

5-1-2007

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Repository Citation

Richard J. Thomas, *Rolling Over Borrowers: Preventing Excessive Refinancing and other Necessary Changes in the Payday Loan Industry*, 48 Wm. & Mary L. Rev. 2401 (2007), <https://scholarship.law.wm.edu/wmlr/vol48/iss6/7>

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ROLLING OVER BORROWERS: PREVENTING EXCESSIVE REFINANCING AND OTHER NECESSARY CHANGES IN THE PAYDAY LOAN INDUSTRY

INTRODUCTION

In 1993, W. Allan Jones began making small, short-term loans in exchange for a postdated check written for the combined value of the loan and a service fee.¹ This practice had not been seen for over half a century, when “salary lenders” provided short-term loans for small sums in exchange for a future paycheck.² In 1999, just six years after Mr. Jones resurrected the deferred payment industry, commonly known as the payday loan industry, payday lenders issued about \$8 billion worth of payday loans.³ In 2004, the industry made \$50 billion in loans,⁴ a staggering 525% increase in just five years. That same year, it was estimated that the industry charged \$3.4 billion a year in fees, such as interest and finance charges, to payday loan borrowers.⁵

The attractive growth potential offered by the payday loan industry has caused an explosion in the number of payday loan stores around the nation; their number doubled between the years 2000 and 2003 and stood, in 2005, at 22,000.⁶ To put this growth in

1. Many authorities credit Mr. Jones with having started the modern payday loan industry in 1993, but this has not been conclusively verified. See Charles A. Bruch, Comment, *Taking the Pay Out of Payday Loans: Putting an End to the Usurious and Unconscionable Interest Rates Charged by Payday Lenders*, 69 U. CIN. L. REV. 1257, 1270 (2001).

2. Lynn Drysdale & Kathleen E. Keest, *The Two-tiered Consumer Financial Marketplace: The Fringe Banking System and Its Challenge to Current Thinking About the Role of Usury Laws in Today's Society*, 51 S.C. L. REV. 589, 618 (2000). Due to the enactment of the Uniform Small Loan Act in 1916, such practices had all but vanished by World War II. See *id.* at 620-21.

3. Teresa Dixon Murray, *Fast Money at a Steep Price: Firms Thrive Providing Quick Cash, Goods at Exorbitant Rates*, PLAIN DEALER (Cleveland), Feb. 13, 2005, at A1.

4. *Id.*

5. Steve Hartsoe, *N.C. Officials Strengthen Payday Lending Inquiry: Advance America Told To Turn Over Papers; Subpoena Issued*, CHARLOTTE OBSERVER, Aug. 27, 2004, at 3D.

6. Ieva M. Augstums, *Fast Cash Is Gaining Currency: Local Firms Expand as Payday Lending Goes Mainstream*, DALLAS MORNING NEWS, Jan. 4, 2005, at 1D.

perspective, there are more payday loan stores in the state of California than there are McDonald's and Burger King restaurants combined.⁷ Despite this rapid expansion, and the subsequent increase in competition among payday loan lenders, the fees charged to borrowers for receiving payday loans have not decreased, as would be expected; since 1993, most fees have remained at the maximum allowed by law.⁸

The dramatic growth of the payday loan industry and the failure of the market to self-regulate payday loan fees have caused concern for many consumer protection advocates, who call for the reform of a system that they claim takes advantage of poor and uneducated borrowers, often forcing these borrowers to refinance when unable to repay their loans.⁹ Payday loan critics also complain that many lenders have aggressive, unfair collection practices.¹⁰ Although payday loan critics have proposed several types of reform, most, if not all, have recommended the imposition of usury laws—laws restricting the amount of interest a lender can charge—to prevent payday lenders from taking advantage of borrowers.¹¹ The imposition of usury law on the payday loan industry presents two concerns. First, loopholes in federal legislation have historically prevented successful enforcement of usury laws against payday lenders.¹² Second, assuming these loopholes could be closed, the enforcement of strict usury laws against payday lenders could, by making payday lending unprofitable, eliminate the industry.¹³ If the goal of a state with payday lending problems is to eliminate the industry, then usury laws would be an effective tool for doing so.¹⁴

If, however, the aim of the state is not to end payday lending, but rather to ensure that borrowers are treated fairly by lenders, then the use of usury laws is not the ideal approach. Instead, payday loan reform should create a situation that is acceptable for both lenders

7. Michael A. Stegman & Robert Faris, *Payday Lending: A Business Model That Encourages Chronic Borrowing*, 17 ECON. DEV. Q. 8, 9 (2003).

8. Creola Johnson, *Payday Loans: Shrewd Business or Predatory Lending?*, 87 MINN. L. REV. 1, 117 (2002).

9. *See id.* at 69-70.

10. *See id.* at 77.

11. *See infra* Part III.

12. *See infra* Part III.A.

13. *See infra* Part III.B.

14. *See infra* Part III.B.

and borrowers. The best way to protect borrowers, while still allowing payday lenders the freedom to issue consensual loans, is to change the way payday lending operates. Four adjustments in payday lending are necessary to enable this balance: (1) ensuring that borrowers are informed; (2) limiting loan refinancing; (3) guaranteeing that fair collection practices are followed; and (4) improving enforcement of the law.

This Note will analyze the problems associated with payday lending in four parts. First, a discussion of the demographics of payday loan borrowers will show that payday loans are often targeted at borrowers who tend to be less educated and economically disadvantaged. Second, a detailed description of how the payday loan industry works will point to refinancing as the most serious problem afflicting payday loan borrowers. Third, analysis of usury laws in connection with payday lending will reveal the flaws inherent in a solution that seeks only to restrict interest rates. Finally, this Note will propose a solution that effectively regulates the industry, without the disadvantages of strict usury laws.

I. PAYDAY LOAN BORROWER DEMOGRAPHICS

One of the reasons most frequently offered to justify regulation of the payday loan industry is that it preys on minorities, women, and those who are poor or uneducated.¹⁵ Statistics supplied by the payday loan industry refute this claim; however, those supplied by various state agencies appear to support it.¹⁶

Most of the industry's statistics are derived from a survey conducted by the Credit Research Center at Georgetown University.¹⁷ According to the survey, about half of payday loan borrowers have an average annual income between \$25,000 and \$50,000.¹⁸ The survey also indicated that almost ninety-four percent of borrowers

15. See, e.g., Johnson, *supra* note 8, at 100-01.

16. See *infra* notes 17-20, 37-46 and accompanying text.

17. GREGORY ELLIEHAUSEN & EDWARD C. LAWRENCE, CREDIT RESEARCH CTR., PAYDAY ADVANCE CREDIT IN AMERICA: AN ANALYSIS OF CUSTOMER DEMAND (2001), available at http://www.cfsa.net/downloads/analysis_customer_demand.pdf.

18. See *id.* at 28.

have a high school diploma, and that more than half have completed at least some college.¹⁹

On their face, these findings lend support to payday loan industry claims that payday lending does not take advantage of poor and uneducated borrowers; however, the survey has serious flaws that cast doubt on its results. First, the findings are based on a very small sample size. The study began with a pool of 5364 payday loan borrowers, randomly selected from payday loan offices nationwide.²⁰ Survey takers then attempted to conduct interviews with the selected borrowers by placing telephone calls to their residences.²¹ An amazing 1274 borrowers, or about twenty-four percent of the initial pool, could not be reached because their phone numbers were invalid.²² Another 1894 borrowers, an additional thirty-five percent of the initial pool, were not available during the interview period.²³ Survey takers made contact with only about half the initial pool, or 2196 borrowers.²⁴ Of those borrowers actually contacted, 1584, or seventy-two percent, either denied having received a payday loan or refused to be interviewed.²⁵ The final sample from which the study drew its conclusions consisted of only 427 borrowers, or eight percent of the total sample.²⁶ That the initial sample of 5364 borrowers itself was only a small sample of the total number of borrowers who use the country's more than 10,000 payday loan offices²⁷ emphasizes how small the final sample of 427 borrowers really was.

The small sample size raises serious concerns about the accuracy of the study's conclusion because it is likely that the sample was not an accurate representation of the average payday loan borrower.²⁸ Furthermore, the authors of the study acknowledged that most

19. See *id.* at 33 (noting that about thirty-six percent of borrowers had completed some college and an additional nineteen percent had college degrees).

20. *Id.* at 20-21.

21. *Id.*

22. ELLIEHAUSEN & LAWRENCE, *supra* note 17, at 20-21.

23. *Id.*

24. *Id.* at 21.

25. See *id.*

26. *Id.*

27. *Id.* at 2.

28. See 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, 663 n.48 (2005).

respondents who quit the interview did so after the first few questions asked about the type of credit the respondents had previously used.²⁹ Those who refused to admit they had used a payday loan “were unwilling to answer financial questions and answered ‘no’ to avoid further questions of this nature.”³⁰ This finding is important because those with the greatest financial difficulties would probably be the most reluctant to participate in an interview because of embarrassment or fear. Also, some of the most impoverished borrowers might not have had access to a telephone, or might have been working longer or more irregular hours, making it less likely that they could have been reached for an interview. All these factors provide reason to believe that those borrowers who did participate in the interview were better off financially than the average borrower.³¹

The second flaw with the study is that the authors interviewed borrowers who had taken out a loan during the six months leading up to and through the holiday season.³² From October to January, even individuals making \$50,000 a year might be in need of extra holiday cash and need to take advantage of a payday loan to make up the difference. Some borrowers may have taken out loans in advance of an expected Christmas bonus, knowing the bonus would arrive in time for the payday loan to be paid in full when due. The survey easily could have avoided this potential problem by drawing from an initial pool of borrowers who had taken out a loan between January and December.

