University of the Pacific Law Review

Volume 52
Issue 1 *Fifteenth Annual International Conference on Contracts*

Article 14

1-1-2020

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Recommended Citation

Lauren Hirota, *Tomayto, Tomahto: The Cunning New Face of Payday Lending*, 52 U. PAC. L. REV. 185 (2020).

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Tomayto, Tomahto: The Cunning New Face of Payday Lending

Lauren Hirota*

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I. INTRODUCTION

Need to take your girlfriend to the movies but tight on cash? Got a baby who doesn't wait until payday? Forgot to buy a wedding gift for your bridezilla sister? Don't wait for pay day—download a wage-advance app and get your hard-earned money instantly with no fees, interest, or credit check required.[1]

Think it's too good to be true?[2] You're probably right.[3]

In recent years, the Federal Trade Commission ("FTC") has cracked down on

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* J.D. Candidate, University of the Pacific, McGeorge School of Law, to be conferred May 2021; B.A., Philosophy and Political Science, San Diego State University, 2018. I would like to thank Distinguished Professor Michael P. Malloy for his continued support, guidance, and review of my Comment throughout this extensive process. I would also like to thank the Board of Directors and editorial staff for their commitment and hard work in making this volume a success. Lastly, I would like to dedicate this Comment to my family, for instilling in me a healthy sense of frugality and resourcefulness, but never allowing me to compromise on the price of my dreams.

1. Earnin App, *Earnin TV Commercial, 'Movie* Tickets', ISPOT.TV, https://www.ispot.tv/ad/dpIE/earnin-movie-tickets (last visited Oct. 25, 2019) (on file with the *University of the Pacific Law Review*).

2. *See* Cyrus Farivar, *Millions Use Earnin to Get Cash Before Payday. Critics Say the App is Taking Advantage of Them*, NBC UNIVERSAL (July 26, 2019, 1:41 AM) https://www.nbcnews.com/tech/internet/millions-use-earnin-get-cash-payday-critics-say-app-taking-n1034071 (on file with the *University of the Pacific Law Review*) ("They just portray it as being so simply and so easy.").

3. *See id.* (discussing the sneaky business practices of tip-based wage-advance companies).

the ruthless business practices of the payday lending industry.[4] And with the news of a $1.27 billion judgment against AMG Capital Management for deceptive lending practices, the Ninth Circuit cemented its broad support for the FTC's recent crusade.[5] But as the confetti settles over the FTC's most recent win against payday lenders, a new and unregulated industry emerges in the financial market.[6]

Wage-advance businesses are attracting a young, strapped-for-cash crowd through the use of smartphone applications ("apps") that offer "no strings attached" paycheck advances.[7] Companies like Earnin use catchy commercials featuring everyday people short on cash to show the ease and expedience of the app's use.[8] Seeking to distinguish themselves from traditional short-term, high-fee payday loans, the wage-advance apps call money transfers "activations" instead of "loans" and claim to offer the money without interest rates or fees.[9] The only catch: a noncompulsory tip, defaulted to ten percent of the amount borrowed.[10] Easy, right?[11] Wrong.[12]

On closer scrutiny, a five dollar tip on a four day advance of $100 equals an annual percentage rate ("APR") of 456%.[13] One man praised the Earnin app online, stating he would regularly tip $30–$35 for every $500 he received.[14]

4. *See* FTC v. AMG Capital Mgmt., LLC, 910 F.3d 417, 426 (9th Cir. 2018), *cert. granted*, No. 19-508, 2020 WL 3865250 (July 9, 2020) (holding AMG Management Capital liable for deceptive business practices regarding the terms of their payday loans); *see also* Julia Kagan, *Payday Loan Definition*, INVESTOPEDIA (July 15, 2019) https://www.investopedia.com/terms/p/payday-loans.asp (on file with the *University of the Pacific Law Review*) (defining a payday loan as "a type of short-term borrowing where a lender will extend high-interest credit based on a borrower's income and credible profile.").

5. *See* AMG Capital Mgmt., LLC, 910 F.3d at 426 (holding AMG Management Capital liable for deceptive business practices regarding the terms of their payday loans).

6. *See generally id.* at 426 (ruling in favor of the FTC regarding the deceptive business practices of the payday lending company, AMG Management Capital).

7. Gaby Del Valle, *How a Silicon Valley Startup is Trying to Rebrand Payday Loans*, VOX (May 22, 2019, 4:50 PM), https://www.vox.com/the-goods/2019/5/22/18636049/earnin-app-startup-payday-loans-fintech (on file with the *University of the Pacific Law Review*); *see Earnin TV Commercial, 'Movie* Tickets', *supra* note 1 (advertising the Earnin app through iPhone-esc videos of young people who use the app to receive advances on their paycheck); *see also* Stephen Middlebrook, *What Business Lawyers Should Know About Wage Advance Products*, ABA (Sept. 5, 2019), https://www.americanbar.org/groups/business_law/publications/blt/2019/09/wage-advance/ (on file with the *University of the Pacific Law Review*) (defining wage-advances as businesses that provides borrowers with instant access to earned wages, due back on receipt of payday).

8. *Earnin TV Commercial, 'Movie* Tickets', *supra* note 1.

9. Farivar, *supra* note 2.

10. *Id*.

11. *See id.* ("They just portray it as being so simply and so easy.").

12. *Id.* (discussing the sneaky business practices of tip-based wage-advance companies).

13. *See generally* Adam Hayes, *Annual Percentage Rate (APR)*, INVESTOPEDIA (Jul 15, 2019), https://www.investopedia.com/terms/a/apr.asp (on file with the *University of the Pacific Law Review*) (defining an annual percentage rate as "the annual rate charged for borrowing or earned through an investment."); Farivar, *supra* note 2.

14. @IAcewingI, REDDIT (January 31, 2019, 8:42 PM), https://www.reddit.com/r/IsItBullshit/comments/9xzn14/isitbullshit_the_earnin_app/ (on file with the *University of the Pacific Law Review*).

Another reviewer commented on the post, warning that such a tip equals a 156% APR.[15] Missouri State Senator, Jill Schupp, opined, "[t]o use the word 'tip' instead of a usury charge, an interest rate or a fee, it's just semantics. It's the same thing at the end of the day."[16]

Other smartphone apps—such as Dave—operate through a small monthly fee to use their services, ranging from $1–29.[17] But on a $100 loan, a ten dollar monthly fee could equal a 117.7% APR.[18] While each wage-advance company's model is different, they all have one thing in common: skirting federal and state payday lending and banking laws.[19]

Wage-advance apps are payday lenders in disguise, charging "tips" or "fees" in place of the traditional interest rate.[20] Such companies enjoy the benefits of covert, inflated interest rates without the burden of state and federal oversight placed on the payday lenders with whom they compete.[21] In states that highly regulate short-term lending, these tipping schemes constitute "deceptive business practices" under the Federal Trade Commission Act ("FTCA").[22] This Comment argues that both state and federal governments should treat wage-advance businesses and payday lenders uniformly and implement stronger standards for both industries through FTC litigation, rules akin to those of the original Bureau of Consumer Financial Protection ("CFPB") 2017 Rules, and stricter state laws criminalizing the fraudulent conduct of loan sharks.[23]

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15. @myerbrigg, REDDIT (February 25, 2019, 10:34 PM), https://www.reddit.com/r/IsItBullshit/comments/9xzn14/isitbullshit_the_earnin_app/ (on file with the *University of the Pacific Law Review*).

