in the Electronic Funds Transfer Act allowing states to regulate ATM fees.³⁷ In our view, it is especially critical that the several states retain the authority to protect their consumers better, in circumstances such as these where the federal government has failed to protect them at all.

³³ Comments to the Treasury on ANPRM 31 C.F.R. Chapter II RIN 15055—AA74, National Consumer Law Center, Consumer Federation of America, et.al. April 1999.

³⁴ Epstein, Jonathan, “Banks for non-bank account working people,” Wilmington News-Journal, June 24, 1999.

³⁵ Epstein, Jonathan, “Axxess Bank gains support for plans,” Wilmington News-Journal, July 7, 1999.

³⁶ “However you feel about payday lending, this legal two-step around state law is wrong, and I’d like to examine ways to prevent it.” Statement of Sen. Joseph Lieberman, 15 Dec 99,

<<http://www.senate.gov/member/ct/lieberman/general/r121599b.html>>

³⁷ For detailed analysis of preemption issues pertaining to the OCC, see PIRG’s “OCC Watch” web page at <<http://www.stopatmfees.com/toppage3.htm>>

SECTION 5: INFLUENCE PEDDLING BY HIGH COST LENDERS
Legislative Activities of Payday Lenders In 1999
In Florida, Illinois, and Wisconsin

Finally, this section of “Show Me The Money” looks in greater detail at the legislative activities of payday lenders in 3 states that were active battlegrounds in the last year.

CASE STUDY—FLORIDA

Despite Florida’s Consumer Finance Act, which has a small loan interest rate cap of 30%, payday lenders, with their triple- and quadruple-digit interest rate figures, are operating there.³⁸ Here’s how it works: while state law caps the annual interest chargeable on loans of less than \$2000 at 30%, licensed check cashers are permitted to charge up to 10% of a check’s face value to cash a personal check, along with an additional \$5 fee for “verifying identity.”³⁹ Therefore, Florida payday lenders have chosen to dub their service check cashing, advancing money on post-dated checks at up to 419% APR, more than 13 times the legal interest limit for small loans.

Where the distinction between check cashing and payday lending occurs, Comptroller Bob Milligan feels, is when the loan is rolled over and a loan transaction is indicated.⁴⁰ When payday lenders in Florida allow rollovers, Milligan deems them to making loans without a license, not cashing checks. “He’s between a rock and a hard place, between what consumers need and what they can get,” says Sunny Phillips, in reference to the lack of quick cash options.⁴¹

Although payday loans are made in Florida through a Comptroller’s regulation for money transmitters, the industry wants a “deferred presentment” law to remove any legal uncertainty and to authorize higher rates and roll-overs. Payday lenders in Florida last year began to flex their moneyed muscles to win such a law. Along with the check cashing industry, they contributed at least \$50,000 to legislators in the 97/98 cycle,⁴² and hired a stable of well-connected lobbyists, including James Bosser, former fundraiser for Florida Gov. Jeb Bush turned lobbyist for payday lender Advance America. Check Into Cash, which didn’t even have any offices in Florida, hired lobbyists including S. Curtis Kiser, former state senator, James Daughton, former assistant chief of staff for Gov. Lawton Chiles, Sam Choate, a prominent lobbyist nationally on the rent-to-own industry, and Martha Barnett, president-elect of the American Bar Association.⁴³

With the help of these lobbyists, the payday loan industry did its best to get legitimacy in the 1999 legislative session. House Bill 2127 and its companion bill, Senate Bill 2294, would have specifically allowed payday lending in the state at interest rates of 15-20% per loan period, translating into annual interest rates of 391% and higher.

In efforts to pass these bills during the first four months of 1999, payday lender lobbyist Robert Levy of the Florida Check Cashers Association reported lobbying expenditures of \$9,500.

³⁸ Florida Consumer Finance Act, Florida Statutes Chapter 516.

³⁹ Money Transmitters’ Code, Florida Statutes Chapter 560

⁴⁰ Conversation with Sunny Phillips, Legislative Director for Florida State Comptroller Bob Milligan, August 6, 1999. Also, see Dyckman, Martin. “Loan Sharks, Then and Now,” *St. Petersburg Times*, April 25, 1999, page 3D.