The final potential problem with the survey is that it was financed in part by the Community Financial Services Association of America, one of the trade associations of the payday loan industry.³³ In fact, Association members provided the names of borrowers for the study.³⁴ The Association’s involvement casts suspicion on whether the study was conducted in a manner that would lead to results favorable to the industry, whether intention-

29. ELLIEHAUSEN & LAWRENCE, *supra* note 17, at 21.

30. *Id.*

31. Graves & Peterson, *supra* note 28, at 663 n.48.

32. Eligible participants were those who had taken out a loan within the six months prior to the December and January interviews. ELLIEHAUSEN & LAWRENCE, *supra* note 17, at 20.

33. *Id.* at iii.

34. *Id.* at 19-20.

ally or unintentionally.³⁵ This suspicion is only bolstered by the fact that the Government Accountability Office (formerly the General Accounting Office) has criticized the Credit Research Center in the past for making assumptions in favor of the lending industry.³⁶

Studies and surveys organized by state-funded organizations have painted a much bleaker picture of the payday loan industry. One Colorado study, for example, found that “[t]he ‘average’ Colorado payday loan borrower is a thirty-six-year-old single woman, making \$2370 per month, employed as a laborer or office worker and in her current job for about three and one-half years.”³⁷ A 1999 survey by the Illinois Department of Financial Institutions found that the average payday loan borrower’s salary was just over \$25,000,³⁸ while the average income for the citizens of the state as a whole was over \$31,000.³⁹ In Wisconsin, the average borrower’s gross income in 2001 was only \$24,673,⁴⁰ whereas the average gross income of Wisconsin citizens that year was almost \$32,000.⁴¹

Statistics like these have led opponents of the payday loan industry to conclude that payday loan lenders specifically target minorities and low-income individuals.⁴² A study conducted for the American Association of Retired Persons found that low-income and minority households were more likely to have a payday loan store within a mile of their homes than higher-income and non-minority

35. This is not to say that the study has no probative value in the payday loan debate and should be completely disregarded. The data, especially the opinions about the payday loan industry offered by payday loan users, can shed some light on the different sides of the debate. That data, however, must be considered carefully, especially in light of the state-funded data that produced different results. See *infra* notes 37-46 and accompanying text.

36. See Elizabeth Warren, *The Market for Data: The Changing Role of Social Sciences in Shaping the Law*, 2002 WIS. L. REV. 1, 11, 18.

37. Paul Chessin, *Borrowing from Peter To Pay Paul: A Statistical Analysis of Colorado’s Deferred Deposit Loan Act*, 83 DENV. U. L. REV. 387, 405 (2005).

38. ILL. DEPT’ OF FIN. INST., SHORT TERM LENDING: FINAL REPORT 26 (1999), available at <http://www.idfpr.com/dfi/ccd/pdfs/Shortterm.pdf> [hereinafter ILLINOIS REPORT].

39. U.S. CENSUS BUREAU, STATISTICAL ABSTRACT OF THE UNITED STATES: 2000, at 460 (2000), available at https://www.census.gov/prod/www/statistical-abstract-1995_2000.html (showing per capita income in Illinois in 1999 to be \$31,278 in current (1999) dollars).

40. Johnson, *supra* note 8, at 99.

41. See U.S. CENSUS BUREAU, STATISTICAL ABSTRACT OF THE UNITED STATES: 2003, at 422 (2003), available at http://www.census.gov/prod/www/statistical-abstract-2001_2005.html.

42. See Johnson, *supra* note 8, at 100.

households.⁴³ A North Carolina survey found that, even among low-income households, African Americans were twice as likely as Caucasians to have taken out a payday loan.⁴⁴ Non-industry-sponsored reports also support the conclusion that the average payday loan borrower's salary falls below national averages,⁴⁵ and that payday loan borrowers are often minorities.⁴⁶

There is nothing inherently immoral or illegal about specifically targeting a service at minorities and low-income individuals, unless the service takes advantage of these groups; an understanding of how the payday loan industry operates demonstrates that at least some lenders are taking advantage of these, and other, payday loan borrowers.

II. THE NATURE OF THE PAYDAY LOAN INDUSTRY

A. *The Payday Loan Process*

Most payday lenders use roughly the same process for issuing loans.⁴⁷ First, the borrower and the lender agree about the size of the loan and the amount of its accompanying finance charge.⁴⁸

43. See SHARON HERMANSON & GEORGE GABERLAVAGE, AM. ASS'N OF RETIRED PERSONS, THE ALTERNATIVE FINANCIAL SERVICES INDUSTRY 4 & fig. 4 (2001), available at http://assets.aarp.org/rgcenter/consume/ib51_finance.pdf.

44. Stegman & Faris, *supra* note 7, at 15.

45. See Johnson, *supra* note 8, at 99 ("In the six states where over half of the nation's payday lenders are located, the median incomes are below the national median, and in four of them, the poverty rates are above average."). Compare Chessin, *supra* note 37, at 406 (noting that the average monthly income for Colorado payday loan borrowers is \$2373, which equals only \$28,476 a year, and noting an "inverse relationship" between income and use of payday loans), and Stegman & Faris, *supra* note 7, at 15 (reporting that in Indiana, Illinois, and Wisconsin, the average income of payday loan borrowers are, respectively, \$25,000 to \$30,000, \$24,000, and \$19,000), with U.S. CENSUS BUREAU, STATISTICAL ABSTRACT OF THE UNITED STATES: 2006, at 452 (2006), available at <http://www.census.gov/compendia/statab/2006/2006edition.html> (showing that from 2000 to 2004, the approximate time period in which the above studies were conducted, the average per capita income in the United States increased from \$29,845 to \$32,937 measured in 2000 dollars), and *id.* at 468 (showing average household income in 2003 to be \$43,564). Because some of the above studies discussed household income and others appeared to focus on individuals, both are included.

46. See, e.g., Johnson, *supra* note 8, at 100; Stegman & Faris, *supra* note 7, at 15.

47. See WILLIAM O. BROWN, JR. ET AL., CONSUMER CREDIT RESEARCH FOUND., THE PAYDAY PRIMER 2 (2004), available at http://www.consumercreditresearchfoundation.org/_files/PaydayLendingFinal_woTitle.pdf.

48. *Id.*

About half of all payday loans are for amounts between two and three hundred dollars, and the typical finance charge runs between fifteen and twenty dollars for every hundred dollars borrowed.⁴⁹ Second, after the lender and borrower have agreed on the loan and its accompanying fees, the borrower usually must show a recent bank statement, a pay stub, and identification.⁵⁰ Third, the lender verifies the information and decides whether the borrower is creditworthy.⁵¹ Fourth, the borrower writes a postdated check (or authorizes a future electronic debit from her checking account) for the combined value of the loan and the finance charge, then receives her loan.⁵² Finally, unless the loan is repaid or refinanced within a specific period of time, usually within two weeks, the lender deposits the check, or electronically withdraws payment from the borrower's account.⁵³

The payday loan industry advertises payday loans as superior to writing bad checks or paying late fees. Instead of paying the national average of twenty-five dollars in bank and merchant return-check fees on a one hundred dollar check, the industry argues, a borrower can take out a payday loan for a fee of only fifteen dollars.⁵⁴ The industry makes similar claims regarding the advantage of payday loans over late payments on car loans, credit card balances, utility bills, and rent.⁵⁵

Although there might be some truth to the industry's claim, the argument has three flaws that limit the value of payday loans as a viable alternative to bad checks and late fees. First, few people write bad checks when they know they have insufficient funds, so few turn to payday loans as a substitute for a returned-check fee.⁵⁶ Second, when the car loan, utility bill, credit card payment, or rent comes due again the following month, the borrower will probably again be unable to pay because repayment of the payday loan will

49. *Id.*

50. Johnson, *supra* note 8, at 9.

51. BROWN ET AL., *supra* note 47, at 2.

52. Drysdale & Keest, *supra* note 2, at 601. In some cases, especially through internet-based lenders, a delayed automatic debit agreement is used in place of a check. *Id.*

53. *Id.*

54. See CMTY. FIN. SERVS. ASS'N OF AM., PAYDAY ADVANCE: A COST EFFECTIVE ALTERNATIVE 10 (2002) [hereinafter PAYDAY ADVANCE].

55. See generally *id.*

56. Drysdale & Keest, *supra* note 2, at 606.

be due.⁵⁷ At best, therefore, a payday loan can defer these fees and late charges only until they are due the next month.⁵⁸

Finally, the industry's argument that payday loans are a convenient alternative to returned-check fees and late charges is defective because borrowers, who often find their funds insufficient the next month to cover both their normal expenses and repayment of the payday loan, are forced to refinance, or "roll over," the loan for an additional fee.⁵⁹ This cycle may continue until the borrower has refinanced so many times that the total cost of the payday loan far exceeds any late fees or returned check charges that the borrower would have faced had she not taken the loan.⁶⁰ This refinancing trap is the most serious consumer interest concern in payday lending.

B. The Refinancing Trap

The availability of and need for refinancing makes payday loans different from other, similar loans, such as those given by rent-to-own stores and pawn shops. With rent-to-own and pawn companies, if borrowers default on the loan, they simply lose their security interest and walk away with no further obligations or charges.⁶¹ Defaulting payday loan borrowers, however, remain obligated to pay not only the loan principal and fees, but also any applicable interest and returned-check charges.⁶²

Refinancing is a common problem in payday lending. A joint survey conducted by the Consumer Federation of America and the U.S. Public Interest Research Group found that about eighty-three percent of payday loan stores allow borrowers to renew unpaid loans.⁶³ A North Carolina study concluded that half of all the payday

57. *Id.*

58. *Id.*

59. *See id.* at 601, 606.

60. *See infra* Part II.B.