16. Farivar, *supra* note 2.

17. Anna Serio, *5 Pay Advance Apps Like Earnin*, FINDER (May 20, 2019), https://www.finder.com/pay-advance-apps-like-earnin (on file with the *University of the Pacific Law Review*).

18. *How Do Payday Loans Work?* IN CHARGE DEBT SOLUTION, https://www.incharge.org/debt-relief/how-payday-loans-work/ (last visited on Oct. 27, 2019) (on file with the *University of the Pacific Law Review*) (explaining how an APR on a payday loan is calculated by dividing the amount of interest paid [here, $10] by the amount borrowed [here, $100], multiplying that by 365, then dividing that number by the length of the repayment term [here, around 31 days], and finally multiplying that by 100 [totaling an APR of 117.7%]).

19. Farivar, *supra* note 2.

20. *See id*. (asserting that wage-advance companies are virtually acting as a payday lender).

21. *See id.* (noting that wage-advance apps do not have to conform to conventional lending regulations due to their lack of a traditional interest rate or debt collectors when customers fail to pay).

22. *See, e.g., PayDay Loan Consumer Information*, CONSUMER FED'N OF AM., https://paydayloaninfo.org/state-information (last visited Mar. 6, 2020), (on file with the *University of the Pacific Law Review*) (discussing the various states, including New York and Arkansas, that protect their constituents from payday lending by limiting or completely prohibiting the industry); *see generally* AMG Capital Mgmt., LLC, 910 F.3d at 426 (ruling in favor of the FTC regarding the deceptive business practices of the payday lending company, AMG Management Capital).

23. *See generally* AMG Capital Mgmt., LLC, 910 F.3d at 426 (ruling in favor of the FTC regarding the deceptive business practices of the payday lending company, AMG Management Capital); *see also* Jim Puzzanghera, *Consumer Protection Bureau Cracks Down on Payday Lender with Tough Nationwide Regulations*, LOS ANGELES TIMES (Oct. 5, 2017, 3:40 PM), https://www.latimes.com/business/la-fi-payday-loan-regulations-20171005-story.html (on file with the *University of the Pacific Law Review*) (discussing new rules for payday lenders introduced by the Consumer Financial Protection Bureau in 2017).

To that end, this Comment proceeds in four parts.[24] Part II introduces payday lending and wage-advance practices and highlights the similarities and differences between the two industries.[25] Part II then argues that because the two industries operate through identical structures, the government should regulate them similarly.[26] Part III addresses states' current inability to regulate payday lenders effectively, as well as the federal government's past and present struggles to regulate the industry.[27] Part IV proposes various regulations that federal and state governments should implement to guard against the abuse and limit the discretion from which the wage-advance and payday lending industries currently benefit.[28]

II. The Payday Lending & Wage-Advance Industries

Angela Garcia frantically grabbed her toddler's car seat as a tow-truck hauled away her Chevy Suburban.[29] The cost of her only mode of transportation was a defaulted $3,200 loan from Loan Mart.[30] With Christmas fast approaching, the single mother of six needed a little extra cash to get her through the holidays and pay her monthly bills.[31] Garcia took out a loan, and, like clockwork, she threw hundreds of dollars at the loan each month.[32] Despite her religious monthly repayments, Garcia was unaware of the loan's high percentage rate and—like many Americans—found herself even more hopeless than when she took out the loan.[33]

Angela's story is not uncommon.[34] One study found that 87% of Oklahoma payday lendees borrowed money more than once within a year.[35] Of those borrowers, 59% opened a new payday loan the same day they repaid the previous loan.[36] Another study found that, on average, 37% of borrowers defaulted within

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24. *Infra* Parts II, III, IV.

25. *Infra* Part II.

26. *Infra* Part II.

27. *Infra* Part III.

28. *Infra* Part IV.

29. CalMatters, *As More Californians Borrow at Triple-Digit Interest Rates, Will the State Crack Down on 'Predatory Lending'?*, THE OCR (May 15, 2019), https://www.ocregister.com/2019/05/15/as-more-californians-borrow-at-triple-digit-interest-rates-will-the-state-crack-down-on-predatory-lending/ (on file with the *University of the Pacific Law Review*).

30. *Id.*

31. *Id.*

32. *Id.*

33. *Id.*

34. *See* Uriah King & Leslie Parrish, *Payday Loans, Inc.: Short on Credit, Long on Debt*, CENTER FOR RESPONSIBLE LENDING 5 (Mar. 31, 2011) *available at* https://www.responsiblelending.org/payday-lending/research-analysis/payday-loan-inc.pdf (on file with the *University of the Pacific Law Review*) (laying out the various data concerning the inability for payday lendees to repay their loans).

35. *Id.*

36. *Id.*

the first year of lending and 44% within their first two years.[37] These reports signify a pattern of borrowers' continuous indebtedness due to their inability to fulfill other financial responsibilities while in repayment of a payday loan.[38]

Section A discusses the mechanics of the payday lending industry and the various political views underlying the industry's continued propriety.[39] Section B introduces the wage-advance industry and the model under which it purports to function separate from the payday lending framework.[40] Finally, Section C compares the two industries and argues the government should treat them indistinguishably when it comes to regulation.[41]

A. Payday Lending

"Quick and easy" payday loans wreak havoc on struggling Americans every day.[42] The payday lending industry offers high-interest, short-term loans to consumers with damaged credit history, providing loan access to patrons that traditional banks deny.[43] Historically, payday lenders target unqualified borrowers that cannot repay on time, resulting in an extension of the loans and trapping borrowers in a cycle of insolvency.[44]

Due to the risky nature of the payday lending industry, lenders also charge borrowers extremely high interest rates.[45] In some states, annual interest rates may reach as high as 500%.[46] Additionally, if a borrower cannot repay his debts, payday lenders employ debt collectors to engage in ruthless and aggressive conduct to recover the money.[47]

Shortly after its inception in the early 1990s, the payday lending industry expanded to encompass over 10,000 lenders throughout the United States.[48] Today, that number has nearly doubled to over 20,000 storefronts across the

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37. Susanna Montezemolo, *Payday Lending Abuses and Predatory Practices*, CENTER FOR RESPONSIBLE LENDING 6 (Sept. 2013) *available at* https://www.responsiblelending.org/state-of-lending/reports/10-Payday-Loans.pdf (on file with the *University of the Pacific Law Review*); King & Parrish, *supra* note 34.

38. King & Parrish, *supra* note 34.

39. *Infra* Section II.A.

40. *Infra* Section II.B.

41. *Infra* Section II.C.

42. *See* Ethan D. Trotz, *Using a Shotgun to Kill a Fly: Issues with the CFPB's Payday Lending Proposal and the Need to Incentivize Banks to Enter the Marketplace*, 21 N.C. Banking Inst. 327, 329 (2017) (on file with the *University of the Pacific Law Review*) (discussing frequent payday lending practice to target low-income individuals with little ability to pay back, ending them into a cycle of insolvency).

43. Ronald J. Mann & Jim Hawkins, *Just Until Payday*, 54 UCLA L. REV. 855, 857 (2007) (on file with the *University of the Pacific Law Review*).

44. Trotz, *supra* note 42, at 328–29.

45. Kagan, *supra* note 4.

46. *See, e.g.*, *id.* (illuminating how California allows for an APR of 459% off a 14-day, $100 loan).