⁴¹ Conversation with Sunny Phillips, Legislative Director for Florida State Comptroller Bob Milligan, August 6, 1999.

⁴² According to campaign contribution records available online from the Florida Division of Elections at: <http://election.dos.state.fl.us>. Also, see “Feeding Frenzy,” *The Orlando Sentinel*, April 1, 1999.

⁴³ According to lobbyist registration records available online from the Florida Legislative Information Services Division, Lobbyist Registration Office at: <http://www.leg.state.fl.us>

This amount, spent in the first four months of 1999 alone, is more than he reported spending in the entire years of either 1997 or 1998.⁴⁴ However, both bills died in committee.

In the House, once state Rep. Bob Starks persuaded the House Financial Services Committee to amend HB 2127 to limit the interest rate cap on payday loans to 10% of the check's face value⁴⁵, the industry lost interest in supporting the bill, saying that it then "did nothing" for them.⁴⁶ In the Senate, Sen. Walter Campbell postponed action on his bill, saying that it still needed too much work.⁴⁷ Sen. Campbell, who is known for being consumer-friendly, reportedly dropped the bill because he realized the extent of the damage it would do to consumers.⁴⁸

Fortunately for consumers, this was not a good session for the payday lenders to try to get legitimacy. The 1999 session was rife with controversy over another form of fringe lending—auto title pawn lending.⁴⁹ The *Orlando Sentinel*, hometown newspaper for both State Rep. Sublette, who is very active in working to regulate title lending, and Senate President Toni Jennings, ran editorials almost every single day on the fringe lending industry's habit of preying on the poor.⁵⁰ So, the payday lenders did not find a sympathetic ear for their argument that 391-591% interest annually was an appropriate small loan interest rate.

In 1999, the Florida legislature did not enact legislation sanctioning payday lending.

CASE STUDY-ILLINOIS

In Illinois, even Benny the Bull is getting in on payday lending.

The popular Chicago Bulls mascot has appeared in newspaper advertisements promoting the grand opening of eight new Chicago locations of the national payday lender chain Check Into Cash. When questioned about the arrangement, a spokesperson for the Bulls called Check Into Cash a "sponsor" of the team.⁵¹

In Illinois, payday lending by licensed lenders occurs in the absence of an annual interest rate cap on small loans. State law says that creditors lending under \$10,000 can charge any interest rate to which both parties agree, and while the state has criminal usury laws prohibiting the charging of excessive interest, licensed lenders in the state are exempted from these laws.⁵² Before 1997, there were few such lenders in the state; as of April 1999, there were more than 400, and the numbers continue to grow.⁵³

In 1998, the state Department of Financial Institutions established a task force to study the fast-growing payday loan industry. However, consumer-friendly participants were noticeably

⁴⁴ According to lobbyist expenditure records obtained from the Florida Legislative Information Services Division, Lobbyist Registration Office.

⁴⁵ The standard the payday lenders were already operating under using the state's check cashing laws.

⁴⁶ Gelbart, Marcia. "House Panel Tightens Payday Lending Bill," *The Palm Beach Post*, April 14, 1999, page 13A. Also, see Dyckman, Martin. "Loan Sharks, Then and Now," *St. Petersburg Times*, April 25, 1999, page 3D.

⁴⁷ Pfankuch, Thomas. "Lawmaker Kills Payday Loan Legislation," *The Florida Times-Union*, April 21, 1999, page B-3.

⁴⁸ Conversation with Mark Ferrulo, Florida Public Interest Research Group, July 27, 1999.

⁴⁹ For a detailed survey of auto title pawn lending, see the 1998 Florida PIRG title pawn survey.

<http://www.pirg.org/floridapirg/consumer/loan98.htm> PIRG is preparing a detailed report on title pawn lending nationally.

⁵⁰ Conversation with Mark Ferrulo, Florida Public Interest Research Group, July 27, 1999.

⁵¹ Coffey, Raymond. "Even Benny in on Payday Loan Act," *Chicago Sun-Times*, March 23, 1999, page 31.

⁵² Bakke, Dave. "Lawmakers Studying Payday Loans," *The State Journal-Register*, March 29, 1999, page 1.