61. Bruch, *supra* note 1, at 1273.

62. *See, e.g.,* Turner v. E-Z Check Cashing of Cookeville, TN, Inc., 35 F. Supp. 2d 1042, 1046 (M.D. Tenn. 1999) (describing a check cashing agreement that included such obligations).

63. CONSUMER FED'N OF AM. & U.S. PUB. INTEREST RESEARCH GROUP, RENT-A-BANK PAYDAY LENDING: HOW BANKS HELP PAYDAY LENDERS EVADE STATE CONSUMER PROTECTIONS 5 (2001), available at <http://www.consumerfed.org/pdfs/paydayreport.pdf> [hereinafter RENT-A-BANK LENDING].

loan borrowers surveyed paid more in refinancing fees than the value of their initial loans.⁶⁴ This refinancing trap has become a problem serious enough to merit the attention of the U.S. Comptroller of the Currency, who stated that “[o]ne of the principal features of payday loans that have led to abuses is frequent renewal, resulting in additional fees to the consumer.”⁶⁵

Despite the accusations levied by consumer advocates, the payday loan industry continues to deny that refinancing is a problem.⁶⁶ According to the industry’s Best Practices guidelines, a list of ideals proposed for payday lenders, a lender should allow a borrower to refinance a loan no more than four times, or the maximum number of times allowed by applicable law, whichever is fewer.⁶⁷

Even if these Best Practices guidelines were binding, lenders could easily evade or ignore them by having borrowers repay the initial loan, sometimes with cash obtained from a different payday loan company, write a new check, and start the cycle anew.⁶⁸ Critics of the payday loan industry refer to this practice as “touch and go” financing.⁶⁹ Some payday lenders do not even consider such transactions to be refinancing. One Colorado payday loan company argued, for example, that a law disallowing the renewal of a payday loan more than once did not apply to a series of loans made to a borrower who, on eight separate occasions, paid back the previous loan, and then immediately took out a new one for the same amount.⁷⁰

64. *Id.* at 9.

65. OCC Corporate Decision No. 2005-11 (July 12, 2005), 2005 OCC Ltr. LEXIS 59, at 5.

66. Community Financial Services Association of America, Payday Advance: Fact vs. Fiction, http://www.cfsa.net/fact_vs_fiction.html (last visited Mar. 18, 2007).

67. Community Financial Services Association of America, Best Practices for the Payday Advance Industry, http://www.cfsa.net/industry_best_practices.html (last visited Mar. 18, 2007) [hereinafter Best Practices]. These best practices apply to payday loan companies that belong to the Community Financial Services Association of America, one of the leading payday lending associations. The Consumer Fed’n of Am. (CFA) is critical of the industry’s guidelines, arguing that “[t]rade groups can’t enforce voluntary guidelines against their own members” Press Release, Consumer Federation of America, Payday Lenders Shred Consumer Safety Net (Oct. 3, 2002), available at http://www.consumerfed.org/releases2.cfm?filename=100302_payloans_shrednet.txt. The CFA believes that “Best Practices’ are more public relations than consumer protection.” *Id.*

68. RENT-A-BANK LENDING, *supra* note 63, at 9.

69. Drysdale & Keest, *supra* note 2, at 601.

70. Johnson, *supra* note 8, at 67.

In reality, despite state laws and the industry's assurances, various studies indicate that many borrowers refinance their initial loans many times.⁷¹ In Illinois, for example, the average payday loan borrower remains a borrower for at least six months.⁷² In Indiana, seventy-seven percent of loans are rolled over, with the average borrower refinancing the loan ten times before it is fully paid.⁷³ The average payday loan borrower will spend \$1105 to repay a \$325 loan, and will have an outstanding payday loan for thirty weeks of the year.⁷⁴ These studies reveal that many payday loan borrowers are finding themselves unable to repay their initial loans within the two-week period, and some are forced to refinance many times before they are able to repay the initial loan.

There are four reasons that borrowers are often required to refinance their payday loans. First, lenders frequently make poor lending decisions by failing to inquire about the borrower's expenses, or by approving a loan equivalent to a large proportion of the borrower's monthly income.⁷⁵ Second, the short period of time borrowers are given to repay the loan is often insufficient for the borrower to assemble the sum necessary for repayment.⁷⁶ Industry critics note that "[f]ew low and moderate income consumers can afford to repay the average [payday loan] in one lump sum and still have enough to cover other expenses without having to roll-over the loan or borrow again before the next payday."⁷⁷ If the borrower's paycheck was insufficient to meet expenses during one pay period, it will probably be insufficient to meet the next pay period's financial needs, especially because additional funds will be required to repay the loan.⁷⁸

71. *E.g.*, Drysdale & Keest, *supra* note 2, at 608.

72. *Id.*

73. *Id.*

74. *Predatory Lending and Its Impact on the Military and Local Communities: Hearing Before the H. Subcomm. on Rural Enterprise, Agriculture, and Technology of the H. Comm. on Small Business*, 109th Cong. 3 (2005) [hereinafter *Hearing*] (written statement of the Center for Responsible Lending), available at http://www.responsiblelending.org/pdfs/Testimony-Graves_payday-032905.pdf.

75. See Johnson, *supra* note 8, at 59-60.

76. *Id.*; see also Bruch, *supra* note 1, at 1281.

77. RENT-A-BANK LENDING, *supra* note 63, at 8.

78. See Johnson, *supra* note 8, at 59.

The third reason for extensive refinancing is the industry's prohibition on accepting partial payments.⁷⁹ Even if a borrower has \$299 to pay back a \$300 loan, he or she cannot repay the loan, but must refinance the full amount and pay an additional finance charge. The industry's unwillingness to accept partial payments leads to the fourth reason refinancing so commonly occurs: if the only way borrowers can prevent default is by rolling over the loan, paying a refinancing fee, and paying returned-check fees if the lender has deposited the postdated check, the borrowers will often be unable to save the required sum of money by the next date payment is due.⁸⁰

For example, a borrower that manages to save only \$100 toward repaying a \$200 loan must refinance, and pay the cost of refinancing the loan, in addition to returned-check fees. These additional fees may end up costing the borrower the entire \$100 initially earmarked for loan repayment. After refinancing the loan, the borrower might again save only \$100 toward loan repayment by the next due date, and would again be forced to spend his entire \$100 in fees. For some borrowers, this cycle ends only after they have spent up to a thousand dollars in their efforts to repay a loan of just a few hundred dollars.⁸¹

Payday loan refinancing continues to be a problem because lenders have little incentive to restrict it.⁸² Most laws designed to restrict refinancing are simply circumvented or ignored by creative lenders.⁸³ A viable solution for the problems associated with payday lending must do more than create laws to restrict lenders; it must provide lenders with an incentive for eliminating those practices injurious to borrowers. Such incentives are essential to payday lending regulation because lenders have, historically, attempted to circumvent regulations.

79. *Id.*

80. *E.g.*, Chessin, *supra* note 37, at 409-10.

81. See Regina Austin, *Of Predatory Lending and the Democratization of Credit: Preserving the Social Safety Net of Informality in Small-loan Transactions*, 53 AM. U. L. REV. 1217, 1222 & n.23 (2004) (citing Peter T. Kilborn, *New Lenders with Huge Fees Thrive on Workers with Debts*, N.Y. TIMES, June 18, 1999, at A28, as an example of such a situation).

82. Dysdale & Keest, *supra* note 2, at 608.

83. See *infra* Part II.C.

C. Attempts To Avoid Regulation

Payday lenders have been creative in their attempts at avoiding the regulations placed on most other types of lending. Some payday loan companies, for example, have created sham business transactions in order to avoid being labeled as "lenders." One such transaction is the sale-leaseback business,⁸⁴ in which the payday loan company "purchases" one of the borrower's appliances for a small sum of money.⁸⁵ The lender then "leases" the appliance back to the borrower for a small fee until the borrower can "repurchase" the appliance for the price the lender paid.⁸⁶ The lender does not take actual possession of the appliance; it remains with the borrower throughout the period of the lease.⁸⁷ Few would disagree that the companies engaged in transactions of this type have little interest in owning used consumer appliances or in leasing those appliances to their previous owners. The true purpose of such transactions is to disguise a loan as a lease in order to avoid lending regulations.⁸⁸

In another ploy, a payday loan company will cash a postdated check for the borrower and then, for a fee, issue the borrower some catalog certificates with which the borrower can purchase items from a catalog provided by the lender.⁸⁹ Essentially, the fees the lender charges the borrower are disguised as the cost of buying the certificates.⁹⁰ In *Cashback Catalog Sales v. Price*,⁹¹ the Southern District of Georgia was asked to determine whether this type of transaction should be considered a loan under state lending laws. The catalog company argued that the cashing of the check and the sale of the catalog certificates were two separate transactions, and that neither could therefore be considered a loan.⁹² Additionally, the company pointed out that no credit evaluations were made, and no

84. See Johnson, *supra* note 8, at 18; Robert Elder, Jr., *Battle Over Small Loans Turns into Big Production*, WALL ST. J. (Texas Edition), Apr. 28, 1999, at T1.

85. See Johnson, *supra* note 8, at 18; Elder, *supra* note 84.

86. See Johnson, *supra* note 8, at 18.

87. *Id.*

88. See *id.* at 24 n.121 ("Payday lenders continue to fabricate new schemes to evade the law.").

89. *Id.* at 19-20.

90. See *id.*

91. 102 F. Supp. 2d 1375 (S.D. Ga. 2000).