47. Trotz, *supra* note 42, at 329.

48. *See* Michael Bertics, *Fixing Payday Lending: The Potential of Greater Bank Involvement*, 9 N.C. Banking Inst. 133, 136 (2005) (on file with the *University of the Pacific Law Review*) (asserting that more than 10,000 payday lenders operated within the US by 2000).

nation.[49] Despite the risky nature of the business, payday lenders generate $2 billion in revenue a year from the over sixty-five million loans distributed annually, as well as from loan extension rollover fees.[50]

Such rapid expansion and wide use of the industry's services raises questions over its largely controversial and unsavory public perception.[51] Opponents of payday lending suggest the industry's practices trap already vulnerable subsets of the community into further debt.[52] Although payday lenders laud themselves as an emergency service—only providing loans to borrowers for "unexpected expenses"—the reality of payday lending tells a different story.[53] Of first-time borrowers, 69% used payday loans for utilities, credit card bills, food, and other recurring expenses, while only 16% used the loan for nonrecurring, unforeseen expenses.[54]

Abbye Atkinson suggests that for credit (e.g., payday loans) to operate effectively, lenders must only extend loans on terms that enhance the borrower's situation.[55] If not, the borrower will remain insolvent and the debt will be just as difficult, if not more difficult, to repay than when the lender offered the loan.[56] Atkinson asserts, "[The] notion of credit as a social provision for the working poor is deeply flawed. . . . [F]or credit to be 'productive,' the resulting debt must be 'repaid by a much richer borrower to whom that amount of debt is worth less.'"[57] For many Americans who utilize payday lending services, this is not the case.[58]

Conversely, proponents of the industry argue that payday loans fill an essential gap in the market: providing access to money for those denied by traditional banks.[59] With more locations in the United States than McDonald's, supporters applaud the expediency, convenience, and availability of payday services.[60] Legislators opposed to payday lending regulations argue that prohibiting access to loans would constitute unwarranted government interference with an important sector of the financial market.[61] To refute claims

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49. PEW CHARITABLE TRS., *Payday Lending in America: Who Borrows, Where They Borrow, and Why* 2 (2012), https://perma.cc/X3MD-2PBQ [hereinafter *Payday Lending in America*] (on file with the *University of the Pacific Law Review*).

50. Bertics, *supra* note 48, at 136.

51. Abbye Atkinson, *Rethinking Credit as Social Provision*, 71 STAN. L. REV. 1093, 1107 (2019) (on file with the *University of the Pacific Law Review*).

52. *Id.*

53. *Id.*

54. *Payday Lending in America*, *supra* note 49.

55. Atkinson, *supra* note 51, at 1099.

56. *Id.*

57. *Id.* at 1098–99 (quoting MONICA PRASAD, THE LAND OF TOO MUCH: AMERICAN ABUNDANCE AND THE PARADOX OF POVERTY 239 (2012)).

58. *Id.*

59. *Id.* at 1105.

60. Trotz, *supra* note 42, at 327.

61. Aimee A. Minnich, *Rational Regulation of Payday Lending*, 16 KAN. J.L. & PUB. POL'Y 84, 88

that payday lenders take advantage of vulnerable communities, payday lending advocates point to data suggesting that 94% of payday borrowers have high school diplomas, while 54% have obtained their college degree or attended some college.[62] The data expounded also asserts that *all* payday loan users possess checking accounts and that over half of lenders earn incomes over the national average.[63] These figures convey a stark contrast to the story propounded by opponents of the industry.[64] The educational and income-levels of lenders embrace a conclusion that lenders are well-informed and understand the repercussions of taking out a payday loan.[65] To proponents, these figures bolster the conviction that regulation of the payday lending industry only hinders a consumer's right to choose.[66]

Debate continues over the proper balance between consumer choice and consumer protection.[67] Ultimately, the court of public opinion supports a conclusion that regulation of payday lending is a social necessity.[68] Representative Carolyn Maloney argued vehemently that legislation embracing consumer choice, rather than consumer protection, "goug[es] low-income consumers with outrageous interest rates."[69] While lending in and of itself may not pose explicit issues for consumers, the predatory practices associated with high-interest lending highlights the ultimate issue and need for stronger regulations.[70]

B. Wage-Advance Industry

In contrast to the payday lending industry, the wage-advance business has a less checkered and controversial past.[71] In 2017, Walmart became one of the

(2006) (on file with the *University of the Pacific Law Review*).

62. *Id.*

63. *Id.*

64. *Compare id.* (discussing the high educational and economic standing of payday lendees), *with* Atkinson, *supra* note 51, at 1107 (analyzing the negative impacts of payday loans on impoverished sectors of the community).

65. Minnich, *supra* note 61, at 88.

66. *Id.*

67. *See* Paris Ward, *Your Rundown of the CFPB's Payday Lending Rule: What It Means for You*, CREDIT KARMA (Apr. 26, 2019), https://www.creditkarma.com/insights/i/rundown-payday-lending-rule-cfpb/ (on file with the *University of the Pacific Law Review*) (outlining the continuous debate regarding the CFPB 2017 Rules and the proper balance between consumer protection versus consumer choice).

68. *See* Atkinson, *supra* note 51, at 1107 (arguing that credit, such as payday lending, as a social provision for low-income Americans is a faulty notion).

69. 164 CONG. REC. H1151 (daily ed. Feb. 14, 2018) (statement of Rep. Maloney) (discussing H.R. 3299, which would allow national bank high-interest rate loans to stay attached to loans "rented" to secondary markets).

70. *Id.* (statement of Rep. Waters) (arguing H.R. 3299 would open consumers up to a variety of abuses state usury laws attempt to prevent).

71. *See* Michael Corkery, *Walmart Will Let Its 1.4 Million Workers Take Their Pay Before Payday*, N.Y. TIMES (Dec. 13, 2017), https://www.nytimes.com/2017/12/13/business/walmart-workers-pay-advances.html (on file with the *University of the Pacific Law Review*) (introducing the employer-integrated wage advance

largest and most prominent companies to offer a wage-advance service to its employees.[72] The wage-advance application, called Even, allowed employees access to their money before payday for days already worked.[73] The application further assisted employees in managing their money to make smarter financial decisions.[74] Previously skeptical Walmart employee, Alexis Adderley, commended the application's utility and ability to calculate—by examining her bank account and her various reoccurring monthly expenses—the amount of money necessary to access before payday.[75]

Wage-advance applications come in two forms: direct-to-consumer and employer-integrated applications.[76] The latter encompasses programs such as Walmart's Even application and work by marketing to employers to provide wage-advances directly to their employees.[77] Direct-to-consumer applications work with the employee, independent from the employer, by deducting the agreed upon amount from the lendee's bank account on payday.[78] While both models effectively allow employees early access to wages, skeptics argue the only appropriate form of wage-advance is employer-integrated.[79]

Employer-integrated applications often subsist through fees the employer pays, leaving the employee to use its services at a reduced rate or even free of charge.[80] The financial tools and assistance employer-integrated applications provide go further than other applications to help the employee make smarter financial decisions.[81] Associate Director of the National Consumer Law Center, Lauren Saunders, asserted, "[t]rue early wage access providers are companies that have agreements with the employer and are integrated with payroll and are not making loans and seeking repayment from the customer."[82]

In addition to the distinction between direct-to-consumer and employer-integrated applications, wage-advance models also differ in the type of fee they

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application to help Walmart employees).

72. *Id.*

73. *Id.*

74. *Id.*

75. *Id.*

76. Middlebrook, *supra* note 7.

77. *Id.*; Michael Corkery, *Walmart Will Let Its 1.4 Million Workers Take Their Pay Before Payday*, N.Y. TIMES (Dec. 13, 2017), https://www.nytimes.com/2017/12/13/business/walmart-workers-pay-advances.html (on file with the *University of the Pacific Law Review*).