⁵³ According to May 1999 list of all Consumer Installment Loan Act licensees, obtained from the Illinois Department of Financial Institutions by Dan Edelman.

absent—while there were 20 industry representatives present, no consumer advocates were allowed a voice in the proceeding.⁵⁴ When the law firm Edelman and Combs discovered the task force, it sought to be included as consumer representatives. Edelman and Combs refused the Department of Financial Institutions' participation conditions, and sued under Illinois' open meetings law. While the suit was initially rejected, when the attorneys appealed the ruling the Department disbanded the task force rather than include non-industry voices in the task force.⁵⁵

In late 1998, release of a survey of lender practices conducted in the state by the Illinois Public Interest Research Group and the Champaign-Urbana Predatory Lending Coalition, in conjunction with the release of a Consumer Federation of America report on the payday loan industry, created a storm of media coverage on the issue.⁵⁶ The Coalition picketed the grand opening of Campus Cash near the University of Illinois. Legislators began to respond. State legislators, such as Rep. Thomas Dart and Sen. Patrick O'Malley, chair of the Senate Financial Institutions committee, started to speak up about payday lending, and the industry was listening.

The payday loan and check cashing industry gave candidates around \$163,000 in just part of the 97/98 election cycle, almost double what they gave in the entire 95/96 cycle and wanted some results for their money.⁵⁷ When Rep. Thomas Dart introduced HB 2704 in early 1999 to cap annual interest on payday loans at the prime rate, the industry sprang into action.

In 1999, the payday lending and check cashing industries had 13 lobbyists registered in the state.⁵⁸ This stable included such well-connected persons as a former House Majority Leader Gerald Shea, a judge of the Illinois Court of Claims, Andrew Raucci, a former U.S. Attorney, Anton Valukas, and a former county State's Attorney, Dallas Ingemunson.

While Rep. Dart's bill was in the House Consumer Protection & Product Regulation committee, it became obvious to him that it was doomed. "The industry had bottled up the committee to the point where the bill wasn't going to get anywhere," Dart says. The industry had, with the help of their 13 lobbyists, "reached" the leadership of the House and Senate. Industry lobbyists paid a visit to Dart as well,⁵⁹ pleading that his bill would effectively shut down their industry. While Rep. Dart says he had no intention of retaining the amendment once HB 2704 reached the floor, he worked with the industry on an amendment that completely changed the character of his bill. This industry amendment allowed charges of up to 20% of the face amount of the loan, resulting in an annual percentage rate "cap" of 520%, and allowed three consecutive rollovers of the loan.⁶⁰

Consumer groups quickly met with Rep. Dart after they heard about industry amendments to HB 2704 to determine what had happened to the consumer-friendly version of the bill.⁶¹

After meeting with the consumer coalition, Rep. Dart withdrew HB 2704 and introduced House Resolution 164, creating a House commission to "conduct a study of the business of

⁵⁴ Conversation with Dan Edelman, Edelman & Combs, August 3, 1999. See also, Coffey, Raymond. "Payday Loan Places Proliferate," *Chicago Sun-Times*, March 5, 1999.

⁵⁵ Conversation with Dan Edelman, Edelman & Combs, August 3, 1999.

⁵⁶ "The Growth of Legal Loan Sharking: A Report on the Payday Loan Industry," Consumer Federation of America, November 1998.

⁵⁷ According to campaign contribution records available from the Illinois Campaign for Political Reform website at: <http://www.ilcampaign.org>.

⁵⁸ According to lobbyist registration records available from the Illinois Secretary of State Index Department at: <http://www.sos.state.il.us/depts/index/division.html>.

⁵⁹ Conversation with Illinois State Representative Thomas Dart, August 3, 1999.

⁶⁰ Amendment #1 to House Bill 2704.

⁶¹ Conversation with Gail Parsons, Illinois Public Interest Research Group, August 4, 1999.

making payday loans.” According to the Representative, he preferred the weight of a commission behind the idea of payday lending reform, as opposed to just his name as a sponsor. Dart also expressed concern about repercussions in the future if the industry form of the bill passed, making him the instigator of the Illinois government’s sanctioning of payday lending practices in the state.⁶² Starting in the summer of 1999, hearings have been held in different parts of the state as part of the House commission set up by House Resolution 164. Representative Dart is preparing the final report from the hearings and has filed a shell bill for this legislative session. Meanwhile a coalition has emerged in Chicago that is concern with the payday loan industry. Chaired by Monsignor John Egan, the coalition is composed of consumer groups, governmental agencies, religious organizations, university officials and consumer lawyers.