92. *Id.* at 1377.

interest or fees were charged for cashing the check.⁹³ The court found, however, that the transaction was a loan, and was thus subject to applicable lending laws.⁹⁴ The court noted that the company advertised in the yellow pages under “Loans” and that the catalog issued by the company did not contain an order form, an address, an “800” number, a website, or any other information indicating how those with catalog certificates could redeem them for merchandise.⁹⁵

These disguised transactions have been increasingly recognized by courts and lawmakers for what they are: consumer loans. The Board of Governors of the Federal Reserve has explicitly stated that payday advances are to be considered loans if the advancer of the funds regularly extends credit and charges a fee for the service, regardless of how the fee is characterized.⁹⁶ As the Board of Governors of the Federal Reserve System noted in 2000, “[t]ransactions in which the parties agree to defer payment of a debt are ‘credit’ transactions regardless of the label used to describe them.”⁹⁷ Although many of the attempts at disguising the loan in order to avoid regulation are no longer practiced, they illustrate the willingness of some in the payday loan industry to skirt regulations. For this reason, effective solutions to payday lending problems must provide incentives so payday lenders will follow the law instead of seeking creative ways to circumvent it.

93. *Id.*

94. *Id.* at 1380.

95. *Id.* at 1377.

96. The Federal Reserve Board’s Division of Consumer and Community Affairs interpreted the definition of credit to comprise such schemes:

Credit includes a transaction in which a cash advance is made to a consumer in exchange for the consumer’s personal check, or in exchange for the consumer’s authorization to debit the consumer’s deposit account, and where the parties agree either that the check will not be cashed or deposited, or that the consumer’s deposit account will not be debited, until a designated future date. This type of transaction is often referred to as a “payday loan” or “payday advance” or “deferred presentment loan.” A fee charged in connection with such a transaction may be a finance charge for purposes of § 226.4, regardless of how the fee is characterized under state law. Where the fee charged constitutes a finance charge under § 226.4 and the person advancing funds regularly extends consumer credit, that person is a creditor

Regulation 2 Official Staff Interpretations, 12 C.F.R. § 226, Supp. 1, at 226.2(a)(14) (2006).

97. Truth in Lending, 65 Fed. Reg. 17,129, 17,130 (Mar. 31, 2000).

D. Questionable Collection Practices

Opponents of the payday loan industry have cited the industry's questionable collection practices as another reason for increased regulation.⁹⁸ While the industry's Best Practices guidelines instruct member loan stores to avoid harassing borrowers,⁹⁹ some critics charge that harassment still occurs.¹⁰⁰ One of the most shocking collection practices, however, takes advantage of bad check laws designed to protect innocent merchants, who unknowingly accept checks, from dishonest buyers, who know that the checks will be returned due to insufficient funds.¹⁰¹ Some payday loan lenders try to coerce borrowers into repaying a loan by threatening criminal prosecution for bad-check writing if a borrower does not repay his loan.¹⁰²

Some states also allow merchants to collect punitive damages, sometimes for up to three times the face value of the check, when a buyer knowingly issues a bad check.¹⁰³ Payday lenders take advantage of these laws by cashing the borrower's postdated check after the borrower fails to pay, knowing it will be returned unpaid.¹⁰⁴ The lenders then threaten to (or actually do) sue for and collect punitive damages against the defaulted borrowers;¹⁰⁵ the theory in support of punitive damages is that when the loan was issued, the borrower knew that the account from which the check would be drawn was insufficient to cover the value of the check

98. See, e.g., Johnson, *supra* note 8, at 77.

99. Best Practices, *supra* note 67.

100. Johnson, *supra* note 8, at 77-78 (describing borrower complaints about "vexing" phone calls, threats of violence, excessive damages being collected, threats of criminal prosecution, and lender requirements that borrowers waive any privacy rights against the lender and provide descriptions of their automobiles).

101. See *id.* at 78.

102. In one Dallas precinct alone, payday lenders filed over 13,000 criminal complaints. Drysdale & Keest, *supra* note 2, at 610.

103. See, e.g., 720 ILL. COMP. STAT. ANN. 5/17-1(B); 5/17-1a (West 2003) (providing treble damages and attorneys' fees as remedies against those who knowingly issue a bad check with the intent to gain control over the property, labor, or services of another person); OHIO REV. CODE ANN. § 2307.61 (West 2004) (allowing the victims of some crimes, including the recipients of bad checks, to recover liquidated damages equaling the greater of \$200 or triple the amount of the check; explicitly exempting checks tendered to check-cashing businesses from the triple damages provision but not from the \$200 provision).

104. Drysdale & Keest, *supra* note 2, at 600-01; Johnson, *supra* note 8, at 78-80.

105. Johnson, *supra* note 8, at 79-80.

written to the lender. One Illinois debtor, for example, borrowed \$200 with a check written for \$240, and eventually defaulted on the loan.¹⁰⁶ The payday lender sued seeking \$1260, almost four times the value of the loan.¹⁰⁷ This figure included the value of the initial loan, an additional \$720 in punitive damages, and \$300 in attorney's fees.¹⁰⁸

The threat and the use of bad check laws further exacerbates the refinancing problem, as explained by the Consumer Federation of America and the U.S. Public Interest Research Group:

A customer who fails to redeem the check for cash or have enough on deposit to cover the deposited check or electronic withdrawal on the due date faces bounced check fees from both the payday lender and the bank. Some lenders in some states sue for triple damages under civil bad check provisions. And, some lenders have threatened or used the criminal bad check laws when customers are unable to repay. Faced with the high cost of default, many borrowers rollover their debts.¹⁰⁹

Fearing criminal and/or civil penalties when they are unable to repay their payday loans, borrowers have little choice but to refinance.¹¹⁰

The availability of bad check laws places payday loan borrowers in a situation that is unique to payday lending. Unlike borrowers from more traditional sources, payday loan borrowers face the possibility of both civil and criminal prosecution, including the possibility of treble or other punitive damages.¹¹¹ This situation forces borrowers, who would ordinarily default, to refinance, rather than face additional repercussions. By allowing lenders to prosecute borrowers for writing a bad check, the law essentially allows borrowers to be prosecuted for defaulting on their debts.¹¹² While the law should seek to discourage borrowers from defaulting on debts,

106. Drysdale & Keest, *supra* note 2, at 612 n.127.

107. *See id.*

108. *Id.*

109. RENT-A-BANK LENDING, *supra* note 63, at 8.

110. *Id.*

111. Compare Johnson, *supra* note 8, at 89 ("Normally, a consumer does not commit a crime when he or she defaults on a loan."), *supra* note 60 and accompanying text, and *infra* note 114 and accompanying text, with Johnson, *supra* note 8, at 78, 86-87.

112. Johnson, *supra* note 8, at 89-90.

it should not do so by criminalizing the failure to pay. Debtor's prison has not existed in the United States since the Civil War,¹¹³ and it should not be reinstituted today for punishing defaulting payday loan borrowers.

Using bad check laws to collect on unpaid loans puts payday loan companies in a favorable position not available to other creditors. "You don't get sued for triple your car payment if you miss a car payment," noted Jean Ann Fox, director of consumer protection for the Consumer Federation of America.¹¹⁴ "But," she added, "payday lenders have been doing this because no one put a stop to it."¹¹⁵ The payday loan industry's recovery efforts should be limited to the remedy available to other lenders: a civil suit for the amount of the debt and reasonable court fees.

Allowing payday lenders to take advantage of bad check laws is especially troublesome because, properly understood, "[p]ayday loan prosecutions concern the breach of a contract to repay a loan, not the deceptive practice of convincing a creditor that a bad check was good."¹¹⁶ Unlike innocent merchants who unknowingly receive bad checks for their wares, payday lenders are fully aware that borrowers do not have sufficient funds in their accounts to cover the check; otherwise, the borrower would not be seeking a payday loan.¹¹⁷ Payday lenders insist on receiving a postdated check from a borrower with full knowledge that the borrower does not currently have sufficient funds in her account,¹¹⁸ and lenders should therefore be estopped from claiming they have been wronged by an action that they themselves demanded.¹¹⁹

Even where this practice has been specifically forbidden by statute, borrowers are often unaware of the protection, so lenders may still threaten borrowers, even if those threats could not be

113. See Graves & Peterson, *supra* note 28, at 665.

114. Teresa Dixon Murray, *State Law Will Help 'Payday' Debtors*, PLAIN DEALER (Cleveland), May 2, 2000, at 1C.

115. *Id.*

116. Johnson, *supra* note 8, at 130.

117. Turner v. E-Z Check Cashing of Cookeville, TN, Inc., 35 F. Supp. 2d 1042, 1051 (M.D. Tenn. 1999).

118. Drysdale & Keest, *supra* note 2, at 601. In some cases, especially through Internet-based lenders, a delayed automatic debit agreement is used in place of a check. *Id.*

119. *Id.* at 611 ("Certainly a lender's exaction of a fee to 'defer' deposit signifies the requisite acceptance ... necessary to remove the transaction from the realm of the criminal bad check statute.").

executed.¹²⁰ After Ohio forbade payday lenders from using bad check laws to collect treble damages, for example, not only were borrowers unaware of the changes, but many payday lenders continued to warn borrowers in their contracts that if the borrower defaulted, the lender would sue for and collect triple the amount owed.¹²¹

Because laws preventing lenders from seeking civil or criminal penalties against defaulting borrowers might not prevent some lenders from nevertheless threatening to do so, effective payday lending reform should ensure that borrowers recognize and understand that the lender cannot use civil or criminal bad check laws. This reform would prevent lenders from using invalid threats in an attempt to collect the debt.¹²² Effective regulation of the payday loan industry must ensure that fair collection practices are followed.