78. Middlebrook, *supra* note 7.

79. Penny Crosman, *A Payday Lender in Disguise? New York Investigates the Earnin App*, AM. BANKER (Apr. 3, 2019), https://www.americanbanker.com/news/a-payday-lender-in-disguise-new-york-investigates-the-earnin-app (on file with the *University of the Pacific Law Review*); Stephen Middlebrook, *What Business Lawyers Should Know About Wage Advance Products*, A.B.A. (Sept. 5, 2019), https://www.americanbar.org/groups/business_law/publications/blt/2019/09/wage-advance/ (on file with the *University of the Pacific Law Review*).

80. Middlebrook, *supra* note 7.

81. *Id.*

82. Crosman, *supra* note 79.

charge to use their services.[83] Some wage-advance applications operate on a monthly participation fee, while others employ a fee per transaction.[84] Other wage-advance businesses, however, claim to operate without any fees at all.[85] Companies, such as Earnin, instead request the borrower's consent to a noncompulsory tip, which defaults to 10% of the cash withdrawn.[86] Earnin, however, labels money transfers as "activations" and claims it does not engage in debt collection if the borrower is unable to repay.[87]

C. Comparing the Two Industries

Despite the illegality or severe restriction of payday lending in 16 states, wage-advance businesses continue to function unencumbered federally.[88] The industry argues it falls outside of the restrictions placed on payday lenders because it does not consider itself a lending industry.[89] Employer-integrated wage-advance businesses maintain their model relies on payroll *deductions* rather than *extensions* of credit to users.[90] Therefore, these companies argue they are exempt from usury and lending laws because they subtract the advanced cash before the deposit of the worker's paycheck, rather than debiting a borrower's account.[91] This reasoning may be compelling.[92] The Consumer Financial Protection Bureau ("CFPB") conceded that employer-employee based forms of wage-advances might be exempt from federal lending laws due to the nature of their services.[93] However, with the postponement of the CFPB's lending rule, questions remain over the definitive parameters of wage-advance businesses' federal exemption.[94]

While employee-integrated wage-advances may avoid federal usury regulations, the CFPB lending rules will likely still encompass direct-to-consumer wage-advance businesses.[95] The direct-to-consumer wage-advance

83. Middlebrook, *supra* note 7; *see* Farivar, *supra* note 2 (discussing the various tipping schemes wage advance apps use, such as "fees," "tips," etc.).

84. Middlebrook, *supra* note 7; Farivar, *supra* note 2.

85. Farivar, *supra* note 2.

86. *Id.*

87. *Id.*

88. *See PayDay Loan Consumer Information*, *supra* note 22 (Outlining the various states prohibiting or restricting payday lending including Georgia, New York, New Jersey, Arkansas, New Hampshire, South Dakota, Arizona, North Carolina, Connecticut, Maryland, Massachusetts, Pennsylvania, Vermont, West Virginia, and the District Columbia).

89. *See* Farivar, *supra* note 2 (relaying the CEO of Earnin's belief that they are not subject to the 2017 federal rules on payday lenders proposed by the CFPB or the Truth in Lending Act of 1968).

90. Middlebrook, *supra* note 7.

91. *Id.*

92. *Id.*

93. *Id.*

94. *Id.;* Ward, *supra* note 67 (outlining the continuous debate regarding the viability of the CFPB 2017 Rules and resulting in the postponement the Rules' enactment).

95. *See* Farivar, *supra* note 2 (discussing the direct access wage-advance business model and how there

model, which operates through direct access to the lendee's bank account, presents problems outside the employer-integrated context.[96] Overdrawn accounts due to insufficient funds, a lack of financial tools in addition to the lending service, and the absence of a responsible intermediary—such as an employer—highlight just a few of these issues.[97]

For example, the Better Business Bureau's website contains hundreds of complaints from customers who use direct-to-consumer applications, such as Earnin.[98] Consumers predominantly reported suffering bank overdraft fees after wage-advance businesses attempted multiple withdrawals from empty bank accounts.[99] While Earnin assures it will reimburse such fees, other customers complain about the inability to contact the company to do so.[100]

The most infamous issue surrounding the direct-to-consumer wage-advance model is the noncompulsory tip or monthly fee associated with using the application.[101] While the employer-integrated applications often offer additional financial services on top of wage-advancement (which may justify the inclusion of a fee) or allow employers to absorb the fee associated with using the system, direct-to-consumer models lack both of these benefits.[102] Additionally, while the tip is purportedly noncompulsory, internal analytics from Earnin suggest that around 80% of consumers tip; and choosing not to tip can lower the amount of cash a consumer may withdraw.[103]

Wage-advance companies contend, however, that their services are notably dissimilar to payday lending because they do not extend "credit" and do not bring legal actions against customers who are unable to repay.[104] Earnin prefers to consider its service a "nonrecourse liquidity product" instead of a lending service.[105] Notwithstanding the progressive name attempting to distinguish the industry, the wage-advance business will fail to make such a meaningful distinction in the courts.[106]

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is little different between its model and those of payday lenders).

96. Middlebrook, *supra* note 7.

97. *See* Complaints About Earnin, BETTER BUS. BUREAU, https://www.bbb.org/us/ca/palo-alto/profile/mobile-apps/earnin-1216-642613/complaints (on file with the *University of the Pacific Law Review*) (displaying user complaints regarding payday lenders over-drafting accounts); *see also* Middlebrook, *supra* note 7 (highlighting the benefits of employer-integrated wage advance models, such as additional financial tools and the presence of an employer, monitoring the wage advance transactions).

98. *See id.* (displaying over 250 complaints against the wage-advance company Earnin).

99. *See id.* ("HAS TRIED TO CONTACT THE COMPANY MULTIPLE TIMES BECAUSE OF CONSTANT OVER DRAFT FEE FOR MULTIPLE WITHDRAWAL FEES. MY SON IS UNABLE TO REMOVE HIS BANK ACCOUNT INFORMATION FROM THIS APP. HELP.").

100. *See id.* (describing consumer inability to reach Earnin for overdraft fee reimbursement).

101. Farivar, *supra* note 2.

102. *See* Corkery, *supra* note 71 (discussing the benefits of employer-integrated applications, such as financial management support).

103. Farivar, *supra* note 2.

104. *Id.*

105. *Id.*

106. *See* Turner v. E-Z Check Cashing of Cookeville, TN, Inc. (Turner v. E-Z Check), 35 F. Supp. 2d

Wage-advance businesses argue they are not "creditors" under the definition provided by the Truth in Lending Act ("TILA") and therefore are outside the obligations imposed by the Act.[107] TILA defines "creditor" as:

A person who both (1) regularly extends, whether in connection with loans . . . or otherwise, consumer credit which . . . payment of a finance charge is or may be required, and (2) is the person to whom the debt arising from the consumer credit transaction is initially payable on the face of the evidence of indebtedness or, if there is no such evidence of indebtedness, by agreement.[108]

TILA also defines "credit" as "the right granted by a creditor to a debtor to defer payment of debt or to incur debt and defer its payment."[109]

The courts have attempted to define the limits of these TILA terms for years.[110] In *Turner v. E-Z Check Cashing of Cookeville, TN, Inc.*, a check-cashing business allowed customers to write checks for the amount borrowed, plus a service fee in exchange for an extension of a cash advance, payable within thirty days.[111] If the customer failed to repay the amount of the check within thirty days or, alternatively, pay an additional service fee for E-Z to defer depositing the check, the business would cash the check in the full amount.[112] The court held that E-Z's practices constituted extensions of credit, as "[t]hey are disbursing funds to people . . . on the promise of repayment of the sum plus the 'service charge,' at a later time."[113] The court continued by stating, [i]f this is not an extension of credit, this Court finds it hard to imagine any transaction that is."[114] The court added that Congress designed TILA to protect consumers from deceptive lending practices; therefore, all courts should construe TILA broadly in favor of consumer protection.[115]

Similarly, wage-advance businesses disburse funds to consumers with the expectation of later payment.[116] While wage-advance businesses requiring mandatory service fees alongside their extension of credit appear to clearly fall under TILA regulations, businesses with "noncompulsory tips" argue they do not deserve the epithet "creditor."[117] Despite the discretionary nature of these

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1042, 1048 (M.D. Tenn. 1999) (reasoning a check-cashing business extended "credit" for purposes of the Truth in Lending Act).