In the Senate, Sen. O’Malley, chair of the Senate Financial Institutions Committee, introduced a similar resolution, SR 42, which ordered the Department of Financial Institutions to study payday lending, and report back to the Senate. As reported in Section 4 above, The Illinois report on Short Term Lending found a high concentration of short term lenders in heavily populated urban centers. The average APR for payday loans in Illinois was 533% and the average customer had 13 loan contracts on file per lender. The report concluded: "the high expense of a short term loan depletes the customer’s ability to catch-up, therefore making the customer "captive" to the lender."

At least two bills have been filed in Illinois in 2000. SB 1275, introduced by Senator O’Malley, authorizes short-term loans with no limit on fees or interest. HB 2900, introduced by Representatives Poe and O’Connor, would set a 24% APR rate cap on short-term loans in a state with no usury limits.

Alderman Toni Preckwinkle of the 4th ward of Chicago, has moved forward with other actions to take on the industry, which she believes has a disproportionate negative impact on her district. On 29 September 1999, Preckwinkle and The Illinois Consumer Justice Council, Inc. filed suit against the Director of the Illinois Department of Financial Institutions to invalidate a secret Department of Financial Institutions rule that permits payday lenders to accept postdated checks. Preckwinkle also won passage of a city zoning ordinance that changed the zoning classification of payday lenders to a special use designation which allows the alderman to hold a hearing when a payday lender wants to open up in a ward.

The City of Chicago government has also weighed in on the payday loan issue with the city’s suit against the Payday Loan Store of Illinois, the first suit of its kind. The city alleged that the Payday Loan Store failed to comply with Illinois lending laws when the store failed to disclose the annual percentage rates for its loans.⁶³ The case, being pushed by Department of Consumer Services Commissioner Caroline Shoenberger, is in settlement negotiations.⁶⁴

Encouragingly, the state legislature did not enact industry-supported legislation in 1999. The results of the Short Term Loan report point to the need for consumer-oriented reform in 2000.

⁶² Conversation with Illinois State Representative Thomas Dart, August 3, 1999.

⁶³ Manor, Robert. "City Sues Payday Loan Firm," *Chicago Sun-Times*, February 19, 1999, page 52.

⁶⁴ Personal communication, Gail Parson, Consumer Advocate, Illinois PIRG, 18 Jan 2000.

CASE STUDY—WISCONSIN

“The payday lenders are literally moving in by the day here,” says Wisconsin PIRG director Kerry Schumann. “We’re watching it happen.”⁶⁵

There were 17 payday lenders in the state of Wisconsin in January 1996. A little over a year and a half later, in August 1997, the number had grown more than tenfold,⁶⁶ and as of July 1999, there were almost 200 payday lenders in the state.⁶⁷

All this growth is the result of the lack of a small loan interest rate cap in the state. Because the interest rates they can charge are not limited by law, payday lenders thrive at rates of 438% and higher.⁶⁸ State regulators limit Wisconsin pawnbrokers to an interest rate no greater than 36% annually,⁶⁹ According to Jean Plale of the state Department of Financial Institutions, in 1998 alone, payday lenders in Wisconsin made 630,300 loans totaling more than \$147 million, an astronomical leap from the 1996 figures of 80,000 loans totaling \$11.2 million.⁷⁰ In December 1998, two class action lawsuits were filed in Wisconsin against two of the country’s largest payday lenders--the national chains The Cash Store and National Cash Advance.⁷¹ As of June 1999, the number of plaintiffs in the suit against the Cash Store was up to about 10,000.⁷² Lawyers for the Center for Public Representation, who, along with the Legal Aid Society of Milwaukee and a Madison law firm, filed the suit, said that payday lenders in the state were taking advantage of the poorest and the most vulnerable consumers.⁷³

In failing to disclose in a conspicuous manner the 500% plus annual percentage rate on loans made to consumers, the suit said, the payday lenders violated state and federal law. The suit also alleged that because of the plaintiffs’ inability to do anything but agree to the lenders’ unreasonable terms, the contracts between the lenders and the plaintiffs were unconscionable.⁷⁴

In the case against National Check Advance, the Eastern District federal court upheld the state law unconscionability claims, paving the way for class certification. The Cash Store case was settled.