III. USURY LAWS

A. Why Usury Laws Fail: Charter Renting

Many payday loan opponents have called for the application of strict usury laws to payday loan transactions in order to solve the problems associated with payday lending.¹²³ Setting aside for a moment questions about the wisdom of usury laws in payday lending, it should be noted that such efforts have often failed to resolve payday lending problems because of what lending commentators call “charter renting.”¹²⁴ The National Bank Act (NBA) allows nationally chartered banks to charge interest at the rate allowed by the state in which the bank is located, even if the usury laws of the

120. See Johnson, *supra* note 8, at 80-81.

121. *Id.*

122. For example, Kentucky amended its payday loan statute to require a posted notice informing borrowers that they could not be criminally prosecuted. KY. REV. STAT. ANN. § 368.100(18) (LexisNexis 2002) (to be codified at KY. REV. STAT. § 286.9-100(18)).

123. See, e.g., Drysdale & Keest, *supra* note 2, at 657-66; Graves & Peterson, *supra* note 28, at 829-31; Robin A. Morris, *Consumer Debt and Usury: A New Rationale for Usury*, 15 PEPP. L. REV. 151, 173-74 (1988).

124. Elizabeth R. Schiltz, *The Amazing, Elastic, Ever-expanding Exportation Doctrine and Its Effect on Predatory Lending Regulation*, 88 MINN. L. REV. 518, 575 (2004); see also Graves & Peterson, *supra* note 28, at 828 (discussing Texas payday lenders' use of the “charter-renting” legal strategy” to evade state law).

state in which the loan is issued set a lower maximum rate.¹²⁵ Similarly, the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA) also allows state-chartered banks that are federally insured to charge an interest rate allowed by the laws of the state in which the bank is located.¹²⁶

Some payday lenders have taken advantage of the NBA and DIDMCA to avoid the usury laws of the state in which they do business. These lenders contract with national banks or federally insured banks from another state, and the banks officially extend credit to the payday borrower.¹²⁷ This strategy enables the payday lender to charge the maximum rate allowed by the law of the state where the bank is located, rather than that of the state in which the lender is located.¹²⁸ In essence, the bank rents its charter to the payday loan lender so that the lender can avoid the usury laws of the state where loans are made. Some payday lending critics have called this "[t]he most controversial issue in payday lending."¹²⁹

One example of the inefficacy of usury laws due to charter renting occurred a few years ago in Virginia. Virginia attempted to eliminate payday lending by enforcing a maximum Annual Percentage Rate (APR) of thirty-six percent on all small loans.¹³⁰ Three national payday loan companies partnered with national banks, however, to circumvent this restriction, and thrived in Virginia by charging around \$17 for every \$100 borrowed.¹³¹

Virginia's trouble regulating payday lending fees is not unique. According 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, Ace Cash Express, and

125. 12 U.S.C. § 85 (2000); *Marquette Nat'l Bank v. First of Omaha Serv. Corp.*, 439 U.S. 299, 313-19 (1978) (holding that a Nebraska national bank was permitted to charge credit card holders in Minnesota the interest rate allowed under Nebraska law).

126. 12 U.S.C. § 1831d(a) (2000).

127. Schiltz, *supra* note 124, at 582.

128. *Id.*

129. See RENT-A-BANK LENDING, *supra* note 63, at 4.

130. *Id.*

131. *Id.* ACE Cash express partnered with Goleta National Bank in California, Money Mart partnered with Eagle National Bank in Pennsylvania, and Advance America partnered with BankWest, a state bank in South Dakota. *Id.*

has given a \$9 million line of credit to Dollar Financial Corporation, the nation's second-largest chain.¹³²

According to payday loan critics, "[t]he primary motivation of the payday lenders in entering into these arrangements was to obtain the benefit of [the NBA's] exportation powers."¹³³ The payday lenders did not partner with banks in order to benefit from the banks expertise in making loans; many of the payday lenders already had extensive experience in making loans.¹³⁴ And payday lenders could easily cash the checks made out to them without needing to partner with banks for their power to accept deposits.¹³⁵ In fact, in most charter-renting partnerships, the banks have had little, if any, control over lending.¹³⁶

Charter renting runs contrary to the purpose of the NBA, which was originally "to establish a system of national banking institutions, in order to provide a uniform and secure currency for the people, and to facilitate the operations of the Treasury of the United States."¹³⁷ Comptroller of the Currency John D. Hawke commented that "[charter renting] gives us an enormous amount of concern because we believe it is an improper use of the national bank charter."¹³⁸ The California Department of Financial Institutions warned banks that partnering with payday loan companies meant risking damage to their reputations.¹³⁹

This is not to say it is impossible to regulate the industry unless the loophole allowing charter renting is closed. Georgia recently passed legislation that might provide a successful blueprint for preventing charter renting.¹⁴⁰ The Georgia legislature recognized that, despite an opinion issued by the state attorney general in

132. Ron Nixon et al., *Borrowing Trouble: Banks Have Financed Payday Lenders' Expansion*, STAR TRIBUTE (Minneapolis), Aug. 15, 2004, at 15A. A list of some other prominent partnerships can be found in Schiltz, *supra* note 124, at 582 n.306.

133. Schiltz, *supra* note 124, at 582.

134. *Id.*

135. *Id.*

136. *Id.* at 582-83.

137. *Mercantile Bank v. New York*, 121 U.S. 138, 154 (1887).

138. Paul Beckett, *Risky Business: Exploiting a Loophole, Banks Skirt State Laws on High Interest Rates*, WALL ST. J., May 25, 2001, at A1.

139. See Mary Fricker, *Any Day Can Be Payday as Check-cashing Stores Proliferate: Sonoma County Banks Take Steps To Offer More Service to Less-traditional Customers*, PRESS DEMOCRAT (Santa Rosa, Ca.), Aug. 26, 2001, at E1.

140. See GA. CODE ANN. § 16-17-1 (Supp. 2006).

2002¹⁴¹ stating that payday lending was illegal, and despite a cease-and-desist order issued by the Industrial Loan Commission, payday loan companies had continued operating by attempting “to cause these transactions to appear to be ‘loans’ made by a national or state bank chartered in another state in which this type of lending is unregulated, even though the majority of the revenues in this lending method are paid to the payday lender.”¹⁴²

In response, Georgia passed legislation forbidding in-state payday loan companies from issuing loans for and acting as an agent for out-of-state banks when the payday loan companies retain more than half of the proceeds from the loan.¹⁴³ The regulation did not prevent national banks or out-of-state banks, however, from issuing their own payday loans within the state.¹⁴⁴

A few payday loan companies and their out-of-state bank partners filed a lawsuit against the Georgia Attorney General and Secretary of State, attacking the validity of the law.¹⁴⁵ The suit alleged that the law was preempted by section 27(a) of the Federal Deposit Insurance Act, that it violated the dormant Commerce Clause, and that it violated the Federal Arbitration Act.¹⁴⁶ The court, however, held that the Georgia statute did not conflict with any federal law because of the exceptions afforded to out-of-state and national banks.¹⁴⁷

By seeking to eliminate the payday loan industry, Georgia’s legislation might eliminate one of the few legitimate credit options some borrowers may have.¹⁴⁸ But this legislation indicates that if a state wishes to stop payday loan companies from renting the charters of national and out-of-state banks, there might be a way to do so that would not require Congress to amend the NBA and DIDMCA.

Some legal commentators have speculated that closing the NBA and DIDMCA loopholes is necessary to prevent payday lenders from avoiding statutory limitations on not only high interest rates but

141. 2002 Op. Ga. Att’y Gen. 3 (2002), 2002 Ga. AG LEXIS 10.

142. GA. CODE ANN. § 16-17-1(c) (Supp. 2006).

143. *Id.*

144. GA. CODE ANN. § 16-17-2(a)(3) (Supp. 2006).

145. *Bankwest, Inc. v. Baker*, 411 F.3d 1289 (11th Cir. 2005).

146. *Id.* at 1300.

147. *Id.* at 1302.

148. See *infra* Section III.B.

also refinancing.¹⁴⁹ No court has directly addressed this proposition. Although one payday loan company tried to avail itself of the argument that the NBA loophole indeed applied to refinancing limitations and exempted the company from those state laws,¹⁵⁰ the court did not address the argument.¹⁵¹ Despite the lack of a definitive decision on the issue, the NBA and DIDMCA are unlikely to be found to apply to refinancing for two reasons. First, courts are increasingly recognizing that payday loan companies are not national or out-of-state banks, and should thus not be afforded *any* of the benefits of such entities.¹⁵² The Office of the Comptroller of the Currency agreed, stating that payday loan companies cannot use federal laws designed for national banks to avoid compliance with state regulations.¹⁵³ Second, the language of the NBA and DIDMCA refers only to interest rates; it does not apply to limitations on refinancing.¹⁵⁴ For these reasons, a court would be hard-pressed to justify applying the loopholes to refinancing laws.

While closing these loopholes is not, on its face, a poor suggestion, payday loan critics who call for the removal of the loopholes focus the debate on interest rates and usury laws, rather than on the refinancing problem, and any successful regulation must address payday loan refinancing. Also, as the following Section will show, imposing usury laws on payday lending could actually harm some potential borrowers.

149. See, e.g., Johnson, *supra* note 8, at 125-27.

150. Colo. *et. rel.* Salazar v. ACE Cash Express, Inc., 188 F. Supp. 2d 1282, 1284 (D. Colo. 2002).

151. The court did not specifically rule on whether the NBA and DIDMCA would apply to refinancing as well as interest rates, making clear that the question was irrelevant because the payday loan company was not a national bank. *Id.* at 1285. According to the court, the case was “strictly ... about a non-bank’s violation of state law.” *Id.*

152. See, e.g., *id.*; Terry v. Payday Loan Corp., No. 99 C 2487, 1999 U.S. Dist. LEXIS 16793, at *3 (N.D. Ill. 1999); Mo. Title Loans, Inc. v. City of St. Louis Bd. of Adjustment, 62 S.W.3d 408, 415 (Mo. Ct. App. 2001).