107. 15 U.S.C. § 1602(g) (2020); Middlebrook, *supra* note 7.

108. 15 U.S.C. § 1602(g).

109. 15 U.S.C. § 1602(f) (2020).

110. *See* Turner v. E-Z Check, 35 F. Supp. 2d at 1047 (attempting to define the terms "creditor" and "credit" under TILA in connection to a check-cashing, deferred presentment transaction).

111. Turner v. E-Z Check, 35 F. Supp. 2d at 1046.

112. *Id.*

113. *Id.* at 1048.

114. *Id.*

115. *Id.* at 1047.

116. Middlebrook, *supra* note 7.

117. *See id.* (discussing the difference between employer-integrated wage-advance businesses and non-employer-integrated wage advance businesses, as well as the business models of wage-advance businesses that offer services for a service fee or noncompulsory tip).

charges, courts should hold these companies accountable as creditors due to the coercive nature of the tipping schemes and the company's ability to modify the amount lent by the amount the consumer tips.[118] Additionally, for a court to deem a business a "creditor" under TILA, payment of a finance charge (i.e., a service charge) is not a requisite condition.[119]

Wage-advance businesses also argue that, unlike deferred presentment check-cashing businesses such as E-Z, they do not threaten legal action if customers are unable to pay.[120] However, threatened legal action was not dispositive in the *Turner* court's conclusion that E-Z was a "creditor" under TILA.[121] Therefore, the lack of legal repercussions by wage-advance businesses, as well as the court's presumption in favor of consumer protection, arguably tip the scales in favor of holding noncompulsory tip-based wage-advance businesses to be "creditors."[122]

III. History of Payday Lending Regulations

Because wage-advance businesses are creditors and subject to the same requirements as those of the payday lending industry, state and federal governments must determine the best course of action in regulating them.[123] Historically, the payday lending industry has enjoyed extensive latitude in operating independent of banking laws.[124] Section A discusses traditional usury laws—both state and federal.[125] Section B analyzes state usury laws' continued inability to regulate the payday lending industry due to federal preemption.[126] Section C introduces the underlying public policy reasons that explain the legislative and judicial hesitance to regulate the industry.[127] Lastly, Section D

118. *See* Farivar, *supra* note 2 (discussing the internal analytics of Earnin, showing that most consumers tip regardless of their noncompulsory nature and that the amount the wage-advance business is willing to lend depends on how much a consumer tips).

119. *See* 15 U.S.C. § 1602(g) (defining "'Creditor' as 'a person who both (1) regularly extends, whether in connection with loans . . . or otherwise, consumer credit which . . . payment of a finance charge is or *may* be required . . .'") (emphasis added).

120. Farivar, *supra* note 2.

121. *See* Turner v. E-Z Check, 35 F. Supp. 2d at 1048 (concluding that the check-cashing business's model of charging a service fee alongside the advancement of cash was significant in finding that the business engaged in actions akin to that of a "creditor" extending "credit" to consumers).

122. *See id.* (concluding that the check-cashing business's model of charging a service fee alongside the advancement of cash was significant in finding that the business engaged in actions akin to that of a "creditor" extending "credit" to consumers).

123. *See* Kirby M. Smith, Comment, *Banking on Preemption: Allowing National Bank Act Preemption for Third-Party Sales*, 83 U. OF CHI. L. REV. 1631, 1634 (on file with the *University of the Pacific Law Review*) (discussing the history of the creation of the NBA and OCC and their impact on the autonomy enjoyed by the lending industry).

124. *See id.* (discussing the history of the creation of the NBA and OCC and their impact on the autonomy enjoyed by the lending industry).

125. *Infra* Section III.A.

126. *Infra* Section III.B.

127. *Infra* Section III.C.

argues that the regulation of usury laws, both state and federal, is only the beginning in regard to the types of payday lending activities that governments should regulate.[128]

A. Traditional Usury Laws

Usury laws limit the amount of interest a lender may charge on a loan.[129] While states often implement usury laws, federal statutory provisions authorize national banks to charge the maximum loan rate of the state in which the bank certified its organization.[130] Such provisions incentivize interstate banks to strategically locate their branches in states with the highest permissible loan rates, virtually deregulating interest rates and preempting state laws.[131]

Payday lenders take advantage of such federal preemption provisions.[132] Before selling the rights of a loan to payday lenders, out-of-state banks offer payday loans to borrowers at the maximum rate of the state in which they are certified.[133] Consequently, payday lenders who acquire the loan but reside in more restrictive usury law states take advantage of other states' maximum rates.[134] This scheme, called "charter-renting," allows payday lenders to circumvent their own state's regulations for the more favorable usury laws of the out-of-state bank.[135] While most banking regulators have prohibited charter-renting, the Federal Deposit Insurance Corporation continues to allow the practice.[136]

Charter-renting and other payday lending practices that take advantage of procedural loopholes raise a significant question regarding the US financial regulatory framework: why have the federal and state governments not been able to curb the conduct of the payday lending industry?[137]

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128. *Infra* Section III.D.

129. MICHAEL P. MALLOY, PRINCIPLES OF BANK REGULATION 187 (West Group, 2d ed. 2003).

130. *See* 12 U.S.C. § 85 (202) ("Any association may take, receive, reserve, and charge on any loan or discount made, or upon any notes, bills of exchange, or other evidences of debt, interest at the rate allowed by the laws of the State, Territory, or District where the bank is located, or at a rate of 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal reserve bank in the Federal reserve district where the bank is located, whichever may be the greater, and no more, except that where by the laws of any State a different rate is limited for banks organized under State laws, the rate so limited shall be allowed for associations organized or existing in any such State under title 62 of the Revised Statutes."); MALLOY, *supra* note 129 at 187.

131. Mann & Hawkins, *supra* note 43, at 871-872.

132. *Id.*

133. *Id.*

134. *Id.*

135. *Id.*

136. *Id.*

137. *See* Smith, *supra* note 123, at 1634 (discussing the history of the creation of the NBA and OCC and their impact on the lending industry).