One week after the filing of the lawsuits, state Representatives Tim Hoven and Dean Kaufert publicly announced that they would be looking into ways consumers could be protected from the perils of payday loans. The representatives did not propose a small loan interest rate cap to protect borrowers from usurious rates, but simply called for “education” of consumers and perhaps a limit on the number of loans a consumer could take out at one time.⁷⁵

⁶⁵ Conversation with Kerry Schumann, Executive Director of Wisconsin PIRG, July 1999.

⁶⁶ “‘Payday Loan’ Companies Increasing in State,” *Wisconsin State Journal*, August 22, 1997, page 8B.

⁶⁷ Conversation with Lisa Lee, Wisconsin Department of Financial Institutions, July 9, 1999.

⁶⁸ According to survey conducted by Wisconsin PIRG for U.S. PIRG.

⁶⁹ Pommer, Matt. “Special Interests Skirt Finance Laws; Cash Poured Into State Races,” *Capital Times*, April 1, 1999, page 4A. Also, Romell, Rick. “Filling a Need,” *The Milwaukee Journal Sentinel*, February 6, 1996.

⁷⁰ 1998 figures obtained from message left by Jean Plale in response to request for information. Also, 1996 figures from: Segall, Cary. “More Control Sought Over Payday Loan Companies,” *Wisconsin State Journal*, December 26, 1998, page 1A.

⁷¹ Segall, Cary. “More Control Sought Over Payday Loan Companies,” *Wisconsin State Journal*, December 26, 1998, page 1A.

⁷² Segall, Cary. “Joint Suit filed vs. Loan Firm,” *Wisconsin State Journal*, June 3, 1999, page 1B.

⁷³ Segall, Cary. “Suit Accuses Wisconsin Loan Companies with Excessive Interest Rates,” *The Wisconsin State Journal*, December 23, 1998.

⁷⁴ Segall, Cary. “Lawsuits Seek to Stop Two Companies that Make 500 Percent Loans to Poor,” *The Wisconsin State Journal*, December 22, 1998, page 1A.

⁷⁵ Segall, Cary. “More Control Sought Over Payday Loan Companies,” *Wisconsin State Journal*, December 26, 1998, page 1A.

Not surprisingly, Hoven and Kaufert's pledge was not received enthusiastically by industry representatives like Pat Essie of the Wisconsin Deferred Deposit Association, the state's payday lender lobbying group. Citing the high cost of making short-term, unsecured loans, Essie touted the usefulness of such a "service," and said that the interest rates charged are reasonable.⁷⁶

Rep. Hoven received at least \$1900 from the payday loan industry in the 1997/98 cycle. Only \$500 of this money was from an in-state contributor; the rest was from out-of-state national chains like The Cash Store⁷⁷—the very same payday lender being sued in the class-action suit that supposedly inspired Hoven's ire. Asked about this seeming contradiction in Hoven's words and his actions in receiving money from the industry, research assistant Michael Welsh said, "It's a business, and he understands that."⁷⁸

Representative Hoven introduced Assembly Bill 612, legislation on payday lending, in the fall of 1999. Components of the bill include a four or five time rollover limit, as well as several "education" measures such as a pamphlet drafted by the state Department of Financial Institutions that would be handed out to payday borrowers. What the bill will not do is cap the exorbitant interest rates—upwards of 400%—that payday lenders are charging in the state.⁷⁹

On January 19, 2000 the Assembly Financial Institutions Committee held a hearing on AB 612. It quickly became apparent that AB 612 was an industry measure, shown by the number of industry lobbyists and spokespeople who turned out to support the bill. Consumer advocates testified in opposition to the bill, calling it a bill that "did nothing to address the real problem of the payday lending industry: exorbitant interest rates." Throughout the hearing, consumer advocates were verbally attacked repeatedly by members of the committee. Even a witness who came to tell her story about being in debt to lenders for two years was badgered by members of the committee.