153. See Nicole Duran, *In Brief: OCC Weighs in on Payday Lender Case*, AM. BANKER, Oct. 3, 2001, at 4.

154. The NBA exception allows national banks to charge “interest at the rate allowed by the laws of the State, Territory, or District where the bank is located.” 12 U.S.C. § 85 (2000) (emphasis added). Similarly, the DIDMCA exception allows out-of-state banks to charge “interest at a rate of not more than ... the rate allowed by the laws of the State, territory, or district where the bank is located.” 12 U.S.C. § 1831d(a) (2000) (emphasis added).

B. The Disadvantages of Imposing Stricter Usury Laws

If states enact and enforce usury laws that are as strict as those called for by opponents of the payday loan industry, the amount of payday loan debt would probably be reduced significantly. This effect would not, however, result from lenders beginning to make reasonable loans; instead, it would occur because payday lenders would most likely stop making loans altogether.¹⁵⁵

There are two reasons that usury laws are not the best solution to payday lending problems. First, payday loans are fundamentally different from other types of loans, and should be recognized and treated as such. Payday lending opponents characterize the fee associated with a payday loan in terms of an APR, and then present the resulting figure, which is normally very high, as proof that payday lenders are taking advantage of borrowers.¹⁵⁶ But the small, short-term nature of the payday loan makes the APR seem more oppressive than it actually is. An APR of 391%, which would be a shocking interest rate for a five-year, \$20,000 auto loan, actually amounts to only a one-time payment of \$15 for a \$100 payday loan.¹⁵⁷

If characterized as an APR, almost any fee can be made to appear preposterously high. For example, a \$29 late fee on a \$100 credit card charge, if expressed as an APR, would be 756%; a \$47 late/reconnection fee on a \$100 utility bill would be considered to have a 1225% APR; and even an ATM charge of \$1.44 for a one day withdrawal of \$100 could be thought of as 526% APR.¹⁵⁸ Calculating fees as an APR does not make sense for payday loans, and some states have wisely focused on limiting the cost of the fees as a percentage of the total loan, rather than attempting to limit the APR. This approach makes more sense; most borrowers can more easily calculate and understand the cost of loan if it is characterized as "10% of the amount borrowed" rather than "350% APR."¹⁵⁹

155. See FIN. SERV. CTRS. OF AM., FREEDOM OF CHOICE FOR CONSUMERS: THE TRUTH ABOUT DEFERRED DEPOSIT SERVICES, pt. IV (1999), <http://www.fisca.org/ddresponse.htm>.

156. See, e.g., Bruch, *supra* note 1, at 1279.

157. PAYDAY ADVANCE, *supra* note 54, at 13.

158. *Id.*

159. This Note does not advocate that the APR should be withheld from the borrower. It only points out that opponents of the payday loan industry often use the APR in their attempts to show that payday lending interest and fees are outrageous, when in fact the fees

The second argument against capping interest rates at a low level is that caps would likely eliminate the payday loan industry completely. Although payday lenders face the same costs associated with offering and underwriting loans that lenders of larger amounts face, payday loan companies have higher-risk borrowers.¹⁶⁰ Because of the short time period and high risk of payday loans, the interest rate must be higher than that of other loans so that the industry entrepreneurs can make a profit.¹⁶¹ The truth of this statement is evident from the experience of banks that have attempted to issue small, short-term loans at an APR lower than that of payday lenders; these banks have found such loans unprofitable.¹⁶² According to the industry, in states where laws have been overly restrictive, payday lending has in fact disappeared.¹⁶³

The payday loan industry and its supporters argue that the complete elimination of payday lending is the real goal of consumer protection groups.¹⁶⁴ At least one industry supporter has even gone so far as to allege that those seeking elimination of the industry “are dictating which types of financial services we should use” and thus threaten the “[c]onsumer freedom [that] is the very core of American

alone (ignoring the issue of refinancing) are not a serious problem for most borrowers. *See, e.g.,* Bruch, *supra* note 1, at 1279. In truth, most borrowers probably care little about the APR and are instead concerned with the amount of the fee. *See* Diane Hellwig, Note, *Exposing the Loansharks in Sheep's Clothing: Why Re-regulating the Consumer Credit Market Makes Economic Sense*, 80 NOTRE DAME L. REV. 1567, 1592-93 (2005) (explaining that despite the frequent use of the term APR, “most consumers do not understand the significance of this credit term or even take note of it”). A borrower is better informed by knowing the cost of the fee than by receiving an annual percentage that the majority of borrowers may not understand. *But see* Graves & Peterson, *supra* note 28, at 661-62 (arguing that APR terminology is appropriate because it is “the uniform metric which all mainstream creditors use” for both long- and short-term loans and borrowers, who, data reveals, do not understand APR, would be surprised to know that a 17.5% principal fee is in fact twenty-six times higher than a 17.5% APR; arguing for APR terminology also because the frequency of refinancing belies claims that payday loans are truly short term and therefore do not necessitate APR terminology); Hellwig, *supra*, at 1593 (arguing in favor of using APR because it provides a standard by which borrowers can evaluate their credit options).

160. Tom Lehman, *In Defense of Payday Lending*, FREE MARKET, Sept. 2003, available at http://www.mises.org/freemarket_detail.asp?control=454&sortorder=articledate.

161. *Id.*

162. *See* Mary Wisniewski, *How To Break the Payday Loan Cycle: Look To Educate Borrowers, Build Long-term Customers*, CHI. SUN-TIMES, Apr. 13, 2005, at 72.

163. FIN. SERV. CTRS. OF AM., *supra* note 155, pt. IV (citing Tennessee as a jurisdiction whose laws have eviscerated the deferred-deposit industry).

164. *Id.*

democracy.”¹⁶⁵ This argument is probably an exaggeration; the elimination of the payday loan industry is unlikely to threaten the very core of democracy. Nevertheless, the best way to both regulate a problematic industry and to preserve consumer freedom is rarely, if ever, to simply eliminate the industry, especially if that industry provides a service that is unavailable from other sources.¹⁶⁶ Instead, the ideal resolution is to find a balance in the market that allows payday lending to be conducted responsibly.

Eliminating the payday loan industry is a poor solution not because it threatens democracy, but because doing away with the industry could eliminate the only source of credit available to some financially strapped consumers.¹⁶⁷ The Financial Service Centers of America (FiSCA), one of the trade associations of the payday loan industry, explains why most payday loan customers seek a payday loan instead of other options:

What [industry opponents have] not told the country is that short-term advances for sums of less than \$500.00 are virtually unobtainable throughout the United States through small loan companies for the deferred deposit service customer. These consumers usually do not have cash reserve accounts at banks, credit card advances available or sufficient unencumbered real estate to support home equity loans. Within the realm of lawful financial products, only deferred deposit services can satisfy the consumer's need.¹⁶⁸

Payday lending has seen such a dramatic increase in the past decade because of an absence of other small loan providers in the traditional market.¹⁶⁹ Deregulation has increased competition, prompting most traditional institutions to abandon small, short-

165. Daniel J. Popeo, Chairman, Wash. Legal Found., In All Fairness: Stealing Consumer Choice (Feb. 24, 2003), <http://www.wlf.org/upload/2-24-03ConsumerChoiceslick.pdf>.

166. See Stegman & Faris, *supra* note 7, at 29.

167. Some experimental credit unions have begun to offer payday-type loans, for lower fees and in combination with financial education. See, e.g., Wisniewski, *supra* note 162. Such programs are rare, however, and conventional payday lenders claim to control ninety-nine percent of the market. *Id.*

168. FIN. SERV. CTRS. OF AM., *supra* note 155, pt. IV.

169. Lisa Blaylock Moss, Note, *Modern Day Loan Sharking: Deferred Presentment Transactions & the Need for Regulation*, 51 ALA. L. REV. 1725, 1732 (2000).

term loans as unprofitable.¹⁷⁰ Most retailers have replaced installment plans with credit card sales, limiting the options available to those who do not qualify for credit cards.¹⁷¹ Finance companies have also abandoned small loans in order to switch their focus to home equity financing.¹⁷² Because of these changes, many payday loan borrowers' only credit option is a payday loan.¹⁷³ Payday loan borrowers do have bank accounts, but some are still unable to obtain other sources of traditional credit.¹⁷⁴ As legal commentator Michael Barr has noted, "[w]hile payday loan consumers are not unbanked, they could well be referred to as 'underbanked': They may lack the savings, credit history, or financial know-how to avoid purchasing a high-cost credit instrument."¹⁷⁵ To eliminate the payday loan industry would mean that when "under-banked" individuals face a legitimate emergency, they have no legal access to money.¹⁷⁶

Some legal commentators believe that this reduction in available credit is good for consumers. They argue that "[w]hile reducing the supply of credit may deprive some incapacitated persons of credit, part of the borrowing by the incapacitated is prompted only by temptation, ignorance, or aberration."¹⁷⁷ This line of reasoning implies that most payday loan borrowers want money for unnecessary expenses, or out of foolishness or ignorance. Supporters of strict usury laws thus argue, whether intentionally or unintention-

170. Michael S. Barr, *Banking the Poor*, 21 YALE J. ON REG. 121, 152 (2004); Moss, *supra* note 169, at 1732. One credit union in Chicago, for example, offers a six-month loan of up to \$500 at 16.5% APR, quite low compared to payday loans. Wisniewski, *supra* note 162. The manager admitted that the credit union loses money on the loans. *Id.*

171. Barr, *supra* note 170, at 152.

172. *Id.*

173. *Id.* According to a study funded by the payday loan industry, seventy-three percent of payday borrowers had previously been turned down for traditional credit or not given as much credit as desired, and sixty-eight percent considered applying for other credit but thought they would be turned down. ELLIEHAUSEN & LAWRENCE, *supra* note 17, at 46.