B. Historical Context & Federal Preemption

The first issue regarding the lack of payday lending regulations is rooted in history.[138] In 1864, Congress enacted the National Bank Act ("NBA") in an effort to create a national banking system separate from the states.[139] Through the NBA, Congress chartered the Office of the Comptroller of Currency ("OCC") to oversee, regulate, and protect national banks against state interference.[140] Congress hoped the NBA would initiate the ultimate demise of state banking systems and the conversion to one federally-regulated banking system.[141] Despite such hopes, federal banking unity has yet to occur, and the NBA and Supreme Court interpretations of the NBA have had more damning than beneficial impacts on the ability to regulate payday lenders effectively.[142]

In *Tiffany v. National Bank of Missouri*, the Supreme Court held that national banks were not subject to the interest rates of a state, so long as the bank's rates were within the limits of the state in which the bank was certified.[143] The Court famously asserted that national banks were "national favorites" and must therefore be protected from "unfriendly legislation by the States."[144] The ruling significantly established the binding federal common law that the NBA preempts state usury laws.[145]

More recently, the Supreme Court extended the federal preemption doctrine to national bank subsidiaries in *Watters v. Wachovia Bank, NA*.[146] In 2006, a federally-chartered bank and its subsidiary sued the Commissioner of the Michigan Office of Insurance and Financial Services ("OFIS") on the grounds that the NBA and OCC regulations preempted Michigan's state laws concerning the national bank's subsidiary—a previously state-chartered mortgage company.[147] While Michigan law exempted state and federal banks from state mortgage lending laws, all subsidiaries had to subject themselves to state supervision and registration with the state's OFIS.[148] While the mortgage

138. *See id.* (discussing the history of the creation of the NBA and OCC and their impact on the lending industry).

139. *Id.* at 1633; *see also* Tiffany v. Nat'l Bank of Mo., 85 U.S. 409 (1874) (calling national banks "[n]ational favorites").

140. Smith, *supra* note 123, at 1634.

141. *See id.* (explaining that, despite expectations, most state banks did not convert to national banks after the NBA's passage).

142. *Id.* at 1638.

143. Tiffany, 85 U.S. at 411.

144. *Id.* at 412–13.

145. Smith, *supra* note 123, at 1636; *See* Tiffany, 85 U.S. at 412 (discussing the congressional intent behind the enactment of the NBA).

146. *See* Watters v. Wachovia Bank, N.A., 127 U.S. 1559, 1561 (2007) (holding that federal preemption and the application of OCC regulations applies the same to nationally-chartered banks as it does to their subsidiaries).

147. *Id.*

148. *Id.*

company—Wachovia Mortgage—had previously registered with Michigan, it surrendered its OFIS registration after it became a wholly owned subsidiary of the federally-chartered Wachovia Bank.[149] In response, the OFIS notified Wachovia Mortgage that it could no longer perform mortgage services in Michigan without reobtaining registration.[150]

The Supreme Court reiterated Congress' intent in enacting the NBA when ruling that the national bank and its subsidiary were exempt from state mortgage laws that overlap with OCC regulations.[151] The Court reasoned that Congress created the NBA and the OCC to protect against "unduly burdensome and duplicative state regulation."[152] Therefore, the power to examine and inspect national banks *and their subsidiaries*—an enumerated power of the OCC—rests not in the states' hands, but in the OCC.[153] The *Watters* ruling extended the national bank favoritism articulated in *Tiffany* to its subsidiaries and created a loophole for payday lenders and other charter-renting entities to take advantage of less stringent usury laws.[154]

Interestingly, the Supreme Court heard the *Watters* case one year before the U.S. market crash of 2008.[155] After the crash, the Supreme Court once again addressed the issue in *Cuomo v. The Clearing House Association, L.L.C.*[156] In *Cuomo*, the Supreme Court took a step back from its well-documented generosity towards OCC-chartered banks, holding that the OCC's interpretation of visitorial rights—powers ironically granted to the OCC by the *Watters* Court—were unreasonable.[157] The Court narrowed the interpretation of *Watters*, arguing that it had granted the OCC "general supervision and control" over a subsidiary of a national bank, not the exclusive right to enforce laws against national banks altogether.[158] Therefore, the State Attorney General may bring enforcement actions against nationally-chartered banks to enforce state laws still applicable to the national banks.[159] While *Cuomo* limited national banks' power and reverted some power back to the states regarding enforcement action, *Watters* remains good law and became the stepping stone for payday lenders to avoid state laws and utilize the benefits of charter-renting.[160]

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149. *Id.*

150. *Id.*

151. *See id.* at 1566 (asserting that Congress created the NBA "[t]o prevent inconsistent or intrusive state regulations from impairing the national system.").

152. *Id.* at 1567.

153. 12 U.S.C. § 484(a) (2020); Watters, 127 U.S. at 1568.

154. *See* Watters, 127 U.S. at 1561 (discussing the intent of Congress to allow national banks larger leeway and protection against state banks).

155. *See id.* at 1559 (hearing the case in 2007).

156. Cuomo v. Clearing House Ass'n, 129 U.S. 2710, 2710–18 (2009).

157. *Id.* at 2719.

158. *Id.* at 2717.

159. *Id.* at 2717–18.

160. *Compare* Watters, 127 U.S. at 1562 (ruling in favor of national banks and their subsidiaries), *with* Cuomo, 129 U.S. at 2717–18 (ruling against national banks and ultimately limiting the OCC's power regarding

Chartering a national bank is relatively simple.[161] During the application period, the OCC reviews only the bank's "business plan, management experience, and financial resources."[162] Due to such accessibility and the holding in *Watters*, payday lenders take advantage of national banks by operating as their subsidiaries, subsequently benefitting from the higher interest rates of the states in which the national bank is certified.[163] This allows payday lenders to operate in states with stricter usury laws without subjecting themselves to such laws.[164]

The recent Second Circuit opinion in *Madden v. Midland Funding, LLC*, however, brought more uncertainty to the payday lending scheme of charter-renting.[165] After nationally chartered Bank of America sold the rights of Saliha Madden's account to Midland Funding, a debt collector, Midland sued Madden to collect on the unpaid balance of the credit.[166] Madden, however, contended that the interest rate charged by Bank of America could not be transferred to or collected by Midland due to New York usury laws, where the debt collectors were located.[167] Essentially, Madden argued that Midland was neither a national bank nor a subsidiary of a national bank and, therefore, could not claim exemption from state usury laws.[168]

In ruling that federal preemption does not carry over to assignees of a national bank, the court highlighted the lack of interest retained by the previous owner—the national bank.[169] While only persuasive in most jurisdictions, the Second Circuit's holding in *Madden* has disconcerted the payday lending industry.[170] Unless subsidiaries to a national bank, payday lenders in the business of charter-renting may no longer be able to claim federal preemption.[171]

C. Public Policy

Another issue impeding enforcement against the payday and wage-advance industry is the desire, or lack thereof, for public officials to do so.[172] As discussed

visitorial powers).

161. Smith, *supra* note 123, at 1638.

162. *Id.*

163. Mann & Hawkins, *supra* note 43, at 871–72.

164. *Id.*

165. Madden v. Midland Funding, LLC, 786 F.3d 246, 251–52 (2d Cir. 2015).

166. *Id.* at 247–48.

167. *Id.*

168. *Id.* at 247–49.

169. *Id.* at 252 & n.2; Smith, *supra* note 123, at 1654.

170. *See* Madden, 786 F.3d at 249 (holding that assignees must abide by the usury laws of the state in which they are located and do not reserve the federal preemption afforded the national bank which sold the rights of the loan).

171. *See id.* (holding that assignees must abide by the usury laws of the state in which they are located and do not reserve the federal preemption afforded the national bank which sold the rights of the loan).