A stronger effort to regulate the industry was presented in April 1999 in the form of Senate Bill 96, introduced by state Sen. Judy Robson. The bill originally placed a 26% interest rate cap on payday loans, a huge decrease from the rate of 520% currently charged by many lenders in the state.⁸⁰ Far from a death knell for the industry, Robson says, "I assume someone could do very well [at 26%]."⁸¹ Early on, SB 96 was amended to set a 36% cap in an attempt to compromise with the payday industry. However, the industry continued to oppose SB 96.

Currently, SB 96 is in the Financial Institutions committee, which held a public hearing in late 1999. After that hearing, Senator Jon Erpenbach, Committee Chair, revised the bill again in an attempt to make it less objectionable to the payday industry. Consumer advocates supported those changes, but considered the bill much weaker than the original 26% interest rate cap. In recent conversations with Senator Erpenbach's office, the Center for Public Representation was told that Erpenbach planned to compromise the bill again. At this point, according to WISPIRG's Kerry Schumann, "As advocates for the public we can't support legislation that does not cap interest rates at a reasonable rate. If SB 96 is compromised any further, it will no longer have the teeth to protect consumers." Both the President of the Senate and the state Attorney General are on record supporting the original version of SB 96. Groups

⁷⁶ Segall, Cary. "More Control Sought Over Payday Loan Companies," *Wisconsin State Journal*, December 26, 1998, page 1A

⁷⁷ Data from the Wisconsin Democracy Campaign, www.wisd.org.

⁷⁸ Conversation with Michael Welsh, Wisconsin state Representative Timothy Hoven's office, July 20, 1999.

⁷⁹ Conversation with Wisconsin state Representative Timothy Hoven, July 20, 1999.

⁸⁰ Pommer, Matt. "Special Interests Skirt Finance Laws; Cash Poured Into State Races," *Capital Times*, April 1, 1999, page 4A.

⁸¹ Squires, Susan. "Wisconsin Lawmaker Wants to Cap Interest on Payday Loans," *The Post-Crescent*, April 13, 1999.

like AARP, Wisconsin PIRG, the Center for Public Representation, and the Wisconsin Bar Association's Public Interest Section are supporting the bill; however, industry representatives have made it known that they are drafting their own legislation. Not surprisingly, the industry legislation is not expected to include an interest rate cap.⁸²

CONCLUSION AND RECOMMENDATIONS FOR CONSUMERS:

The growth of the payday lending industry over the last several years has resulted in increased public scrutiny of its practices. The findings of this report provide a blueprint for state governments and the Congress to fight back against usurious payday lenders and, ideally, roll back some of the gains they have made in legislatures around the country. It is also critical that Congress, even if it does not enact the Rush legislation to set minimum state standards for payday lending, force the OCC to revoke the perceived ability of banks to participate in payday lending in defiance of state law. Congress can close the national bank loophole by either enacting a federal usury law or by prohibiting FDIC-insured financial institutions from making payday loans.

In addition, we urge public policymakers to be forewarned that another high-cost, predatory lending industry is beginning to flex its muscles to enact similar legislative safe harbors for its practices. In many ways, the auto title pawn industry, which offers similar small loans secured not merely by a check but by the title to your car (and often a copy of the keys), offers a greater threat to low-income consumers than even the payday lenders.

PIRG and CFA recommend that cash-strapped consumers avoid the high costs and risks of using payday loans. Consumers with short-term cash needs should try to solve their immediate problems without borrowing money, such as asking for more time to pay a utility bill. If a loan is unavoidable, shop for the lowest cost credit available, comparing both the dollar finance charge and the Annual Percentage Rate. Cash advances on credit cards and traditional small loans are less expensive than a typical payday loan. Consumers with on-going financial problems can seek help with budgeting and debt management from local non-profit consumer credit counseling agencies or their credit union. Payday loan customers should only borrow what they can afford to repay on their next payday without having to borrow again before the next paycheck arrives.

⁸² Conversation with Kerry Schumann, Executive Director of Wisconsin PIRG, July 19, 1999.

APPENDIX 1: STATUS OF STATE PAYDAY LENDING LAWS (1 page)

APPENDIX 2: SURVEY OF PAYDAY LENDERS (10 pages)

METHODOLOGY

In the summer and fall of 1999, state PIRGs and CFA members surveyed 25 states by telephone, calling check cashers, small loan companies and payday lenders listed in local phone books. 230 payday lenders were identified in 19 states and DC. No payday lenders were found in the other 6 states surveyed (MA, NH, NJ, NY, RI and VT). No conclusions can be made about payday lending in the other 25 states, which were not surveyed due to lack of resources.