174. Barr, *supra* note 170, at 153.

175. *Id.*

176. See Moss, *supra* note 169, at 1732 ("[A] large number of consumers lack sufficient credit card limits or bank overdraft protection to meet their needs for small unsecured loans.").

177. Morris, *supra* note 123, at 174.

ally, that a limitation on credit is necessary to protect consumers from their own foolishness.¹⁷⁸

The payday loan industry responds that the majority of its borrowers use payday loans for unforeseen circumstances, and not for frivolous purchases.¹⁷⁹ Economists Michael Stegman and Robert Faris, staunch opponents of the industry, conducted a study finding many problems with the payday loan industry. Despite their distaste for the industry, they concluded that the elimination of the payday lending was not in the best interest of consumers:

Although some might argue that the way to deal with abuses discussed in this article is ... to ... ban payday lending outright, we do not agree that this is the best approach. The reality is that decent, hard-working families who end up with too much month left at the end of their money will go underground if necessary to get help.¹⁸⁰

If payday loans are eliminated, borrowers who have a genuine emergency, but no access to other credit, might be forced to obtain illegal, unregulated, less desirable loans.¹⁸¹

One obvious solution to payday lending concerns would be to implement programs that eliminate the need for small, short-term loans. This solution is perfect in theory, but is unperfected in reality. One proposal is the use of individual development accounts, or IDAs. IDAs are matched savings accounts for the poor, funded using both private and public money.¹⁸² The accounts can be used to help buy a house, to receive higher education and training, or to open a small business.¹⁸³ According to proponents, \$600 million from

178. *Id.* (calling usury standards “a paternalistic goal, perhaps, but a legitimate use of paternalism”).

179. According to the Credit Research Center, about two-thirds of payday loan borrowers needed the loan for an emergency or to get through a temporary income reduction. ELLIEHAUSEN & LAWRENCE, *supra* note 17, at 47.

180. Stegman & Faris, *supra* note 7, at 29.

181. *See id.*

182. Ray Boshara, *Individual Development Accounts: Policies To Build Savings and Assets for the Poor*, 32 BROOKINGS INSTITUTION POLICY BRIEF: WELFARE REFORM & BEYOND 1 (2005), available at <http://www.brookings.edu/es/research/projects/wrb/publications/pb/pb32.pdf>.

183. *Id.*

public funds and private donations could, within the next decade, extend IDAs to half a million people.¹⁸⁴

Even if IDAs could be issued to all impoverished Americans, they would still fail to eliminate the need for short-term loans. IDAs are a useful tool to help establish financial independence, but they cannot be used for emergencies such as health care or car repairs.¹⁸⁵ For these expenses, borrowers would still have to look to payday or similar lenders for relief.

There will always be some who need extra cash and are willing to do almost anything necessary to obtain it. It is better to have a regulated payday loan industry that provides the needed funds than to impose strict usury laws that eliminate profitable payday lending and force desperate consumers to turn instead to illegitimate sources.

IV. A BETTER, MORE BALANCED SOLUTION

Many payday lending reformers have called for tighter caps on the interest rate of payday loans.¹⁸⁶ Yet, few borrowers are overwhelmed because of the initial service charge;¹⁸⁷ most financial problems arise when borrowers are forced to refinance and to pay the refinancing fee several times before the loan is paid in full.¹⁸⁸ Even the Center for Responsible Lending, an organization that calls payday lending interest rates “outrageous,” recognizes that multiple refinancing is “the bigger problem.”¹⁸⁹ Only when the loan is refinanced several times do the “triple-digit APRs charged by most payday lenders ... go beyond what is fair and become abusive and predatory.”¹⁹⁰

There are four changes that must be made to the payday loan industry to ensure that borrowers are treated fairly: better assur-

184. *Id.* at 7.

185. *See id.* at 1.

186. *See supra* note 123 and accompanying text; *see also supra* Part III.B.

187. The average fee of one large payday loan provider is only \$53.81 for an average loan (including principal and fee) of \$360.39. *QC Holdings, Inc. Reports Third Quarter Results: 53 Stores Added During the Quarter*, BUSINESS WIRE, Nov. 2, 2005.

188. *See supra* Part II.B.

189. *Hearing, supra* note 74 (written statement of the Center for Responsible Lending), available at http://www.responsiblelending.org/pdfs/Testimony-Graves_payday-032905.pdf.

190. *See Stegman & Faris, supra* note 7, at 20.

ances that borrowers have enough information to make an informed decision, a reduction in the number of times a borrower can refinance, reform of collection techniques, and increased enforcement of regulations.

A. Provide Information

The first step to regulating payday lending is to ensure that borrowers have enough information and shopping freedom to be able to make educated decisions. For payday loan borrowers, some types of information are more valuable than others. The most valuable information is that which helps a borrower make rational choices between options:

Information may be useful [for] borrowers if it informs them of the presence and location of alternative sources of lower cost credit. This kind of information may help these borrowers participate in the bargaining process more fully and effectively if the market has alternatives for them. If the market does not have alternative sources, however, information is relatively unimportant to them. Again, information strategy favors the educated borrower and disfavors the less mobile or educated borrower, like the elderly and the poor.¹⁹¹

Payday lenders sometimes mislead, lie to, or conceal information from borrowers, effectively preventing them from shopping around for better terms and from gaining enough knowledge to make an informed decision.¹⁹² There are three ways lenders make loan shopping difficult for borrowers. First, lenders are often not required to disclose the terms of the contract until immediately before the borrower signs the contract.¹⁹³ Second, lenders can refuse to discuss loan terms until the borrower's employer is called, making borrowers less likely to shop around because of fear that their employer will be called multiple times.¹⁹⁴ Finally, some lenders do not allow

191. Morris, *supra* note 123, at 174-75.

192. See Johnson, *supra* note 8, at 32.

193. *Id.*

194. Christopher L. Peterson, *Truth, Understanding, and High-cost Consumer Credit: The Historical Context of the Truth in Lending Act*, 55 FLA. L. REV. 807, 896 (2003) ("After the first employment verification telephone call, many prospective debtors immediately end their

the borrowers to take the contract from the store or to have a copy of their signed contract even after the loan is made.¹⁹⁵

Payday lending laws must ensure that lenders cannot engage in these practices. Lenders should be required to allow the borrower adequate time and privacy to study the contract terms before agreeing to the loan. Lenders should not be allowed to withhold vital information or to forbid the contract from leaving the store. One piece of information especially important to borrowers is the total cost of the loan's fees.¹⁹⁶ Borrowers care most about the cost of the fee initially charged; they are often unconcerned with, and rarely understand, the APR.¹⁹⁷ In fact, three-fourths of payday loan users acknowledge that they do not know the APR charged in their most recent payday loan transaction.¹⁹⁸ Requiring disclosure of total cost of the loan will mean that borrowers can more easily compare the costs of competing offers. If borrowers have the ability to compare the loans of competing companies, the increased competition could lower costs for borrowers.

The value of information may be limited in some circumstances. In those cases in which all payday loan options are similar and the borrower has no option other than a payday loan, information has little value, because it will not matter which payday loan the borrower chooses. Regardless of the limitation on the value of information in some circumstances, information should still be provided so that borrowers who do have some options can weigh the costs and benefits of their potential choices.

B. Reduce Refinancing

The high "interest" charged by payday loan companies, considered alone, does little harm to the consumer.¹⁹⁹ Few consumers have difficulty paying a one-time fee of about \$15 for every \$100 borrowed. Financial problems do surface, however, when the borrower

search because they ... predict that embarrassment and the risk of jeopardizing their jobs from additional phone calls will outweigh any potential savings from searching for a cheaper loan.").

195. Johnson, *supra* note 8, at 35-36.

196. See Lehman, *supra* note 160.

197. *Id.*

198. See *supra* note 159.

199. See *supra* notes 154-58 and accompanying text.

is forced to pay the fee multiple times before the loan is paid off, especially when relatively large amounts of money are involved.²⁰⁰ The payday loan regulation needed most is not a limitation on the APR, but on refinancing. There are four changes that must be made for the refinancing trap to be eliminated.

First, the amount of time a borrower has to repay a loan must be extended to thirty days in order to give the borrower adequate time to repay the loan.²⁰¹ Second, lenders should be required to accept partial payments.²⁰² The loan should not be declared in default, and no refinancing charge should be made, if the borrower repays at least half of the loan by the time payment is due. The borrower should then be given an additional two weeks to repay the remainder of the loan. These two steps essentially give the borrower six weeks (instead of two) to pay off the entire loan, while ensuring that the lender receives at least half the amount owed during this period. The borrower should be allowed to refinance only once for a thirty-day extension at a cost equal to that of the fee initially charged.

The third change necessary to reduce extensive refinancing is to limit the value of outstanding payday loans a borrower can have at one time.²⁰³ The number of loans at one time should be capped at two, the value of which should not exceed \$500.²⁰⁴ Some payday loan opponents express concern about state laws that allow payday

200. See *supra* Part II.B.

201. See Stegman & Faris, *supra* note 7, at 29.

202. Indiana has allowed for partial payments before the date the loan is due. IND. CODE ANN. § 24-4.5-7-402(3) (West, Westlaw through 2006 2d Reg. Sess.). But this provision does little for the borrower because the borrower still must have the loan paid in full within two weeks. If the due date arrives and the borrower does not have the full amount, he or she still must refinance. The Virginia Senate recently approved a bill that would allow borrowers with three or more consecutive payday loans to repay through the use of an extended payment plan; the plan would allow borrowers to repay the loan over sixty days. S.B. 1014, 2007 Gen. Assemb., Reg. Sess. (Va. 2007). After debate in the House about a seventy-two percent interest-rate ceiling, which critics feared would eliminate the payday loan industry in Virginia, Pamela Stallsmith & Jeff E. Schapiro, *Payday-lending Bill Pulled: House Proposal Would Have Capped Interest Rate at 72%; Senate Bill May Be Pulled Also*, RICHMOND TIMES-DISPATCH, Feb. 8, 2007, at A6, the legislation was passed, in a form very similar to the Senate bill, without any interest rate cap. Amy Gardner, *House Passes Payday Lending Reform Bill Without a Rate Cap*, WASH. POST, Feb. 17, 2007, at B3.