172. *See* Atkinson, *supra* note 51, at 1105 (discussing the various policy considerations of payday lending regulation).

above, much debate remains over whether such regulations are harmful or advantageous to the overall welfare of society.[173] The contention is discernable from the ongoing debate over the CFPB 2017 Rules.[174]

In 2017, the CFPB issued a proposed rule that strived to regulate the payday lending industry.[175] The payday lending rule originally included a prospective "ability-to-repay" provision, requiring payday lenders to evaluate borrowers' ability to repay before entrusting them with a loan.[176] The provision would restrict unqualified borrowers from taking out payday loans, thereby preventing possible defaults and patterns of insolvency.[177] Opponents of the "ability-to-repay" provision, including the payday lending industry itself, argue it will restrict the market so severely as to kill the industry entirely.[178]

In January of 2019, the CFPB repealed the "ability-to-repay" provision after its new director, Kathy Kraninger, stated the rule would harm consumers most dependent on the industry's loans.[179] The CFPB also looks to review the viability of a similar proposed provision that limits a consumer's ability to reborrow consistently.[180] Originally projected to take effect in 2017, the CFPB has postponed the payday lending rules' enactment until November 2020 to engage in further review.[181] Due to the delay, the federal government has yet to implement a cohesive set of rules that would effectively regulate payday lending behavior at a national level.[182] The CFPB 2017 Rules underscore the lack of consensus among federal administrations over the proper balance between payday lending regulations and autonomy.[183]

D. High Interest Rates: Tip of the Iceberg

While state legislators often advocate for stronger usury laws, the ability of

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173. *See id.* (discussing the various policy considerations of payday lending regulation).

174. Ward, *supra* note 67 (outlining the continuous debate regarding the CFPB 2017 Rules).

175. *Id.*

176. *Id.*

177. *Id.*

178. *Id.*

179. *Id.*

180. Kate Berry, *CFPB to Scrap Key Underwriting Portion of Payday Rule*, AMERICAN BANKER (Jan. 14, 2019, 12:38 PM), https://www.americanbanker.com/news/cfpb-to-scrap-key-underwriting-portion-of-payday-rule (on file with the *University of the Pacific Law Review*).

181. *Payday, Vehicle Title, and Certain High-Cost Installment Loans; Delay of Compliance Date; Correcting Amendments*, Consumer Fin. Protection Bureau, https://www.consumerfinance.gov/policy-compliance/rulemaking/final-rules/payday-vehicle-title-and-certain-high-cost-installment-loans-delay-compliance-date-correcting-amendments/ (last visited July 3, 2020) (on file with the *University of the Pacific Law Review*).

182. *See* Ward, *supra* note 67 ("Consumer advocates are worried that the CFPB's proposal to strike the ability-to-repay requirement is a sign that the agency is backing away from its mission of protecting Americans from unfair financial practices and regulating financial products like student loans and payday loans.").

183. *Id.* (outlining the continuous debate regarding the CFPB 2017 Rules).

payday lenders to federally charter-rent makes such usury laws a nullity.[184] Furthermore, the regulation of high interest rates among payday lenders merely scratches the surface regarding the regulatable practices of payday lenders.[185] Legislators must refocus their attention from the distracting shimmer of usury charges to the various other issues littering the payday lending market, such as deceptive business practices.[186]

In 1914, President Woodrow Wilson signed the Federal Trade Commission Act into law, effectively creating the FTC.[187] Designed to protect consumer interests and promote economic competition, Congress gave the FTC the power to prohibit unfair or deceptive practices in commerce.[188] Utilizing this power, the FTC has recently cracked down on the deceptive business practices of the payday lending industry.[189]

In *FTC v. AMG Capital Management*, the FTC sued the payday lending entity AMG Capital ("AMG") for inaccurately disclosing the terms of its loans.[190] The Ninth Circuit held that the Loan Note would not put a reasonable consumer on notice of the total payment due to its misleading nature.[191] The Ninth Circuit also affirmed the $1.27 billion in equitable monetary relief for victims of AMG's payday lending scheme.[192] The Ninth Circuit's holding marks one of the largest settlements against the payday lending industry and displays an increasing determination by the FTC to control the once rogue industry.[193]

IV. Future Regulation

Despite the state and federal governments' previous inability to effectively regulate the payday lending industry, recent developments—such as the

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184. *See generally* Watters, 127 U.S. at 1562 (holding that federal preemption applies to subsidiaries of national banks).

185. *See generally* AMG Capital Mgmt., LLC, 910 F.3d at 423 (holding a payday lending company liable for deceptive business practices in violation of the Federal Trade Commission Act).

186. *See generally id.* (holding a payday lending company liable for deceptive business practices in violation of the Federal Trade Commission Act).

187. Federal Trade Commission Act § 5, 15 U.S.C. § 45(a)(1), (2) (2020); *Our History*, FTC, https://www.ftc.gov/about-ftc/our-history (last visited June 26, 2020) (on file with the *University of the Pacific Law Review*).

188. 15 U.S.C. § 45(a)(1).

189. AMG Capital Mgmt., LLC, 910 F.3d at 423 (holding payday lending company, AMG Capital Management, liable for the deceptive business practice of misleading customers via the Loan Note).

190. *Id.* at 422.

191. *Id.* at 423.

192. *Id.* at 428.

193. *See generally id.* (upholding the $1.27 billion judgement against AMG Capital); *U.S. Court Finds in FTC's Favor and Imposes Record $1.3 Billion Judgment Against Defendants Behind AMG Payday Lending Scheme*, FTC, https://www.ftc.gov/news-events/press-releases/2016/10/us-court-finds-ftcs-favor-imposes-record-13-billion-judgment#:~:text=U.S.%20Court%20Finds%20in%20FTC's,Lending%20Scheme%20%7C%20Federal%20Trade%20Commission (Oct. 4, 2016) (on file with the *University of the Pacific Law Review*).

monetary award granted in *FTC v. AMG Management Capital* and the holding in *Madden v. Midland Funding LLC*—give hope that regulation is possible.[194] To effectively regulate payday and wage-advance lenders in the future, the federal government must continue to pursue litigation akin to *FTC v. AMG* in an effort to curb deceptive business practices beyond merely the unconscionability of high usury charges.[195] The ability of the FTC to target all forms of practices the FTCA deems "deceptive" gives the agency a unique position to police *all* lending activity without the bureaucratic obstacles associated with legislation.[196]

State governments should also implement their own regulatory schemes to curb the payday lending and wage-advance industries.[197] One suggestion is to criminalize the business of payday lenders within the state.[198] Through the use of their police powers, states can overcome the federal preemption issues associated with state usury laws by deeming the very practice of payday lending illegal.[199] In essence, state laws attempting to limit payday loan interest rates and practices would be replaced with the criminalization of the industry altogether.[200]

Some states already utilize this tactic.[201] New York and New Jersey have outlawed payday lenders from conducting business in their states.[202] Georgia, on the other hand, prohibits payday lenders from operating through the use of racketeering laws.[203] North Carolina—ironically one of the first states to authorize payday lending—reached an agreement to temporarily halt payday lending within the state in 2006.[204]

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194. *See generally* AMG Capital Mgmt., LLC, 910 F.3d at 423 (holding, notably, a payday lending company liable for their deceptive business practices regarding a Loan Note); Madden, 786 F.3d at 249 (holding assignees of a loan accountable to the usury laws in which they are located).

195. *See generally* AMG Capital Mgmt., LLC, 910 F.3d at 423 (regulating a payday lending company for deceptive business practices); Madden v. Midland Funding, LLC, 786 F.3d 246, 249 (2d Cir. 2015) (declaring the assignees of a loan subject to the usury laws of the place in which assignees were located).