Surveyors asked questions that consumers shopping for deals would ask and sought rate quotes on payday loans. Many lenders were evasive and some hung up the phone. It was particularly difficult for surveyors to obtain information about whether the store allowed roll-overs and how roll-overs work. Lenders were also evasive about their partnerships with banks.

PARTICIPATING PIRGs and CFA STATE AND LOCAL ORGANIZATIONS

AZ-Arizona Consumers Council and US PIRG;
CA-California PIRG;
CO-Colorado PIRG;
DC-US PIRG;
FL-Florida PIRG;
GA- US PIRG;
IL-Illinois PIRG;
LA-US PIRG
MD-MARYPIRG and Womens' Law Center of Maryland;
MN-Minnesota PIRG;
MO-Missouri Credit Union System and Missouri PIRG;
MT-Montana PIRG;
NC-North Carolina PIRG and North Carolina Consumer Council;
NM-New Mexico PIRG;
OH-Ohio PIRG;
OR-Oregon State PIRG;
PA-Mercer County Community Action Agency and Pennsylvania PIRG;
TN: CFA and US PIRG;
VA-Virginia Citizens Consumer Council;
WI-Wisconsin PIRG.

[Also surveying, with no payday lending identified: Massachusetts PIRG (MA, NH, RI), New Jersey PIRG, New York PIRG and Vermont PIRG.

APPENDIX 1
Status of State/Territory Payday Loan Law⁸³

CATEGORY 1: States that prohibit payday loans due to small loan interest rate caps, usury law, and/or specific prohibitions for check cashers (19 states, PR, VI)

Alabama ⁸⁴	Alaska	Arizona	Connecticut
Georgia	Indiana ⁸⁵	Maine	Maryland ⁸⁶
Massachusetts	Michigan ⁸⁷	New Jersey	New York
North Dakota	Pennsylvania	Puerto Rico	Rhode Island
Texas	Vermont	Virginia	Virgin Islands
West Virginia			

CATEGORY 2: States that permit payday loans: no small loan rate cap or usury limit / min. finance charge (8 states)

Delaware	Idaho	Illinois	New Hampshire
New Mexico	Oregon	South Dakota	Wisconsin

CATEGORY 3: States with specific payday loan laws or regulations that permit payday loans (23 states and DC)

Arkansas	California	Colorado	Florida ⁸⁸
Hawaii	Iowa	Kansas	Kentucky
Louisiana	Minnesota	Mississippi	Missouri
Montana	Nebraska	Nevada	North Carolina
Ohio	Oklahoma ⁸⁹	South Carolina	Tennessee
Utah	Washington	Wyoming	District of Columbia

⁸³ Source: Consumer Federation of America, January 2000.

⁸⁴ Loans currently permitted under terms of court injunction in case pending between Alabama Banking Department and the Alabama Check Cashers Association. .

⁸⁵ Opinion issued by Attorney General Jeffrey A. Modisett, January 19, 2000 found that lenders violate Indiana law when they offer supervised loans at finance charges that exceed Indiana's 36% APR limit and violate loansharking statute if lender charges an interest rate greater than twice the authorized finance charge in the consumer credit code.

⁸⁶ Maryland Office of Attorney General issued an opinion November 24, 1999 to Senator Bromwell finding that payday lending is subject to Maryland small loan law that caps interest on loans under \$6,000 at 33% APR.

⁸⁷ Michigan Financial Institutions Bureau has stated that companies are not required to be licensed under the Regulatory Loan Act if they charge no more than 7% per annum interest plus the check casher's fee for cashing personal checks. Check cashing rates are not regulated in Michigan. The Michigan Attorney General filed a Notice of Intent to take action against a stand-alone payday lender in late 1999.

⁸⁸ Florida money transmitter regulations permit licensed money transmitters to cash post-dated checks at same fee as cashing personal checks. Roll-overs or extensions of loans violate Florida usury and/or consumer finance act.

⁸⁹ Oklahoma permits loans of under \$101.97 as single-pay one-month loans. Any loans for \$102 or more have a minimum term of 60 days.