203. See, e.g., IND. CODE ANN. § 24-4.5-7-404 (West, Westlaw through 2006 2d Reg. Sess.); S.B. 1014, 2007 Gen. Assemb., Reg. Sess. (Va. 2007).

204. Five hundred dollars is roughly twenty-five percent of the average monthly salary of a payday loan borrower. See *supra* notes 36-40.

lenders to avoid refinancing restrictions with the “touch and go” strategy, issuing a second loan to a borrower to pay off a first one, as long as the amount of the loan does not exceed that allowed by statute.²⁰⁵ This practice is a problem because a borrower may use the second loan to pay off the first, take a third loan to pay off the second, and so on ad infinitum. To eliminate this “touch-and-go” lending, after a second loan within the \$500 limit, a payday lender should not be allowed to make a new loan until seven days after both the loans have been paid in full.²⁰⁶

Finally, payday loans should not exceed a certain percentage of the borrower’s income. Indiana prohibits a payday lender from making a loan if the “total payable amount of the ... loan exceeds fifteen percent (15%) of the borrower’s monthly gross income” as shown by the paycheck stub the lender already requires.²⁰⁷ By limiting the loan according to the borrower’s income, lenders will be less likely to issue a loan that exceeds the borrower’s ability to repay.

If refinancing has resulted in such a large portion of payday lenders’ business,²⁰⁸ these regulations may cut into the industry’s profits. They would not, however, eliminate profit completely, as would usury laws.²⁰⁹ The reduction in profits could be offset by two potential benefits. First, a large portion of payday loans currently end in default.²¹⁰ By discouraging practices that encourage default, such as excessive refinancing, the regulations this Note proposes would ensure that a borrower could more easily repay loans and would be less likely to default.²¹¹ Second, these changes will give payday lending a greater appearance of validity, and more people will be willing to turn to a payday loan as a legitimate credit option.

205. See, e.g., Johnson, *supra* note 8, at 65-66.

206. Proposed legislation in Virginia would prevent a payday lender from issuing a loan to a borrower on the same day that the borrower repays a previous loan. S.B. 1014, 2007 Gen. Assemb., Reg. Sess. (Va. 2007).

207. IND. CODE ANN. § 24-4.5-7-402 (West, Westlaw through 2006 2d Reg. Sess.).

208. See *supra* Part II.B.

209. See *supra* Part III.B.

210. See Bruch, *supra* note 1, at 1272.

211. See Tia Martarella, *Crimes and Offenses*, 21 GA. ST. U. L. REV. 59, 60 (2004) (discussing the difficulty of getting out of a cycle of refinancing debt).

C. Forbid Dubious Collection Methods

A few states have recently enacted legislation that specifically forbids the use of bad check laws in payday loan collection.²¹² This is a much needed start, but simply forbidding the use of bad check laws is insufficient. If the borrower is unaware of the law, the payday loan company can use the threat of bad check laws in order to encourage the borrower to pay back the loan, regardless of the fact that such threats cannot be enforced.²¹³ To ensure that lenders cannot threaten the use of bad check laws, a means must be created by which borrowers will be aware of their rights.

One way to ensure that borrowers are aware that payday lenders cannot use bad check laws in the case of default is to require borrowers to read and sign a disclosure statement specifying that bad check laws do not apply to their loans.²¹⁴ The disclosure statement should make the borrower aware that the payday loan company can use neither criminal nor civil bad check laws to pursue repayment. To ensure that this disclosure statement is given, a payday lender should not be allowed to sue a borrower in the case of default unless the lender attaches the signed disclosure statement to the complaint. This creates an advantage over laws requiring a posted notice. Currently, officers and state employees cannot ensure that laws demanding a posted notice are followed without visiting the payday loan stores to see that the notice is posted as required. By requiring, instead, that lenders have a signed disclosure statement before bringing suit against a borrower, the regulation would be self-enforcing; compliance with the statute would be in lenders' best interest, so the lenders themselves would make certain that the requirement was met. Self-interest would regulate without burdening state resources.

212. *See, e.g.*, ARIZ. REV. STAT. ANN. § 6-1260 (West, Westlaw through 2006 2d Reg. Sess.); DEL. CODE ANN. tit. 6, § 1301A (2005).

213. *See supra* notes 119-20.

214. Some borrowers may sign the notice without reading or fully understanding its content. By requiring the disclosure to be written in simple, conspicuous language, this possibility could be limited.

D. Provide Adequate Enforcement

Although many states have enacted payday loan regulations, enforcement has been difficult.²¹⁵ After an empirical study of payday loan companies in twenty states, Steven Graves and Christopher Peterson were forced to declare that “[l]iterally thousands of payday lenders around the country openly and systematically ignore state consumer protection laws.... [N]o industry with which we are familiar, with the possible exception of the illegal narcotics business, so openly ignores the law.”²¹⁶ For example, borrowers may obtain loans from several different stores or use a loan from one store to pay off a loan from another store.²¹⁷ The best way to ensure that payday loan regulations are followed is to provide incentives for payday lenders to know and follow the law.

As previously discussed, borrowers should be indebted to only one payday lender at a time for no more than \$500. One proposal for ensuring that lenders know whether a borrower has outstanding loans from another payday loan company is to create a state-wide database that the lender must check before issuing a loan. Florida has recently created such a database.²¹⁸ Payday lenders in Florida are required to submit personal information, such as the borrower's name, address, driver's license number, the amount of the transaction, and the date of the transaction, into the Internet-accessible database, which is available only to Florida payday lenders.²¹⁹

Instituting a system similar to that of Florida would not be prohibitively costly.²²⁰ Many lenders already use tracking technology in their risk management system, and this could be incorporated into a state-wide database that lenders could check to see whether the borrower has taken out a loan from another company within the

215. See Graves & Peterson, *supra* note 28, at 827.

216. *Id.*

217. Drysdale & Keest, *supra* note 2, at 601.

218. FLA. STAT. ANN. § 560.404(23) (West Supp. 2006). Proposed Virginia legislation would create a similar, Internet-based system in Virginia. S.B. 1014, 2007 Gen. Assemb., Reg. Sess. (Va. 2007).

219. *Id.*; see also Graves & Peterson, *supra* note 28, at 740-41.

220. Florida covers the cost by imposing a one dollar fee per transaction. FLA. STAT. ANN. § 560.404(23) (West Supp. 2006). Pending Virginia legislation proposes paying for a similar system by allowing lenders to charge borrowers a fee of fifty cents. S.B. 1014, 2007 (Gen. Assemb., Reg. Sess. (Va. 2007).

previous seven days.²²¹ If proper incentives are provided for the lender to use the system and stay within the regulation, the state would be required to provide little enforcement.

Much like with the proposed bad check law regulation, the lender should be barred from filing a suit to collect a payday loan debt unless the lender shows proof that the loan was filed in the system, did not exceed either the \$500 cap or fifteen percent of the borrower's gross income, and was issued at least seven days after all other payday loans were repaid (or, in the alternative, that the customer signed a statement attesting that the loan does not exceed the limitations). Self interest would then ensure that lenders would stay within the regulation.

Such a system would not be perfect. Some borrowers may receive loans from an unregistered lender or use the Internet to obtain loans from other states that would not show up in the state system.²²² Further, some consumers may have privacy concerns, although such a system seems little different from traditional credit reporting systems, especially because only payday lenders would have access. Despite these concerns, Florida has shown that the database works. Since its implementation, instances of consumers having multiple outstanding payday loans have decreased by eighty-two percent.²²³

CONCLUSION

The payday loan industry must be regulated. Too many borrowers are forced to refinance loans until they have paid thousands of dollars for a loan of a few hundred dollars. Too many borrowers are threatened with lawsuits or criminal charges when they are unable to repay their loans. Too many payday lenders have sought to avoid regulation by creatively circumventing, or simply ignoring, the law.

Contrary to the arguments of many legal commentators, however, imposing strict usury laws on lenders is not the most effective means of resolving these problems. First, efforts in the past have been skirted by payday lenders who have paired up with national banks. Second, enforcing low interest rates could cause the industry

221. Stegman & Faris, *supra* note 7, at 29.

222. Graves & Peterson, *supra* note 28, at 741.

223. *Id.* at 740-41.

to disappear completely and eliminate the only means of credit available to some borrowers.

The best regulations would not risk the elimination of the payday loan industry. The best answer for payday lending problems is to focus on providing information to borrowers, reducing refinancing, protecting borrowers from unfair collection practices, and enforcing regulations. If these changes are made, borrowers will remain able to take advantage of a useful service, and yet be protected from abuse. If these changes are made, Allan Jones's revitalization of the payday loan industry can be preserved in a manner that satisfies both borrowers and lenders.

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* The author wishes to thank his wife, Tricia, for her constant support and advice during the process of writing this Note. The author also wishes to thank his parents, who instilled in him a love of learning by reading to him when he was a child. Finally, the author is grateful to the staff of the *William and Mary Law Review*, whose suggestions and corrections made this Note incalculably better.