196. *See* Madden, 786 F.3d at 249 (holding assignees of a loan accountable to the usury laws in their respective states of business).

197. *See* AMG Capital Mgmt., LLC, 910 F.3d at 423 (upholding the $1.27 billion judgement against AMG Capital by arguing that the business was engaging in deceptive/fraudulent business practices).

198. *PayDay Loan Consumer Information*, *supra* note 22 (discussing New York's and New Jersey's criminal usury statutes outlawing payday loans over 35% APR).

199. *See, e.g.*, N.Y. Penal Law § 190.40 (McKinney 2020) (setting a usury cap at 25% interest, virtually outlawing short-term, high-fee loans).

200. *Compare* Watters, 127 U.S. at 1566 (allowing national banks massive leeway and protection against state bank usury laws), *with* § 190.40 (setting a usury cap at 25% interest, virtually outlawing short-term, high-fee loans), *and* N.J. Stat. Ann. § 2C:21-19 (West, 2020) (setting a usury cap at 30% interest, also outlawing short-term, high-fee loans in New Jersey).

201. *See PayDay Loan Consumer Information*, *supra* note 22 (outlining the New York and New Jersey usury statutes criminalizing the activity of payday lending).

202. § 190.40; § 2C: 21-19.

203. *See* Ga. Code Ann. §§ 16-17-1 et seq. (2020); *see* Shobhit Seth, *Racketeering*, INVESTOPEDIA (Apr. 10, 2020), https://www.investopedia.com/terms/r/racketeering.asp (on file with the *University of the Pacific Law Review*) ("Racketeering may refer to the act of acquiring a business operation through illegal activity, operating a business with illegally-derived income, or using a business operation to commit illegal acts.").

204. Uriah King, et al., *Financial Quicksand: Payday Lending Sinks Borrowers into Debt with $4.2 Billion in Predatory Fees Every Year*, CENTER FOR RESPONSIBLE LENDING 5 (Nov. 30, 2006),

Arguments against criminalization of payday lending mirror arguments against regulation of the industry.[205] Outlawing payday lending will potentially prevent informed consumers from accessing essential cash and force them to seek alternative avenues.[206] After Ohio virtually banned payday loans in 2008, residents in need of cash turned to pawn shops for emergency credit.[207] Pawn shops, which operate through the exchange of valuable items for credit, saw a 97% increase in use after the payday lending ban.[208] Such data reaffirms a conclusion that payday lending might actually fill an essential gap in the financial market.[209] However, the Center For Responsible Lending projected that citizens in North Carolina and Pennsylvania—two states that have banned payday lending—would save a total of $1.4 billion in predatory payday fees due to the restrictions.[210]

Federal circuits should also follow the Second Circuit's lead, adopting the holding of *Madden v. Midland Funding LLC*.[211] Adoption of *Madden* would create a cohesive expectation that federal courts no longer tolerate payday lenders' practice of charter-renting.[212]

Payday lenders—and now wage advance businesses—will no longer be able to utilize federal preemption as a loophole to charge higher usury rates than the state in which they are located.[213] The extension of the *Madden* ruling will also allow state usury laws to reacquire purpose by forcing payday and wage-advance lenders located in the state to follow its regulations.[214]

Alongside judicial opinions limiting the once unchecked power of national banks and their subsidiaries, the CFPB should reinstate the CFPB 2017 Rules in their original form.[215] The rules should include an ability-to-repay provision to assess the borrower's capacity to repay the loan and to avoid the possibility of

https://responsiblelending.org/payday-lending/research-analysis/rr012-Financial_Quicksand-1106.pdf (on file with the *University of the Pacific Law Review*).

205. *See* Minnich, *supra* note 61, at 88 (discussing the benefits of consumer choice, as well as the need for payday loans to fill an essential gap in the market).

206. *See* Atkinson, *supra* note 51, at 1105 (outlining and refuting the argument that payday loans fill an essential gap in the market).

207. Natasha Forst, *Banning Payday Loans Sends Desperate Borrowers Running to Pawn Shops*, QUARTZ (Mar. 1, 2019), https://qz.com/1561643/ohios-ban-on-payday-loans-sent-people-running-to-pawn-shops/ (on file with the *University of the Pacific Law Review*) (discussing Ohio's Short-Term Loan Law that limited APR to 28%, effectively outlawing payday lenders within the state).

208. *Id.*

209. *See id.* (outlining the argument that consumers across the nation rely on payday lending as an essential service).

210. King, *supra* note 204.

211. *See* Madden, 786 F.3d at 249 (holding assignees of a loan accountable to the usury laws in their respective states of business).

212. *See id.* (holding a debt collector's practice of charter-renting from the national bank who assigned the loan was invalid).

213. *See id.* (restricting assignees of national banks' ability to utilize federal preemption as a means to skirt state laws).

214. *See id.* (subjecting assignees of national banks to the laws of the state in which they are located).

215. *See* Ward, *supra* note 67 (outlining the ability-to-repay provision and its benefit to consumers).

cyclical insolvency.[216]

V. CONCLUSION

The payday lending industry has gone virtually unregulated since its inception in the early 1990s.[217] And with the wage-advance industry emerging, federal and state consumer-protection regulations are more crucial than ever.[218] While the wage-advance industry refuses to concede they are payday lenders, the reality remains that the two are indistinguishable markets and should be regulated accordingly.[219] However, regulation is easier said than done.[220] The government's historical inability—or refusal—to regulate the payday lending industry has presented problems that have just recently begun to resolve.[221] The FTC's and federal courts' willingness to hold lenders accountable and give effect to state usury laws is a recent development in U.S. history.[222] Federal and state governments' continued insistence on holding the industry accountable—through litigation, federal payday lending rules, and state criminalization of the industry—is necessary to protect consumers and financial institutions.[223] Despite wage-advance businesses' claims of ease and expedience in using their applications, the unresolved and deep-seated issues surrounding the lending industry, indeed, make wage-advance app too good to be true.[224]

216. *See id.* (discussing the proposed changes to the original CFPB 2017 Rules).

217. Smith, *supra* note 123, at 1633.

218. *See* Farivar, *supra* note 2 (highlighting the need for wage-advance businesses that are currently skirting federal and state usury and consumer protection laws to be regulated).

219. *Id.*; *see* Turner v. E-Z Check, 35 F. Supp. 2d at 1048 (reasoning a check-cashing business extended "credit" for purposes of the Truth in Lending Act).

220. Smith, *supra* note 123, at 1634.

221. *See id.* (discussing the historical deference given to national banks over state banks).

222. *See* AMG Capital Mgmt., LLC, 910 F.3d at 423 (holding, in 2018, a payday lending company liable for their deceptive business practices regarding a Loan Note); Madden, 786 F.3d at 249 (holding, in 2015, assignees of a loan accountable to the usury laws in their respective states of business).

223. AMG Capital Mgmt., LLC, 910 F.3d at 423 (advocating for better consumer transparency between payday lenders and its customers when laying out the terms and conditions of the loan); Madden, 786 F.3d at 247-48 (protecting consumers against debt collectors attempting to skirt state usuary laws and take advantage of more favorable federal laws).

holding assignees of a loan accountable to the usury laws in their respective states of business).

224. Farivar, *supra* note 2 (highlighting the similar problems associated with the traditional payday lending industry and the new wage advance industry, as well as the wage advance industry's current lack of regulation by either usury or payday lending laws).

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